Republic of South Africa Public Expenditure and Financial Accountability

Public Financial Management Performance Assessment Report

Final Report

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ECORYS Nederland BV

Ronald E. Quist
Corina Certan
Jerome Dendura

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ECORYS

ECORYS

ECORYS Nederland BV
P.O. Box 4175
3006 AD Rotterdam
Watermanweg 44
3067 GG Rotterdam
The Netherlands

T +31 (0)10 453 88 00
F +31 (0)10 453 07 68
E netherlands@ecorys.com
W www.ecorys.com
Registration no. 24316726

ECORYS Macro & Sector Policies
T +31 (0)10 453 87 53
F +31 (0)10 452 36 60

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The information contained in this report does not necessarily reflect the position or opinion of the National Treasury or of the European Commission. Responsibility for the views expressed and for any errors of fact or judgement remains with the consultants who are accountable for providing an accurate assessment of events, opinions and comments. The PEFA Assessment exercise and the consultants aim to be as factual as possible.

Please send any comments or questions to:
Ronald E. Quist: quistron@gmail.com
Corina Certan: corina.certan@ecorys.com
Jerome Dendura: jdendura@gmail.com

Currency and Exchange Rates	*Fiscal Year*	*PEFA Assessment Period*
Currency Unit - Rand (R)	FY 2005/2006	April 1st to March 31st
Euro 1 = R 11.95	FY 2006/2007	
US$ 1 = R 7.66	FY 2007/2008	

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Abbreviations and Acronyms

AccG	Accountant General
ADR	Alternative Dispute Resolution
AG	Auditor-General
AGA	Autonomous Government Agencies
ALM	Assets and Liability Management (Division)
AO	Accounting Officer
ASB	Accounting Standards Board
ASGISA	Accelerated and Shared Growth Initiative for South Africa
BAS	Basic Accounting System
BBEEA	Broad based Black Economic Empowerment Act
BC	Budget Council
BIU	Business Intelligence Unit
BO	Budge Office
BS	Budget Support
CFI	Consolidated Financial Information
COFOG	Classifications of Functions of Government
CPI	Consumer Price Index
CSDRMS	Commonwealth Secretariat Debt Recording and Management System
DDG	Deputy Director General
DG	Director General
DORA	Division of Revenue Act
DORB	Division of Revenue Bill
EC	European Commission
ENE	Estimates of National Expenditure
EP	Economic Policy (Division)
FDI	Foreign Direct Investment
FMIP	Financial management Improvement Programme
FY	Fiscal Year
GDP	Gross Domestic Product
GFS	Government Financial Statistics
GNI	Gross National Income
GRAP	Generally Recognised Accounting Practice
HDI	Human Development Index
IA	Internal Audit
ICT	Information & Communication Technology
ID	Identification Document
IDASA	Institute for Democracy in South Africa
IDC	International Development Co-operation
IFMS	Integrated Financial Management System
IGR	Intergovernmental Relations (Division)
IIA	Institute of Internal Audit

IMF	International Monetary Fund
INTOSAI	International Organisation of Supreme Audit Institutions
ISA	International Standards on Auditing
JBC	Joint Budget Committee
LG	Local Government
MCB	Ministers Committee on Budget
MEC	Member of the Executive Council
MFMA	Municipal Finance Management Act
MF	Minister of Finance
MTBPS	Medium Term Budget Policy Statement
MTEC	Medium Term Expenditure Committee
MTEF	Medium Term Expenditure Framework
NA	National Assembly
NDM	National Department Minister
NCOP	National Council of Provinces
NRF	National Revenue Fund
NT	National Treasury
ODA	Official Development Assistance
OMA	Offices, Ministries, Agencies
PAA	Public Audit Act
PAIA	Promotion of Access to Information Act
PCF	Portfolio Committee on Finance
PE	Public Enterprise
PEFA	Public Expenditure and Financial Accountability
PETS	Public Expenditure Tracking Survey
PF	Public Finance (Division)
PFM	Public Finance Management
PFMA	Public Finance Management Act
PFM PMF	Public Finance Management Performance Management Framework
PI	Performance Indicator
PPP	Public Private Partnership
PU	Procurement Unit
R	Rand, South African currency
RDP	Reconstruction and Development Programme (Fund)
SA	South Africa
SACCI	South African Chamber of Commerce Institute
SACU	Southern African Customs Union
SADC	Southern African Development Community
SARB	South African Reserve Bank
SARS	South African Revenue Service
SBS	Sector Budget Support
SCM	Supply Chain Management
SCOPA	Standing Committee on Public Accounts
SEIFSA	Steel and Engineering Industries Federation of South Africa
SITA	State Information and Technology Agency
SNG	Sub National Government
SOE	State Owned Enterprise
TOR	Terms of Reference
TSA	Treasury Single Account
VAT	Value Added Tax

Summary Assessment

This Public Expenditure and Financial Accountability (PEFA) assessment was initiated and sponsored by the European Commission. It has been undertaken with the formal agreement and active support of the Government of South Africa. The assessment adopts the widely accepted methodology of the Public Financial Management Performance Measurement Framework (PFM-PMF) issued by the PEFA multi-donor programme in June 2005. The approach is based upon a careful consideration of the demonstrated observable public financial management (PFM) systems, procedures and practices in South Africa at the time of the assessment as determined through direct interviews with Government officials and the reviews of official documents and reports. It is also based upon the use of corroborating evidence sought from a variety of independent sources where ever possible.

The purpose of the PFM Performance Report is to assess the current status of the public financial management system of the central government. It should serve to identify both areas of strength and weakness. It is important to note that for South Africa the assessment's restriction to the coverage of the central government PFM systems means that it provides a snap shot on the PFM systems, procedures and practices of only about a third of the Public Sector PFM activity. Beyond this restriction to a relatively small proportion of Public Sector PFM systems, procedures and practices assessed here, it should be further pointed out that given the concurrent roles of the national versus provincial governments there is only a limited opportunity presented to assess technical and allocative efficiency. Given the national government's role to be principally policy, regulation, oversight, revenue administration, debt and cash management, budget release management, and monitoring and evaluation, this review provides limited opportunity to assess the efficiency of expenditure management or the effectiveness of the application of expenditure even where funds may have been allocated at an aggregate level to areas of strategic priority; these latter functions being principally the role of the provincial governments.

This assessment is not designed to comment upon any aspects of specific fiscal or expenditure policy and has been careful not to do so. It has not taken into account considerations of capacity, except to the degree implicit in the capacity to successfully carry out the assessed PFM procedures. It is important also to underscore that the objective of the assessment has not been to evaluate and score the performance of institutions or any PFM offices or officials, but rather to assess the capacity of the PFM systems themselves to support sound fiscal policy and financial management[1].

The PEFA performance review for South Africa presents an assessment of the 31 high-level indicators of the PEFA Performance Measurement Framework. It is anticipated that the PEFA assessment shall support the on-going dialogue between the government and its development partners on aid delivery modalities and arrangements for support to PFM reform in South Africa[2]. While this report, by design, neither articulates specific recommendations for PFM improvements nor details an action plan, it is anticipated that the results, which establish areas of both strength and weakness, shall assist the government in further defining its PFM reform priorities and subsequent reform activity sequencing and pacing schedule. Further, it should serve separately as a useful tool to donors for supporting dialogue in providing harmonised donor support to the Government's PFM reform efforts.

Integrated Assessment of PFM Performance

In the following sections of the summary the performance of PFM systems, procedures and practices as measured through the PEFA assessment are described in terms of six critical dimensions of PFM as defined within the PEFA methodology. These are credibility of the budget; comprehensiveness and transparency; policy based budgeting; predictability and control in budget execution; accounting, recording and reporting; and external scrutiny and oversight. While donor practices were also assessed, these are not treated under a separate section. Rather they are considered as part of the discussion by way of their impact on the country's PFM within each section on the six critical dimensions of PFM.

Credibility of the budget

When considered at the aggregate level, and restricted to an assessment of primary expenditure, South Africa scores very well with respect to the credibility of the budget especially with regards to revenue estimates versus outturns and aggregate original primary expenditure estimates versus outturns. However, when the assessment considers expenditure in greater detail, and looks beyond primary expenditure there are important issues that impact negatively on the credibility of the budget. These include the lack of predictability (both volumes and timeliness) in the disbursement of donor sector budget support, the large proportion of off-budget donor activity, the lack of a consistent definition of budget estimate for donor funds, and the lack of alignment of donor budget estimates and financial reporting with the government's fiscal year. It also includes weaknesses in procurement and expenditure management as is revealed in growing expenditure arrears measured as a proportion of Departmental expenditure rather than the

[1] In essence this assessment provides a measure of whether the main necessary conditions for delivering upon sound PFM practice has been met, rather than providing an insight into all of the sufficient conditions necessary to conclude that sound PFM is being carried out. For example while it assesses whether the PFM systems provide a sound framework for assessing fiscal risk arising from Public Enterprise activity, it makes no comment as to what authorities do or should do in response to the information provided by the fiscal risk assessment. Such responses may be purely political and a comment on such would be beyond the remit or competence of a PEFA assessment.

[2] The National Treasury notified an assembly of donors in one of the PEFA workshops its intent to convene a workshop to discuss with donors how to improve coordination and aid effectiveness using the PEFA findings as a basis.

PEFA prescribed total primary expenditure. These expenditure arrears are a consequence of accelerated expenditure practice close to the end of the fiscal year; as Departments rush to spend their entire allocated resources so as not to lose these funds[3]. In the following sections a detailed assessment of the credibility of the budget is presented.

The careful macro-economic considerations, that reconciles independent economic analysis by the National Treasury and the South African Reserve Bank in the development of a three-year revenue forecast frame, updated annually and refined bi-annually achieves for South Africa the first pre-requisite towards obtaining a credible budget. Revenue outturns match very well the budget projections and thus provide a sound starting point for achieving a credible budget. South Africa adopts a fairly technical approach to revenue forecasting and this even when taking into account cyclical factors has tended to under estimate revenue performance. This, in the period considered, has been partially due to the novel global economic trends especially with respect to the strengthening in commodity prices, which in turn have had a direct and significant impact on corporate tax revenue. Coupled with this have been the positive trends in revenue collection that have arisen as a result of increasing economic activity shifts from the informal sector to the formal sector. These shifts have been in response to both very active tax education programs as well as government policies that have resulted in demonstrable benefits to participation in the taxed economy. The upshot of these factors has been revenue outturns that exceeded budget estimates for all three fiscal years considered. Officials emphasise that this has not been the result of having adopted an intentional conservative posture on revenue forecasts. This assertion would be supported by the rather dramatic decreases in outturn to estimate ratio that is observed over the three years reviewed in accordance to down turns in the global economy that have impacted South Africa.

The well matching revenue and expenditure outturns to budget estimates have their genesis in the adoption of a three-year fiscal framework that not only takes into account careful-macro-economic considerations, but also is realistic about political dynamics and demands. The fully credible revenue forecasting along with a successful debt management strategy that has brought debt/GDP levels to 22.3% has provided the fiscal space to facilitate the specification of a meaningful fiscal framework to serve as an effective and realistic top-down budgetary discipline tool which can expect to meet service delivery demands, while being cognizant of the economic and political dynamics and demands. Indeed the successful fiscal framework has provided the basis for a successful implementation of a three year medium term expenditure framework (MTEF)[4].

The aggregate expenditure out-turns matches the budget estimates very closely and reflects a measure of strict fiscal discipline exercised through a credible three year fiscal

3 With the possibility of committed expenditures being rolled over for payment in the following budget year, Departments have an incentive to commit as much expenditure as possible (properly controlled by commitment ceilings) before the end of the year, even if the remaining time in the fiscal year does not permit the full implementation of the expenditure cycle including payment before the close of the fiscal year. This end of year phenomenon is significant enough for the Steel and Engineering Industries Federation of South Africa (SEIFSA) and South African Chamber of Commerce and Industry (SACCI) members and to identify it as an area of complaint by its members on delayed payments at the close and beginning of the fiscal year.

4 Out of a host of countries that undertook in the mid 1990's to adopt a medium term expenditure framework as part of their PFM efforts, South Africa's MTEF implementation is unique in its level of success.

framework that is effectively applied as an instrument of top-down discipline to the budgetary process (see PI-12), coupled with effective cash and debt management (PI-17), and budget release predictability (see PI-16), as well as excellent salary management (see PI-18). The story however is more mixed with respect to the effectiveness of expenditure controls (see PI-4, PI-19, PI-20); expenditure through a procurement vehicle (goods, works and services) forms a small proportion (approximately 7%) of central government expenditure which is largely taken up by very well managed debt service, transfers and subsidies. Consequently only the most severe of weaknesses in the very small proportion of expenditure managed through procurement would be exposed within the assessment of aggregate figures as is the case for the indicators PI-1 to PI-4. When a more revealing analysis of expenditure arrears accumulation is made against Department expenditure (see narrative to PI-4) the results show that there is not insignificant weakness in the area of expenditure arrears.

For all the years considered in this assessment, actual revenue outturns have exceeded revenue estimates; decreasing from 11% to 1%. It should be noted though, that such revenue excess has not led to significant expenditure over budget either at the aggregate or vote level (see PI-1 and PI-2). The evidence suggests that excess revenue over budget estimate has been channelled principally to debt reduction; which has seen a dramatic decline from 29.7% (2005/2006) of GDP to about 22.3% (2007/2008). In contrast though while the quantum of expenditure arrears as a ratio of total central government expenditure remained small (less than 2% of expenditure) they increased dramatically over the period (see PI-4). This apparently has not been due to top down budgetary management weaknesses, but more specifically an issue of expenditure management weaknesses. The increasing expenditure arrears appear to be impacted by the absence of effective procurement planning that would seem to contribute to the existence of an end of year expenditure spike *(the March Spike)* (see PI-20), and weaknesses in commitment reporting with the subsequent missed opportunities for managing expenditure rates (see PI-24). It should be noted that such expenditure arrears occur in spite of a very effective commitment control system being in place. Expenditure arrears arise as a consequence to rush expenditure at the close of the physical year, leaving a high proportion of outstanding payments anticipated to be addressed in the next fiscal year. There are incentives for deferring expenditure as long as possible, but then committing all funds before the close of the fiscal year. In this way Departments are not penalised for unutilised funds; nor is there much risk of being penalised for expenditure over budget ceilings.

When one considers the variance of expenditure outturn for budgetary votes up and above aggregate expenditure deviation from aggregate budget estimates there is evidence that there is effective budget control. The low variances up and above the expenditure deviation at the aggregate level suggest a strong coupling between the budget formulation and preparation process, and in turn between budget estimate and implementation. It demonstrates that the budget releases are very closely aligned with the vote and that the commitment control procedures are largely effective. While the PFM Act accommodates for a supplementary budget process which is implemented in October each year through an Adjustment Budget process, this does not appear to introduce significant adjustments to the original budget estimates.

The PFM systems deliver predictable and well controlled virement procedures with well documented and suitably controlled procedures for in-year adjustments to budget allocations above the level of management of Departments through a well controlled use of adjustment budgets with full and effective parliamentary oversight. That the budgetary adjustments take place with clear guidelines and cannot be undertaken informally add to the credibility of the budget. The credibility of the original budget allocations is maintained by specifying, in advance, an adjustment mechanism in a systematic and fairly transparent manner.

Two factors that can undermine the credibility of the budget are significant extra-budgetary activities, and the poor monitoring of fiscal risk, debt and contingent liabilities. The PFM systems effectively address fiscal risk vis-à-vis the National Revenue Fund that might emanate out of unforeseen expenditure burdens arising out of sub national government loans or public enterprise bail outs (see PI-9). Further, a contingency reserve is set aside to address unforeseen and unavoidable expenditure such as responses to natural disasters or for programmes announced in the budget but not yet appropriated. In the current fiscal year the requirements to support Eskom's debt drive to address an accelerated program of increased electrical generation capacity has resulted in fairly large contingency reserve of R6 Billion in 2007/2008 increasing to R20 Billion in 2009/2010.

While the government has been careful to address extra-budgetary activity by way of Departmental revenues, unbudgeted bail outs, unreported deferred funding through Public Private Partnerships (PPPs), unreported unconventional debt instruments to address losses in Public Enterprises (see PI-7(i)), there still remains in the area of donor activity a considerable proportion (approximately 75% of donor funds) that remains outside of the budget process. As it turns out, the total quantum of donor assistance currently remains small (less than 1%) and hence has not impacted negatively upon the scoring[5].

The lack of a standard for budget estimates with respect to donor contributions impact negatively on budget credibility. There are neither standard definitions for such budget estimate elements as pledges, available funding, commitments nor are there clear and consistent methods for deriving Donor funded budget estimates from these. What is employed, when provided by donors, is instead a reflection of some combination of pledge, commitment and projected disbursement. This, rather than a careful estimate of actual disbursement based upon commitment, the likelihood of disbursement given the applicable conditionalities and the absorptive capacity taking into account the procurement planning and implementation schedules of the projects to be financed. The limited attention to actual budget estimates rather than the unfiltered adoption of pledges, commitments and projected disbursements tend to undermine the credibility of the budget (see D-2).

[5] Using estimates upon verified amounts obtained directly from donors it would appear that the total donor activity remains below 1% at this time, but with anticipated increases from such donors as the EC, US and China this almost certainly increase donor inputs beyond 1% and so without drastic improvements of the incorporation of donor funds into the budget process future PEFA assessments may score PI-7(ii) a C.

Comprehensiveness and transparency

By way of comprehensiveness and transparency, South Africa's central government PFM systems and procedures are outstanding. The PFM reforms carried out since the mid 1990s have evolved a comprehensive budgetary process. Fiscal forecasts are realistic and debt management is based upon a clear and well articulated debt management strategy with a regular, accurate and timely reporting and monitoring of the debt stock. The budget documentation is complete, comprehensible and comprehensive including the macroeconomic assumptions, the fiscal balance along with the make up of any deficit financing, the debt profile and status, the financial assets, the historical budget outturns and clear explanations on the impacts of new major revenue and expenditure policy initiatives.

The government has adopted standards for the budget formulation and execution, based on economic, administrative, programme and sub-programme that can produce consistent documentation according to GFS/COFOG standards. The budget documentation reports on program and sub programme classifications as well as on cluster and functional classifications. The budget classification is also reflected directly in the institutional arrangements for managing the budget. The chart of accounts incorporates and is consistent with the budget classifications. The budget classification, institutional arrangements and accounting and financial reporting are well capable of supporting a policy based budgeting process. There are though ongoing efforts to define programmes more consistently and to better specify output indicators.

The budget documents submitted to parliament are comprehensive and comprehensible. They include a Medium Term Expenditure Framework which appropriately addresses the requirements for both meaningful budgetary formulation as well as to properly guide and control budget implementation. All revenues generated directly by Departments are transferred to the National Revenue Fund which operates as a Treasury Single Account. All expenditure is made through a centralised payments system. This arrangement provides effective control over the extent of extra-budgetary expenditure by the Departments that can be undertaken. The National Treasury has the capacity to oversee revenue and expenditure transactions through daily bank reconciliations and to monitor the public entities plans and financial management. There are no unreported Public-Private Partnerships, nor unreported unconventional financing instruments for addressing losses of Public Enterprises (including any foreign exchange losses of the South African Reserve Bank). All security agency funds are reported on in aggregate, even if details of expenditure remain undisclosed. The financial reports consolidation process includes a reconciliation process between sources of funds and applications which reasonably assures that there are no significant extra-budgetary funds outside donor funds. The comprehensiveness of extra-budgetary reporting ends with the reporting on donor activity (see D-2). The proportion of Donor funds managed through the Reconstruction and Development Programme (RDP) representing approximately 25% of donor funds is budgeted for and reported on fairly transparently and comprehensively. However, approximately 75% of all donor funds are operated off budget. Even with the inclusion of (estimated) off budget donor funds the total amount is almost certainly less that 1% of total expenditure, thus leading to a high score for the extent of unreported government operations in PI-7.

The high level of transparency in South Africa's budget processes is anchored in the PFM Act and has resulted in significant gains by way of market risk perceptions and consequently positively impacting upon the cost of money, and expanding participation in the tax economy. There is broad transparency demonstrated by way of inter-governmental fiscal relations, the oversight of public enterprises and public borrowing, and with respect to public access to key fiscal information.

A review of the mechanisms for the vertical and horizontal allocation of resources to Sub-national Government suggests a fully evolved and transparent system which incorporates parliamentary oversight. The budget allocation process provides reliable information on the allocations to be made to them well in time before the start of their detailed budgeting processes. The budget releases to sub-national government entities are timely and fully predictable. There are two levels of sub national government: the provincial and the local governments. Fiscal reporting of provincial government is consolidated into the national financial reports. Financial reports of the Local Authorities are consolidated into a separate annual report consistent with central government fiscal reporting.

There is comprehensive direct integration of the public enterprises[6] financial reporting (90% by expenditure) into the Consolidated Financial Information (CFI). This even with the differing accounting standards (accrual versus modified cash basis) used by the commercial public enterprises and the central government. There is a fairly careful risk assessment of Public Enterprise operations using a comprehensive risk analysis framework, however at this time not all major public enterprises are complying fully with the Assets and Liability Management Division's financial reporting requirements to make the system fully effective. The budget process seeks to anticipate the requirement for public enterprise recapitalisation to possibly support rapid expansion (re: Eskom), subsidies or loan defaults that might lead to calls on guarantees. There is the timely and regular audited fiscal reporting of public enterprises operations to permit effective oversight by the National Treasury and for the 9 major commercial public enterprises by the Public Enterprises Department.

The culture of transparency with regards to budget documentation is very active and there is budgetary, tax revenue, procurement and audit information that is made available in a timely fashion on the Internet through government websites. Fiscal information is also made available through public and academic libraries. There have been efforts made at improving access to public information through the use of simplified budget material and encouraging direct public interaction with Minister of Finance through web submissions. The Provincial Governments provide financial reporting that indicates the resources received in aggregate by primary schools and primary health care clinics.

Policy-based budgeting

With respect to policy based budgeting, the central government scores very well save for two specific areas. These are in respect of when parliament approved the appropriations bill, and the preparation of fully costed sector strategies within a forecasted fiscal frame. South Africa has adopted a three-year Medium Term Expenditure Framework for its

6 Note that the PEFA manual refers to autonomous government agencies and public enterprises – these are termed Public Entities and National Government Business Enterprises within PFM reports in South Africa.

budgetary processes. The budget process occurs within a pre-announced resource envelope based upon three-year credible macro-fiscal forecasts and has strong bottom-up elements from the budget entities. The macro-fiscal framework is derived from a three year revenue forecast, a there-year pro-forma debt profile based upon careful macro-economic considerations. At the present time the macro-fiscal framework considerations exclude donor contributions which currently account for less than 1% of central budget expenditures. South Africa adopts a single budget process with both the recurrent and capital budget process coordinated by the National Treasury. The macro-fiscal framework defines both aggregate as well as cluster and functional forecasts which are directly linked to the annual budget ceilings.

The budget process encompasses policy input both by the parliament and the cabinet at the beginning and the end of the budget process. There are strong institutional arrangements in place for ensuring both strong policy as well as technical review. These include the Minister's Committee on the Budget that considers key policy and budgetary issues prior to the budget being tabled before the cabinet. The MinMEC serves as a political forum where national and provincial departments within a given sector discuss their budgets and the MTEC which is the technical committee responsible for evaluating the Departmental MTEF budget submissions. At the beginning of the budget cycle, parliamentary oversight is facilitated through the Medium Term Budget Policy Statement and at the end of the cycle by the debates on the Budget Review, the Division of Revenues Bill, and the Estimates of National Expenditure (ENE).

The budget process occurs in accordance with a definite budget calendar and is guided by clear and timely call circulars that facilitate an early budget preparation process by the budget holders. The budget preparation process as carried out by the budget holders is based upon firm base lines, if not hard budgetary ceilings, that are provided by the previous year's MTEF. The Departments have six to eight weeks to prepare their budget bids. Finalised ceilings authorised by cabinet which are provided towards the end of the budget preparation cycle facilitate about a month for Departments to finalise their budgets with approved bids incorporated. The preparation of budgets within final ceilings may be viewed as an amendment to the MTEF base lines since they typically differ by just a few percent from the previous budget ceilings and are allocated solely to new or expanded initiatives.

The national vision, mission and development objectives have been articulated within the Government's Contract with the People of South Africa. The Accelerated and Shared Growth Initiative for South Africa (ASGISA), which was formally launched in 2006, is the national development strategic framework aiming to raise growth and reduce employment and poverty. This national strategy has been updated through a medium term national development framework, the Medium Term Strategic Framework, which refines a 5 year national development framework. The strategic horizon is largely determined by the executive election cycle. The policy framework may be updated through the annual State of the Nation speech which highlights the "*Apex*" priorities. This, as was the case in 2008, can then be taken into account in the preparation of annual sector corporate plans and budgets. This national development framework serves as a basis for the development of sector strategies.

Most Departments prepare 5 year sector strategies along with updated annual corporate plans. Such strategies, however, are not developed within a fiscal frame nor are they always costed. Even when costed this is not done with recurrent cost implications taken into account. Links between the sector development plans and the budget occur mainly on a qualitative basis. Many elements of sound strategic planning have been introduced directly into the budget process and there are important elements of multi-year budgeting that are in place, however these elements remain constrained. There are strategic advantages missed when an insufficient planning horizon is assumed; when there are not direct links between the national plans, the sector plans, the MTEF and the annual budget process; and when planning is not carried out within a fiscal frame with some costing considerations as a basis for prioritisation. In the absence of these programmes and projects may reduce to a wish list. Indeed, officials indicated some concern that the inclusion of Departmental programmes and priorities into the MTEF may some times be somewhat ad hoc. While South Africa has evolved a very strong MTEF process there remains significant weakness in its longer term planning processes. The annual budgeting and medium term expenditure framework is well evolved in South Africa, however the strategic planning process and its linkage to the budget through the MTEF process omit some important aspects that suggest that some strategic advantages and investment efficiency improvement opportunity may be missed.

The inclusion of projects into the MTEF process follows a much stricter process which requires a complete costing process that includes both investments as well as forward linked recurrent expenditure ramifications. The Medium Term Expenditure Committee (MTEC), responsible for evaluating the MTEF budget submissions of national departments, and making recommendations to the Minister of Finance, places a high priority on the appropriate accommodation of forward linked recurrent expenditures. MTEC provides the aggregate and sector ceilings for the budget. Further, there is a direct and quantitative link between the MTEF process and the annual budget process with MTEF projections being used as the basis for the following year's budget preparation and resource re-allocation.

Debt sustainability analysis is performed on an annual basis by the National Treasury as well as the South African Reserve Bank. The debt sustainability assessment has become somewhat routine especially because of the very low debt stock levels that are currently at only 22.3% of GDP.

While the executive completes its budget allocation planning four to six weeks prior to the start of the fiscal year, the Parliament approves the appropriations three to four months after the start of the fiscal year after subjecting the budget proposals to vigorous debate. The PFM Act allows for continued spending by the executive up to a third of the proposed budget for the first four months of the new fiscal year.

While the quantum of donor contribution is small, its strategic and policy impact can be substantial especially in regards to the piloting of new initiatives and the transfer of expertise. The large components of donor funds that are off budget miss the opportunity to contribute positively in alignment with the budget policy objectives. Indeed, officials state that in some cases donor activities have undermined the achievement of policy objectives by forcing the unforeseen reallocation of national resources to complete projects whose funding may have been suspended or delayed due to unmet conditionalities. The complete implementation of the budget formulation process based upon the integration of a strategic planning process and centred on a Medium Term Expenditure Framework that is directly linked to the annual budget process should allow the Donors to align their support with the Government's own clear strategic development objectives and mange it in a way that harmonises well with the budget implementation and reporting.

Predictability and control in budget execution

The PFM systems of South Africa's central government score well overall with respect to predictability and control in budget execution save for one area. This area is with respect to procurement and non-salary expenditure management as it pertains to adherence of the procurement regulations close to the end of the fiscal year. Predictability in budget execution is premised upon revenue adequacy which in turn requires sound revenue administration. Many elements of revenue administration work very well. These include clarity of taxpayer obligations and liabilities, the legal constraints on officer discretion in the application of penalty waivers and rates, the sustaining of vigorous tax awareness and educational programs, the selection basis, planning and implementation of tax audits. Most directly and immediately the reconciliation of collections and transfers to the National Revenue Fund work very well. There is however one area of revenue administration that scores poorly in this assessment with respect to the stock and collection of tax arrears (see PI-15(i)). Closer inspection though reveals that current collection rates on tax arrears are very high and that the high stock of tax arrears may just be a historical characteristic made more prominent by a combination of historically high interest rates, and accounting policies that tend to overstate the level of arrears and the inclusion of substantial uncollectible tax arrears stemming from prior to 1994[7] that are yet to be written off.

Cash management and debt management are very well managed in the central government of South Africa and facilitate highly predictable budget releases. It should be noted though that cash management in the central government of South Africa succeeds primarily on careful considerations of predictability of revenue and debt service and do not require the same level of success with respect to non salary expenditure predictability. The reason for this is that given the large component of transfers and subsidies in the central government budget and with wages and salaries being predictable only approximately 7% of budget expenditure occurs through the procurement vehicle. South Africa uses a centralised payments system out of the National Revenue Fund which beyond daily bank balance consolidation that informs and guides payments facilitates the integration of cash management and debt management allowing the National Treasury to trade instruments on the money markets to effectively manage liquidity (fiscal) and earn interest income.

The effective management of debt and the government policy to reduce debt well below 20% of GDP has ensured adequate fiscal space within which to operate budget releases and hence avoid the need for cash rationing or undermining the administration's capacity to disburse to the Departments in accordance with agreed draw-down schedules. Debt

[7] 1994 is the year that South Africa transitioned to full democracy.

management is enhanced by having the authority to incur loans being vested in a single authority - the Minister of Finance. South Africa has adopted a debt management policy that is prudent and has led international rating agencies to assess South Africa's credit ratings as positive. Debt is monitored using the ARABAS system and regularly reconciled and reported on with respect to stock as well as debt service.

The central government employs a transverse computerised system BAS for expenditure management, accounting and financial reporting. Budget allocation and budget release discipline is strong. There is commitment control system built into the BAS which contributes to the achievement of expenditure outturns that closely match budgetary intent. There remain some issues pertaining to procurement planning and reporting on commitments which may contribute to the "*March spike*" phenomenon where there is a rush to spend unutilised funds at the close of the year. This in turn may be part of the reason for working around procurement procedures and incurring increasing expenditure arrears.

Payroll management is facilitated using a transverse computerised payroll system, PERSAL. This system directly links three databases: the establishment of posts, the personnel database which serve as control files, and the payroll database. Changes to these databases leave an audit trail and permit only selected access dependent upon function. The databases are encrypted. All civil servants are registered through PERSAL that include appropriate fields to protect against duplication. There are effective controls with respect to the creation of new posts, that include budgetary controls, the hiring of new employees (controlled by the posts database), and the assignment of promotions, transfers, allowances and terminations. Further, through the use of verification procedures, exception reports and regular physical payroll audits, there is fair assurance of the integrity of the payroll management system.

Both the Institute for Democracy in South Africa (IDASA) and the Steel and Engineering Industries Federation of South Africa (SEIFSA) report on a perception of public procurement being fair, responsive to open competition and broadly accessible. While it was not possible to demonstrate strict adherence to open competition across all National Departments the analysis of data from the Department of Health did show close compliance. There is a fully effective procurement complaints resolution process which is subject to oversight of an independent body. SEIFSA considers the complaints resolution process to be effective.

That said there are a few areas of concern. While effective controls exist for each of the main steps of the expenditure cycle, procurement controls remain less than fully effective. The legal regulatory requirements do not clearly establish open competition as the default method of procurement. They would suggest that practical considerations determine the use of other less competitive procurement methods. When coupled with the absence of clear regulation to curb the use of dilatory practice to justify the use of sole sourcing under emergency procedures, this may become an area of abuse. Indeed there is some evidence (see PI-4, PI-20) that expenditure is rushed at the end of the fiscal year, and on occasion procurement rules are by passed. Indeed such abuse is a concern of the National Treasury (see PI-20).

Internal audit in South Africa adopts the IIA standards and have developed manuals that are aligned with these standards. Quality assurance exercises, to ensure compliance with the standards are carried out each year, with independent bodies performing the quality assurances reviews once every five years. The Internal Audit Units prepare a risk assessment of their Departments and elaborate 3-years audit plans as well as annual operational plans. The plans incorporate a range of audit types including compliance, financial audits, payroll audits, system including information technology audits, forensic and performance audits. Audit work plans suggest that more than 50% of audit time is spent on systems audits.

Given their small proportion of the total budget expenditure (0.2% through the RDP fund account, and another approximately 0.6% outside of the budget) there are no impacts on expenditure predictability of donor practices discernable at an aggregate level. However, there are still significant impacts upon budgetary performance that can be introduced. Less than 85% of the committed disbursements under sector budget support were released during the period reviewed, and what was released was generally neither timely nor predictable. This finding is particularly significant given that the immediate impetus for this assessment was to justify the intended move towards sector budget support. Without improved performance, such a move would further impact negatively on budget predictability in the central government budget.

Accounting, recording and reporting

South Africa has achieved a full integration of cash management and debt management. This has been facilitated by the near real time status of its treasury managed bank account reporting and reconciliation. These are formally reported (Section 32) on a monthly basis within four weeks of the close of the month. There are a number of donor funded accounts that are not reported on by donors[8]. Indeed, in contravention to the PFM Act a number of such accounts are opened without the explicit authorisation of the National Treasury. Reconciliation and clearance of suspense accounts take place monthly[9] within a month of the close of the month (except for a few identified accounts) and are force closed as part of the end of year procedures.

Government accounting standards that promote full disclosure are applied across all Departments consistently and are included in the annual reports that present the audited annual financial statements. The monthly expenditure returns are comprehensive, consistent with the budget classification and structure, and allow direct comparison of budget implementation to the original budget. The reporting format does not, however, distinguish commitments. The PFM Act requirement (Section 32) to consolidate the Department expenditure returns and publish within 30 days of the close of the month has ensured their timeliness and hence their effectiveness as a management tool. The report also includes a reconciliation of revenues, net changes in debt position, expenditures and

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8 Some donors argue that such accounts are implementing agency accounts or their still own accounts rather than government accounts that are being managed and controlled by them or their designated agents. A logical conclusion to such an interpretation would be that the government as beneficiary receives only in-kind donations and the financial reporting should reflect that.

9 In the current year 2008-2009 clearance of suspense accounts have taken place quarterly in response to recent changes that have been made to the chart of accounts. This has been an intentional decision to build up accounting statistics to better manage the process over time. It is anticipated that the standard of monthly clearances will be returned to in the next fiscal year.

consolidated bank balances. This aggregate reconciliation provides assurance as to the accuracy of the reports.

The BAS accounting system, a transverse system used across the central as well as provincial governments provides reliable information on resources received in cash and kind by the primary schools and the primary health clinics across the country. The front line service delivery units are managed by the nine provinces and five metropolitan authorities and their expenditure reported upon annually. The National Treasury compiles this data and presents it in a consolidated report: the Provincial Budgets and Expenditure Review.

Consolidated government accounts are prepared annually with revenue and expenditure information as well as a table of financial assets and liabilities. The annual appropriations accounts are completed and audited within six months after the close of the fiscal year.

External scrutiny and audit

Both the position and the office of the Auditor-General (AG) meet all of the standards of independence[10] set by INTOSAI for supreme audit institutions. These include the legal requirements with respect to the appointment and termination of the Auditor-General, the financing of the budget, the hiring of staff, the auditor's jurisdiction and the timing and extent of dissemination of audit reports. In practice all central government entities are audited every year. A full range of audits are performed, including systems audits, financial and compliance, procurement and performance audits as well as payroll and Information Technology audits. Public Enterprises are audited by private audit firms. These audit reports are disseminated to the Auditor-General. The standards applied are the International Standards on Auditing (ISA) and the International Organisation of Supreme Audit Institutions (INTOSAI). The Auditor-General uses this combination as the INTOSAI standards do not provide sufficient guidance on specific matters for providing assurance.

Departmental audit reports along with their audited financial statements are submitted to the legislature within five months from the end of the fiscal year which is equivalent to three months from submission to the AG. Step one; Departments submit their financial statements within two months from the fiscal year-end to the Office of the Auditor-General. Step two; the AG audits the statement within two months. Step three; Departments submit their annual reports to the legislature within one month. As a separate process a Consolidated Financial Information (CFI) report on departmental financial statements is prepared by the National Treasury and submitted to the AG separately within five months from the end of the fiscal year. These are further submitted to the legislature within six months of the end of the fiscal year.

There are audit committees responsible for ensuring timely and systematic follow up on audit findings by accounting officers. While there appear to be systematic follow up on internal audit findings, there is little evidence of systematic and timely follow up on

[10] There may be some question raised as to the independence of the AG with respect to the dissemination of audit reports because these are submitted to the Minister of Finance for onward transmittal to parliament; however the PFMA states that should the Minister of Finance fail to do so then the AG will.

external Audit findings and it is often left to the field auditors to ensure that recommendations are followed through as part of subsequent audits. It appears that there may be opportunities missed to strengthen further the PFM system as the recommendations made by the Auditor-General are not enforced through the full implementation of corrective measures.

South Africa is characterised by a democratic system and the parliamentary oversight of the government's budget processes also includes actual expenditure achievements and the quality of expenditure management. The parliamentary debates cover fiscal policies, the medium term fiscal framework as well as the details of revenue and expenditure estimates. The annual budget legislative review takes about five months including the review of the Medium Term Policy Paper at the start of the budget cycle. In practice, it usually begins with the tabling before parliament of the appropriations bill about a month before the end of the fiscal year. It usually allows for passing the budget to occur about three months after the start of the financial year. The process of budget review is subject to clear rules and a specific calendar and so permits the thorough review by committees and sub-committees to facilitate vigorous debate.

The Adjustment Budget Estimates presented by the Minister of Finance and voted by the parliament, is reviewed once a year usually in October. This stance is consistent with the Government's emphasis on a strong fiscal discipline objective to its public finance management. Clear rules exist with respect to in-year budget amendments by the executive with respect to item, programme and vote amendments.

A review of expenditure anomalies as identified through external audit is done through a public accounts committee, SCOPA. At the present time SCOPA relies on the Audit Committees to ensure that Accounting Officers fully implement its recommendations. However there have not been systematic or timely follow up on SCOPA recommendations across all Departments.

Assessment of the impact of PFM strengths and weaknesses

When viewed from the perspective of the three main objectives of a sound PFM system, namely aggregate fiscal discipline, strategic allocation of resources and the efficient delivery of services; South Africa scores very well with respect to aggregate fiscal discipline. The PFM systems are capable of allocating resources in accordance with priorities. The utilisation of a three year macro fiscal framework, with a definite budget calendar that facilitates the meaningful bottom-up participation by Departments, along with the very successful integration of cash management and debt management, and the achievement of predictable budget releases and effective payroll management all point to efficient delivery of services. However these positives are negatively impacted by some procurement and non salary expenditure management challenges. The PFM systems provide financial feedback at the end of the service delivery cycle - the receipts by the front line facilities such as primary schools and primary health care facilities.

There are two main factors that colour the PFM of the central government in South Africa:

1. *The concurrent role of the central government with the provincial governments*: The central government is responsible for regulation, policy and planning, revenue administration, cash and debt management, consolidated financial reporting and monitoring and evaluation. The provincial governments are responsible for delivering on the effectiveness of the strategically allocated funds of the central government; and for service delivery. These concurrent roles lead to a somewhat shared role of PFM as well. Consequently an assessment of the PFM systems, procedures and practices of central government are more a measure of the legal and regulatory framework, the main institutional arrangements, the level of aggregate fiscal discipline achieved. It measures only to a degree the achievement by way of the strategic allocation of resources (front end) – since it would require the provincial governments working as partners to deliver on the effectiveness (back end) of such strategically allocated resources. The assessment of the central government is not provided much opportunity to measure service delivery. For example the Department of Health is directly responsible for managing three medical laboratories. All hospitals and clinics are operated directly by the provinces. Consequently, a full picture of the strategic allocation of resources and efficient service delivery will only emerge when PEFA assessments have been applied to the provinces;
2. *The implementation of transverse computerised systems:* The central government has implemented a number of transverse computerised systems that operate on country wide networks that facilitate the full country wide roll out of a number the PFM systems. These include the revenue administration systems for income tax, VAT and customs duties; the BAS which provides computerised accounting across all Departments and PERSAL which is the system used to manage payroll. The two systems together provide an opportunity for the integration of cash management and debt management. There is also the LOGIS system used for procurement, but this is not yet available across all departments.

Aggregate Fiscal Discipline

With respect to aggregate fiscal discipline, South Africa's well developed debt strategy, and comprehensive transparent management of debt; effective fiscal risk assessment and oversight of public enterprises; credible three year fiscal forecasts (revenue, net borrowing and debt service, and expenditure) that serves as the basis for top-down budgetary discipline; well managed budget releases and a comprehensive and effective commitment control process all point to the ability to deliver strongly on aggregate fiscal discipline (see PI-1, PI-2, PI-3, PI-16 and PI-17). This is further strengthened by a strict commitment control system supported by an effective cash management system. However, there remain some concerns with respect to the accrual of expenditure arrears, commitment reporting and procurement management.

Strategic Allocation of Resources

South Africa has in place a number of important steps towards achieving a budgetary process that is fully capable of the strategic allocation of resources (see PI-5, PI-11 and PI-12). However, there are still a number of important steps that are not fully implemented including the development of sector strategy fiscal frames and full costings of the sector strategy elements with a more direct link to the medium term expenditure framework. The budget classification in South Africa is well capable of supporting a policy based budgeting process and thus provides a necessary input for achieving the strategic allocation of resources. South Africa issued the Medium Term Policy Framework to serve as its national development framework which includes a clear articulation of its development policy objectives. Although the development objectives do not rely heavily upon Donor inputs, there are missed strategic opportunities that arise due to the lack of a close alignment of donor grants with the budget process and a broad absence of timely reporting on project and programme achievements consolidated into the national consolidated financial reporting framework. The effectiveness of the central government's success in allocating resources strategically, followed by disciplined budget releases in accordance with such strategic considerations will still rely upon provincial governments to deliver on such strategy as well as the incorporation of effective monitoring and evaluation to inform and continue evolving and refining strategy. Particularly important to assessing the impact of policy objectives is the tracking of resources received by front line service delivery units such as primary schools and primary health care facilities (see PI-23). The consolidation of Provincial Budget Statements with their detailed reports on primary school and primary health care receipts of cash and kind by the National Treasury into the Provincial Budgets and Expenditure Review presents a sound basis to better manage the achievement of effectiveness.

Efficient Service Delivery
The concurrent arrangements between the central government and the provincial governments on public finance places little focus on service delivery within the central government's operations. However, significant contributions to efficient service delivery can be made through effective monitoring of transfers to frontline service delivery units to guide policy and inform the strategic allocation of resources. This, as indicated above is presented annually in the Provincial Budgets and Expenditure Review. There are areas that South Africa has had much success in contributing to efficient service delivery. These include the successful collection of revenues which provides a sound basis for achieving the efficient delivery of services; and also there have been considerable efficiency gains that have arisen as a consequence of South Africa's successful integration of cash and debt management both with respect to efficient liquidity management, as well as with respect to the market response to sound debt management with the subsequent reduction in the cost of money to government. One factor that appears to have adversely affected the efficiency of service delivery has been some areas of concern in procurement and non salary expenditure management (see PI-19, PI-20).

Prospects for reform planning and implementation

South Africa has evolved its reform approach away from a comprehensive integrated approach centred on a single integrated strategy, with emphasis on sequencing and coordination, to a more incremental one. Implicit in the approach of PFM reform in the first decade or so was a focus on three broad stages or platforms. These were achieving fiscal discipline, the efficient delivery of services, and the strategic allocation of resources. The incremental approach appears to work because the main fundamental changes to the PFM have already been achieved and the focus is now more on capacity development rolled out to the provinces and municipalities. It can remain effective in delivering on improvements because it has already made the major transition to a reformed PFM system and is now focusing upon continuing improvements of the reformed systems informed by the lessons learned through the decade long reform experience.

The commitment to continuing improvements in PFM in South Africa has political championship at the very highest levels through the Minister for Finance. Implementation oversight and monitoring is the responsibility of the National Treasury's Heads of Division. Coordination of the reform efforts is the responsibility of the Budget Office. The Special Functions Division that includes the PFMA Implementation Unit has been playing a particularly important part in drawing lessons from experience on the legal and regulatory framework and coordinating its evolution.

The Government of South Africa has embarked upon a number of very successful PFM reforms over the last decade and a half or so. The reform agenda focused upon:

- The establishment of a legal and regulatory framework to strengthen and improve upon the transparency, comprehensiveness and credibility of the budget, debt management and external scrutiny and oversight;
- A focus away from input controls to delivered outputs supported by improved financial reporting and public and parliamentary access to budget and fiscal documents, and the introduction of Audit Committees to better hold budget managers accountable;
- A better alignment of policy, planning and budgeting;
- A move to a multi-year budgeting framework to allow the re-allocation of resources to new priorities;
- The improvement of debt management through the introduction of suitable institutional arrangements; taking over the responsibility for funding decisions from the South African Reserve Bank; reforming the money market; integrating cash and debt management, diversifying the debt portfolio and restricting the proportion of foreign debt; and establishing a risk management function;
- The revenue administration with respect to the improvement of revenue collections and promoting education, service and enforcement;
- Strengthening the independence and the effectiveness of the office of the Auditor-General;
- The reform initiative in local government was implemented through the Municipal Finance Management Act (MFMA), which became effective in July 2004 and whose implementation is supported by the annual Division of Revenue Act. The National Treasury has developed a phased implementation strategy of financial and technical support for local government based around the MFMA, including conditional grants, subsidies, technical guidelines, policy advice and the placement of international advisors with various municipalities. This strategy takes into account the diverse capacity of municipalities for implementing the reforms.

The early phases of PFM reform were premised upon the issuance of detailed reform strategy, which while largely adhered to was never passed as a white paper. With the substantial achievements in PFM reform over the last decade and a half, as attested to by the results of this PEFA assessment, continuing PFM reform is probably better characterised as a process of strengthening and improving rather than a process of full reform. In this maturing phase, the centralised reform coordinated approach is deemed to be less effective rather than allowing departments to get on with building capacity and improving their reformed systems.

Quite distinct from the early period of reform which saw the introduction of new laws, changes in institutional arrangements, the introduction of new budget systems; the current phase of reform is characterised by amendments to the law, the improvement (and replacement) of existing computerised systems, continue to improve upon programme structure and descriptions, improving the specification, measurement and monitoring of output targets and continue broadening the scope of the consolidated financial statements.

This approach to reform is consistent with the adopted philosophy of allowing managers to manage and holding them accountable for results. Hence specific improvements are carried out by divisional heads with fewer requirements for careful coordination with other divisions since the improvements at this stage are incremental. This appears to work because the main fundamental changes to the PFM have already been achieved.

By way of donor participation and support of PFM improvements, this would require a broader dialogue within the budget formulation process of the National Treasury, the Parliament and the Office of the Auditor-General which would identify within their sector strategies and/or budgets reform improvement programmes and projects that could be flagged for support from donors.

Table 0.1 Overall summary of PFM Performance Scores

PFM Performance Indicator		Scoring Method	Dimension Ratings i.	ii.	iii.	iv.	Overall Rating
A. PFM-OUT-TURNS: Credibility of the budget							
PI-1	Aggregate expenditure out-turn compared to original approved budget	M1	A				**A**
PI-2	Composition of expenditure out-turn compared to original approved budget	M1	A				**A**
PI-3	Aggregate revenue out-turn compared to original approved budget	M1	A				**A**
PI-4	Stock and monitoring of expenditure payment arrears	M1	A	A			**A**
B. KEY CROSS-CUTTING ISSUES: Comprehensiveness and Transparency							
PI-5	Classification of the budget	M1	A				**A**
PI-6	Comprehensiveness of information included in budget documentation	M1	A				**A**
PI-7	Extent of unreported government operations	M1	A	A			**A**
PI-8	Transparency of inter-governmental fiscal relations	M2	A	A	B		**A**
PI-9	Oversight of aggregate fiscal risk from other public sector entities	M1	B	A			**B+**
PI-10	Public access to key fiscal information	M1	A				**A**
C. BUDGET CYCLE							
C(i) Policy-Based Budgeting							
PI-11	Orderliness and participation in the annual budget process	M2	A	A	D		**B**
PI-12	Multi-year perspective in fiscal planning, expenditure policy and budgeting	M2	A	A	D	A	**B**
C(ii) Predictability and Control in Budget Execution							
PI-13	Transparency of taxpayer obligations and liabilities	M2	A	A	A		**A**
PI-14	Effectiveness of measures for taxpayer registration and tax assessment	M2	A	A	A		**A**
PI-15	Effectiveness in collection of tax payments	M1	D	A	A		**D+**
PI-16	Predictability in the availability of funds for commitment of expenditures	M1	A	A	A		**A**
PI-17	Recording and management of cash balances, debt and guarantees	M2	A	B	A		**A**
PI-18	Effectiveness of payroll controls	M1	A	A	A	A	**A**
PI-19	Competition, value for money and controls in procurement	M2	D	D	B		**D+**
PI-20	Effectiveness of internal controls for non-salary expenditure	M1	A	A	C		**C+**
PI-21	Effectiveness of internal audit	M1	A	A	A		**A**
C(iii) Accounting, Recording and Reporting							
PI-22	Timeliness and regularity of accounts reconciliation	M2	B	A			**B+**
PI-23	Availability of information on resources received by service delivery units	M1	A				**A**
PI-24	Quality and timeliness of in-year budget reports	M1	C	A	A		**C+**
PI-25	Quality and timeliness of annual financial statements	M1	A	A	A		**A**
C(iv) External Scrutiny and Audit							
PI-26	Scope, nature and follow-up of external audit	M1	A	B	B		**B+**
PI-27	Legislative scrutiny of the annual budget law	M1	A	A	A	A	**A**
PI-28	Legislative scrutiny of external audit reports	M1	A	A	B		**B+**
D. DONOR PRACTICES							
D-1	Predictability of Direct Budget Support	M1	D	D			**D**
D-2	Financial info provided by donors for budgeting/reporting on project/program aid	M1	D	D			**D**
D-3	Proportion of aid that is managed by use of national procedures	M1	D				**D**

1 Introduction

1.1 Objective of the PFM-PR

The purpose of this Public Expenditure and Financial Accountability (PEFA) Assessment has been to assess the current status of the Central Government of South Africa's Public Finance Management (PFM) systems, procedures and practices using the PEFA methodology. This is based upon a set of 28 high-level performance indicators that measure the current status of the Central Government's PFM systems, plus 3 high-level performance indicators that measure the performance of donor practices with respect to the impact on the government's budgetary processes. This assessment is being carried out in order to set a baseline for the continued use and assessment of these indicators. The performance indicators, which are scored on a rating system from A to D is presented along with a narrative to provide a brief description of PFM processes and procedures adopted by the government, and also to support and explain the scorings. In addition to the performance indicators, the PFM performance report reviews the country context in which such PFM is carried out, the legal and regulatory framework, the institutional arrangements and an assessment of the PFM reforms currently being undertaken.

This assessment aims to benchmark current PFM systems, procedures and practices within the central government of South Africa and through the identification of weaknesses, serve as a basis for guiding improvements to achieve better public financial management. The PEFA approach is consistent with South Africa setting its own agenda for PFM reform around which a coordinated program of donor participation can be aligned. This Performance Measurement Report is intended to serve as a common information pool on PFM performance in the Central Government of South Africa for government, donors and other stakeholders at country level. The report set out below and the baseline established will also serve as one element of the monitoring and evaluation (M&E) framework available for monitoring on a long term basis the outcomes of the PFM reform.

In keeping with the "*Strengthened Approach*", and hence adopting a harmonised approach, it was agreed to conduct a full PFM assessment in accordance with the Performance Measurement Framework developed by the PEFA Secretariat. The immediate impetus for carrying out this PEFA Assessment is in the short-term the European Commission's (EC) move from project support to sector budget support. The EC will use the PEFA assessment as a basis for information and PFM performance monitoring so as to fulfil its internal requirements for transitioning to sector budget support. The EC Guidelines for Budgetary Support mandate a preliminary assessment of Public Financial Management to ascertain the feasibility of such an approach to development aid in the country.

The broader rationale though for carrying out this PEFA Assessment has been to benchmark the PFM performance of the central government of South Africa against a widely adopted international standard, to provide feedback on the outcome of its extensive PFM reforms over the past decade and a half, and to identify areas of weakness to guide the areas of focus for continuing improvements. Further this assessment should serve to provide all donors with a common information pool on the PFM systems, procedures and practices as a way to assist with their decision making with regards to the most effective aid modalities for continuing support to South Africa. Finally, it is to serve as a basis for achieving effective dialogue on how to achieve improved outcomes from donor participation in the budgetary process.

It is important to emphasise that the purpose of this evaluation has not been to evaluate and score particular institutions or responsible individuals in the Government. It makes no comment on fiscal or expenditure policy, nor does it address any issues pertaining to capacity or capacity development. The focus of the PFM Performance Measurement Framework both with respect to intent and execution is solely on the PFM systems. The report, in keeping with the "*Strengthened Approach*" intentionally does not proffer any recommendations.

1.2 Process of preparing the PFM-PR

This PEFA assessment was sponsored by the European Commission which prepared the terms of reference (TOR). The TOR was circulated to a number of development partners and to the government. At the start of the mission a presentation of the PEFA methodology was made to Government Officials as well as separately to a group of Cooperating Partners. An Inception Report including a Work Plan was prepared and disseminated to the EC and a number of government officials who were to participate in the interview process.

There was excellent cooperation from Government officials in terms of making time available on short notice in spite of their own pressing work demands. Officials were fully engaging during meetings and any information requested was provided promptly. In particular a number of officials agreed to meet the Consultants together as a way of accommodating the tight interview schedule. One outcome of the interview process which involved a great number of personnel, covering a cross section of PFM officials in the central government, was a clear demonstration of how well officials understand the PFM systems and procedures for which they are responsible, and to what degree they focus upon grappling with the challenges of improving performance further.

A mid-assignment review was carried out and a presentation made to government officials and a widely representation of the cooperating partners. There was also an exit workshop to present the aide memoir. The draft report was shared with the Government and its cooperating partners for their comment and input. Copies were also sent to the PEFA Secretariat for review. A final mission took place after the revision of the current draft report in order to discuss the findings of the assessment with government officials particularly those interviewed.

1.3 Methodology

The PEFA evaluation was carried out between June and September 2008. The field mission was carried out between June 20th and August 1st 2008, and a follow up mission carried out between September 13th and September 20th. Meetings were arranged with the assistance of the National Treasury. A National Treasury Official accompanied the consulting team on many of the interviews. The PEFA assessment involved:

- Reviewing legal and regulatory documentation, budget documentation and financial and audit reports;
- Assessing the requirements for further analysis and evaluation of PFM practice in the central government of South Africa, based upon:
    - Interviews with Government Officials in the National Treasury as well as the South African Revenue Services, South African Reserve Bank, the Parliament, the Office of the Auditor-General, the Departments of Provincial and Local Government, Education, Health Public Works, Public Enterprises, and Public Service Administration; donors including the United States, the United Kingdom, the European Commission, Canada, Japan, Netherlands, Germany, the World Bank and the IMF; and private sector organisations;
    - Quantitative analysis of official financial and budgetary data;
    - Reviews and assessment of legal and regulatory documentation;
    - Assessments of PFM procedures and systems; and
    - The application of professional judgement.

An important consideration in developing these indicators is an appreciation of the quality, comprehensiveness and accuracy of data that is used to determine the indicators. The reliability of the indicators can only be as good as the accuracy of the financial data upon which they were calculated. The consultants therefore emphasised the completeness and quality of financial data in determining the PEFA indicator measures.

1.4 Scope of the assessment

The assessment focuses on all public revenues and expenditures of the central government and the institutions responsible for such. The scope of the PEFA Assessment is limited to the central government and does not include the Provincial or Local Governments. Nor does it include an assessment of the public enterprises (commercial and non commercial, financial and non financial). Consequently, this assessment covers approximately a third of the public sector; albeit the third that includes the majority of public sector revenues and the majority of public sector debt service. Table 1.1 provides a summary of public sector expenditure indicating the proportion of central government expenditure labelled National Departments. The assessment covers the fiscal years 2005/2006, 2006/2007 and 2007/2008.

Table 1.1 Proportion of Central Government Expenditure to Total Public Sector Expenditure (million Rand)

	2004/2005		2005/2006		2006/2007	
Public Enterprises	152,948	28%	153,107	25%	152,813	23%
National Departments	167,289	30%	194,723	32%	212,629	31%
Provinces	138,511	25%	154,368	25%	178,871	26%
Local Government	97162	17%	83,410	18%	128,106	20%
Total	555,910	100%	615,080	100%	672,419	100%

Source: Budget Review 2008, Consolidated Financial Information for the years ended 31 March 2006 and 2007; Local Government Budgets and Expenditure Review 2003/04 - 2009/10.

Payments in South Africa are highly centralised with expenditure being managed through the BAS system which serves as the central General Ledger. In respect of analysis performed, the assessment segregates out primary expenditure and domestic revenues from grants (except for direct budgetary contributions made through the Reconstruction and Development Program fund account) and loan revenues and grant and loan funded expenditure.

The PEFA methodology presumes that assessments shall be carried out every three to four years and in doing so will provide a clear and accessible basis for monitoring PFM reform progress over the long term. Extending the assessment over time to the provinces would provide a more complete (both quantitatively and qualitatively speaking) measurement of the PFM activity in the Public Sector of South Africa.

The structure of the rest of the evaluation report is as follows:
- Chapter 2 provides background information and the economic and fiscal context for the evaluation;
- Chapter 3 explains the scores for the 31 individual performance indicators;
- Chapter 4 describes the government's reform programme; and
- A series of appendices provides more detailed reference information, including the TOR for the evaluation (Annex 1); a summary of the PEFA scoring calibration (Annex 2); a list of the stakeholders visited by the team (Annex 3), and a list of the documentation reviewed (Annex 4). An organigram of the National Treasury is presented in Annex 5. A summary of the comments and responses to the draft PEFA Report is presented in Annex 6.

2 Country background information

2.1 Description of country economic situation

2.1.1 Country context

South Africa is a middle-income emerging market with a GNI per capita of $4,960 with a population of about 47.9 million. It has a full spectrum economy; with features of both developing as well as developed countries with the consequent uneven distribution of wealth and income. The primary sector is based on manufacturing, services, mining, and agriculture. It features a sound and well regulated financial sector and a modern and extensive infrastructure base. Economic growth in South Africa has been robust since 2004. Table 2.1 provides a summary of key economic indicators.

The Accelerated and Growth Initiative for South Africa (ASGISA) targets an average economic growth of 4.5% until 2010 and of 6% between 2010 and 2014. South Africa's economy grew in real terms by more than 5% during the period 2005-2007. This growth, however, has slowed abruptly to an annualised rate of only 2.1% in the first quarter of 2008 reflecting the impacts of the slowing down in global growth rates and the inflationary pressures due to higher oil and food costs.

Despite the growth progress in the last years, the reduction of unemployment and poverty has been lagging behind. Inequality is widening mainly as a result of the unemployment challenges. South Africa's income inequality remains one of the highest in the world according to the World Development Report of 2006. The Human Development Index (HDI) for South Africa is 0.674 ranking the country 121st out of 177 countries with data. For the period 1996 to 2006, there has actually been a slight rise in inequality in South Africa as a whole.

Since 2004 inflation has started rising after a period of remarkable progress in lowering the inflation rate. SARB reports that at the beginning of 2008 both producer and consumer prices reached double-digit rates of inflation. The high inflationary pressures are particularly due to soaring food prices, increasing petrol prices, and domestic supply constraints in certain sectors.

The current account deficit increased noticeably in the period 2005-2007 and is mainly reflected by a higher growth in imports vis-à-vis exports, as well as large dividend payments to foreign shareholders. The deficit was covered by portfolio and FDI inflows.

South Africa is member of the Southern African Development Community (SADC)[11] and has placed regional integration by SADC member states at the top of its foreign economic agenda. South Africa is also member of South African Customs Union (SACU)[12] which shares a common tariff regime without any internal barriers. Customs revenues are shared according to an agreed formula.

Table 2.1 Selected Economic Indicators

	2004	2005	2006	2007
Population and unemployment				
Total population[13], millions	46.6	46.9	47.4	47.9
Annual population growth, %	1.25	1.16	1.06	0.94
Unemployment rate, %	26.2	26.7	25.5	23.0
National income and prices				
GDP constant 2000 prices, R billions	1,062,028	1,115,136	1,175,216	1,235,627
GDP current prices, R billions	1,395,369	1,541,067	1,741,060	1,993,894
GDP, annual real growth, %	4.8	5.1	5.0	5.1
Real GDP per capita, annual % change	3.8	4.1	3.7	3.8*
CPI (annual average), %	1.4	3.4	4.7	7.1
External sector (US$, billions)				
Current account balance	-7.4	-9.8	-16.6	-17.7*
Capital account balance	0.1	0.0	0.0	0.0
Financial account balance	6.8	11.4	15.1	20.7*
Overall balance of payments	5.8	5.4	4.4	3.0*
Total foreign debt	45.0	48.4	59.2	…

Source: Statistics South Africa (population, GDP, unemployment, inflation); IMF Country report No. 07/274 (2007) for Balance of Payments data and GDP growth rates; SARB for foreign debt.

Note: (*) – IMF projections.

2.1.2 Overall government reform program

The Government's ten-year vision for South Africa for the second decade of freedom and democracy is reflected in the Government's Contract with the People of South Africa. The Accelerated and Shared Growth Initiative for South Africa (ASGISA), which was formally launched in 2006, is the government development strategic framework aiming to raise growth and reduce unemployment and poverty. The Programme of Action 2007 focuses government action into a series of integrated clusters in order to synergise policy approaches and implementation towards the achievement of the national goals.

11 SADC comprises Angola, Botswana, the Democratic Republic of Congo (DRC), Lesotho, Malawi, Madagascar, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe.

12 SACU comprises Botswana, Lesotho, Namibia, Swaziland and South Africa.

13 Mid-year estimate.

2.1.3 Rationale for PFM reforms

With the transition to a democratic state in 1994, the South African Government was faced with high expectations on the integration of a large segment of its population disenfranchised by its history of apartheid. It would not be enough merely to articulate a vision of growth and shared prosperity, but to be able to deliver on such promise. This requires a sound public finance management framework, its implementation being consequent to the successful implementation of PFM reforms. In 1996 the government commenced upon a number of major financial management and budget reforms in order to improve the fiscal sustainability, alignment of spending with the new national priorities and the maximisation of existing resources towards these priorities.

This reform has achieved many substantial improvements as attested to by the results of this assessment however, there remain a number of areas that still require improvement especially as it pertains to the effectiveness of expenditure in line with strategically allocated resources and the achievement of value for money in service delivery.

2.2 Description of budgetary outcomes

2.2.1 Fiscal performance

The budget deficit has over a sustained period been reduced progressively through both revenue measures and expenditure restraint, and for the last two years of the review period the budget has been in surplus. South Africa's revenue benefited from strong economic growth and increasing efficiency in tax collection. The taxation revenues increased steadily from 24.4% of GDP in 2004/05, to 26.6% of GDP in 2006/07 leading to a primary surplus of 3.5% of GDP in 2006/07. The improvement in the fiscal balance has also benefited from lower debt service costs achieved through improved debt management and increased transparency.

The effective debt management strategy has enabled the country to achieve a sustainable fiscal framework, as defined by a decreasing debt to GDP ratio. Domestic debt as percentage of GDP decreased from 30.3% in 2004/05 to 26% in 2006/07. Foreign debt decreased from 4.9% of GDP in 2004/05 to 4.6% of GDP in 2006/07. The improved budgetary performance has contributed to lower interest costs. Government debt and the costs of servicing that debt are expected to fall further in the medium-term. Government's net debt is projected to be 16% of GDP by 2011.

Table 2.2 provides a summary of the central government's fiscal operations. The medium-term budget plan calls for surpluses to continue. The government's fiscal objective in the medium-term is to restrain increases in overall expenditure, sustain the revenue to GDP ratio around 30 per cent and to limit the external debt stock to current levels. For the next three years non-interest public spending is projected to grow by 6.1% a year in real terms, after growth of almost 10 per cent a year over the past five years.

Although the medium-term budget plans assume that the budget surplus will continue, it is recognised that some revenue gains have a temporary character. To accommodate for these cyclical factors, a new measure of the fiscal stance, the cyclically-adjusted budget balance was introduced. The government states that the moderate budget surplus recorded in the present period is the correct fiscal response to these circumstances, and that it represents a strengthening of the state balance sheet in anticipation of future investment requirements and as protection against financial risks or deteriorating trade conditions[14]. The preliminary data suggest a surplus in 2007/08 fact that provides reassurance for the ability of government to meet its commitments and minimise the potential risks or cyclical shifts.

Table 2.2 Central government fiscal operations (R, million)

	2004/05	2005/06	2006/07	2007/08*
Total revenue	347,854	411,748	481,201	557,962
Tax revenue (gross)	354,980	417,334	495,515	571,063
Departmental & other receipts, repayments	6,202	8,559	10,881	11,612
Less: SACU payments	-13,328	-14,145	-25,195	-24,713
Total expenditure	368,459	416,684	470,192	542,117
State debt cost	48,851	50,912	52,192	52,829
Current payments	62,517	69,822	77,979	89,966
Transfers and subsidies	251,746	288,966	333,661	392,277
Payments for capital assets	5,345	6,984	6,360	7,045
Budgetary balance	-20,605	-4,936	11,009	15,845
Extraordinary payments	-9,787	-4,554	-4,214	-771
Extraordinary receipts	2,492	6,905	3,438	1,837
Net borrowing requirement	-27,900	-2,585	10,233	16,911
Financing (net)	27,900	2,585	-10,233	-16,911
Domestic short-term loans (net)	6,132	5,716	5,334	5,750
Domestic loan-term loans (net)	33,409	23,086	892	-4,001
Foreign loans (net)	4,538	518	182	-3,471
Change in net cash/other balances	-16,179	-26,736	-16,640	-15,190
GDP	1,427,445	1,584,743	1,807,316	2,045,533
Total revenue, % of GDP	24.4%	26.0%	26.6%	27.3%
Total expenditure, % of GDP	25.8%	26.3%	26.0%	26.5%
Budgetary balance, % of GDP	-1.4%	-0.3%	0.6%	0.8%
Primary balance, as % of GDP	2.0%	2.9%	3.5%	-0.8%
Cyclically adjusted primary balance[15]	2.1%	2.9%	3.0%	0.1%
Financing (net), % of GDP	2.0%	0.2%	-0.6%	-0.2%
Net loan debt, as % of GDP	33.0%	29.7%	26.4%	22.3%

Source: National Treasury, 2008 Estimates of National Expenditure and Budget Review 2008.

Note: (*) - Revised estimates.

[14] See Budget Speech 2008.

[15] IMF data using tax-specific elasticities to tax-specific base gaps (Source: IMF Country Report No. 07/274, August 2007).

2.2.2 Allocation of resources

ASGISA is the government strategic development framework which aims to raise growth and reduce employment and poverty. The national strategic priorities are translated in 5-year sector strategies and further in the 3-year MTEF and operationalised into the annual budget. Sector budget allocations tend therefore generally to reflect the overall priorities of the government; however the longer-term strategic framework is not developed within fiscal envelope (see PI-12).

The economic expansion since 1999 has allowed public spending to rise rapidly in all areas. The progressive extension of social security has been a central element of the anti-poverty strategy, made possible by the fiscal space created over the past decade. In the last three years however, the share of social services in the overall expenditure has slightly decreased (particularly health and education) in favour of economic services and infrastructure (e.g. transport). As depicted in Table 2.3, the largest functional category of government spending is expenditure on social services (about 36% of total expenditure at the central level). It accounts for more than half of the expenditure on a consolidated basis. The composition of expenditure by functional category in the last years is skewed towards the economic services and infrastructure expenditure[16] (26.3% of total central level expenditure). Overall government expenditure for infrastructure spending will continue to increase between 2007 and 2010. Of this, about 40% will be spent by public enterprises, mainly Eskom (on energy generation, transmission and distribution) and Transnet (on harbours, ports, railways and petroleum pipelines). The 2008 Budget speech stipulates that over the period ahead the government's spending plans allow for a progressive extension of public services.

Table 2.3 Actual expenditure by functional classification (as a percentage of total expenditures)[17]

	2004/05	2005/06	2006/07	2007/08*
Central Government Administration	3.8%	4.0%	3.6%	3.9%
Financial and Administration Services	7.2%	6.2%	6.8%	6.8%
Social Services	37.7%	37.0%	36.0%	35.3%
Justice and Protection Services	30.2%	29.8%	27.2%	25.8%
Economic Services and Infrastructure	21.1%	23.0%	26.3%	28.2%
Total	100.0%	100.0%	100.0%	100.0%

Source: National Treasury, 2008 Estimates of National Expenditure.

Note: (*) - Revised estimates.

Table 2.4 shows the allocation of expenditure by economic classification. Less than 11% of the total expenditure reflects compensation of government employees (i.e. salaries and wages, and social contributions) at the central level. The compensation of employees accounts for about a third of total spending at general government level. The biggest share of salaries and wages are paid through the sub-national governments. The share of transfers and subsidies to sub-national governments (including large capital projects), departmental agencies, public and private enterprises/institutions increased from 68.3% in 2004/05 to

16 Housing and community services are increasingly becoming priority areas.

17 Includes direct charges against the National Revenue Fund (e.g. President and Deputy President salaries, Parliament Members remuneration, skills levy and Setas, Judges and magistrates salaries), but exclude state debt costs and provincial equitable share.

71% of the total expenditure in 2006/07. Growth in payments for capital assets reflects the government commitment to address infrastructure backlogs and accelerate economic growth. Capital spending is projected to expand further to accommodate infrastructure investments in stadiums and public transport for the 2010 FIFA World Cup.

Table 2.4 Actual expenditure by economic classification (as percentage of total expenditures)

	National				Consolidated[18]			
	2004/05	2005/06	2006/07	2007/08*	2004/05	2005/06	2006/07	2007/08*
Current payments	30.2%	29.0%	27.7%	26.3%	59.4%	57.6%	55.7%	54.1%
Compensation to employees	10.9%	10.6%	10.6%	10.5%	33.5%	32.2%	31.3%	31.0%
Goods and services	5.9%	6.1%	6.0%	6.1%	12.9%	13.6%	13.7%	13.8%
Interest and rent on land	13.3%	12.2%	11.1%	9.7%	12.8%	11.7%	10.6%	9.3%
Financial transactions in assets and liabilities	0.2%	0.1%	0.0%	0.0%	0.2%	0.1%	0.1%	0.0%
Transfers and subsidies	68.3%	69.3%	71.0%	72.4%	36.4%	37.7%	39.7%	41.4%
Payments for capital assets	1.5%	1.7%	1.4%	1.3%	4.3%	4.7%	4.6%	4.5%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Source: National Treasury, 2008 Estimates of National Expenditure and National Treasury, 2008 Budget Review.

Note: (*) - Revised estimates.

2.3 Description of the legal and institutional framework for PFM

2.3.1 The legal framework for PFM

The legal framework for PFM in South Africa encompasses a range of laws and regulations that emanate out of the Constitution (1996). The main PFM laws are the Public Finance Management Act (1999), the Municipal Finance Management Act (2003), and the Division of Revenue Act.

Constitution

The South African Constitution (1996) provides the basis for public financial management. It assigns clear roles and responsibilities to the different levels of government (central and sub-national) which are supported by the provisions of the PFMA and MFMA. It gives teeth to performance assurance through Sections 100 and 216 allowing for the intervention by the national government when an entity of government fails to perform an executive function related to financial management, and prescribes circumstances under which the National Treasury may withhold funds.

[18] Consolidated national, provincial and social security funds expenditure.

The key areas pertaining to public finance management include:

- The general guidelines for the regulation of financial affairs of all levels of government (See Chapter 13);
- The role of the National Revenue Fund to which all government revenues must be deposited (See Section 213);
- The allocation of resources between the three levels of government (See Section 214);
- The powers assigned to the National Treasury to prescribe measures to ensure transparency and expenditure control in all government spheres (See Section 216);
- The requirement that public procurement be done in a fair, equitable, transparent, competitive and cost-effective manner (See Section 217);
- Guidance on the issuance of Government's loan guarantees and on disclosure of this information (See Section 218);
- The role of the Office of the Auditor-General (See Section 188);
- The establishment of an independent Fiscal and Finance Commission to advise the Parliament and other authorities on fiscal matters (See Section 220).

Further, the Constitution recognises 11 official languages. It also establishes the Bill of Rights (See Chapter 2) and provides for public access to information as well as the right to appeal on a Department of State's decision.

Public Finance Management Act (PFMA)

The PFMA and its Amendment (1999) detail the financial management regulatory framework for national and provincial government institutions, which include national and provincial departments, and the entities under their ownership or control. The PFMA adopts an output-based and responsibilities-based approach to financial management as opposed to the previous Exchequer Acts rule-driven approach. The Act is part of a broader strategy on improving financial management in the public sector.

The PFMA, in concordance with the Constitution, addresses the National Revenue Fund, the budgetary process, the specification of uniform treasury norms and standards, the institutional arrangements for procurement, the procedures, controls and the application of procurement methods, the pre-requites for the issuance of government guarantees, and the intervention of the national government when a public entity fails to perform.

In respect of budgetary oversight, the PFMA requires parliament to vote the budget estimates by programme rather than departmental votes. It also restricts the powers of accounting officers to move funds between programmes. Such virement is restricted to 8% of the total allocation for a programme. PFMA regulates the borrowing operations of the national government and specifies a single officer authorised to borrow on behalf of any national or provincial government entity. The PFMA sets also clear reporting requirements for in-year budget execution.

Under the current PFM Act Money Bills may only be debated by the legislature but not amended. It has to be mentioned however that one area of PFM reforms (see Chapter 4) relates to amendments to the Legal and Regulatory framework, which includes the introduction of a Money Bill. There is separate draft legislation with respect to amendments to the budget.

Municipal Finance Management Act (MFMA)

The MFMA (2003) is the local government finance management act and adopts the PFMA as its model. It forms an integral part of the broader reform package for local government, as outlined in the 1998 White Paper on Local Government. MFMA aims to modernise budget, accounting and financial management practices of the local government to achieve efficient service delivery to communities. It specifies the approach to be adopted through setting and monitoring outputs, outcomes and measurable objectives. One of the underlying principles of the MFMA is the role to be played by councillors in exercising their oversight role through considering the annual report of the municipality. Given this defined oversight role, and in keeping with a separation of player and referee roles, both the Systems Act and MFMA require that councillors no longer serve on tender committees of municipal entities.

Division of Revenue Act and Intergovernmental Fiscal Relations Act

This Act of Parliament is voted annually to determine the vertical and horizontal allocation of resources. The Division of Revenue Act (DORA) is the subject of policy research and analysis by the Finance and Fiscal Commission, a constitutional body that advises the Parliament and the National Treasury. DORA establishes the annual transfers to provinces and municipalities including the equitable share and the conditional grant share. Both are determined by a well-defined formula. The *Intergovernmental Fiscal Relations Act* (1997) establishes the process of intergovernmental consultation in enacting the Division of Revenue Bill.

Procurement legislation

The requirements for a procurement framework are prescribed in the Constitution and in the PFMA. Guidelines and regulations for procurement are detailed in the *Treasury Regulations, General Procurement Guidelines (2000), Preferential Procurement Policy Framework Act (2001), Framework for Supply Chain Management (SCM, 2003), Guide for Accounting Officers on SCM (2004), Broad Based Black Economic Empowerment Act (BBBEEA, 2003)* and other practice notes. Procurement is a decentralised, with public entities made responsible for managing procurement, and the role of the National Treasury (through the Supply Chain Management Unit) being limited to oversight, regulation, monitoring and evaluation, and capacity development.

Procurement rules are based on five pillars: Value for Money, Open and Effective Competition; Ethics and Fair Dealing, Accountability and Reporting, Equity. Under the current procurement framework the responsibility for procurement is given to the Accounting Officer. The existing legal and regulatory framework does not explicitly establish open tender as the default method for Government procurement.

The *Preferential Procurement Regulations* (2001) establishes the preference point system, and the rules for evaluation of tenders, awarding of tenders not scoring highest points, cancellation and re-invitation of tenders. The BBBEEA promotes broad-based and effective participation of black people in the economy.

2.3.2 The institutional framework for PFM

Legislature

The Constitution vests the legislative power in the Parliament which consists of the National Assembly with 400 seats, and the National Council of Provinces (NCOP) with 90 seats. The National Assembly is responsible for electing the President, passing laws, oversight of the executive and providing a forum where people's representatives can publicly debate issues of national concern. The National Council of Provinces is also involved in the law-making process and provides a forum for debate on issues affecting the provinces. The Parliament has the prerogative to establish Committees that should oversee the activities of the executive. Among these are a number of committees dealing with fiscal oversight:

- *Standing Committee on Public Accounts* (SCOPA) – this committee examines the financial statements as well as audit reports on the statements of all government departments and constitutional institutions. It also examines the Auditor-General's reports, and other financial statements or reports referred to it. It may also initiate any investigation in its area of competence, and may perform other functions related to financial oversight or supervision;
- *Portfolio Committee on Finance* - is responsible for the National Treasury and examines the macro-economic policies of the Government.
- *Joint Budget Committee* - considers the budget in terms of the Medium Term Expenditure Framework in order to allow Parliament to have an input during the process of drafting the budget. It is also responsible for the in-year monitoring of expenditure and oversight of the implementation of corrective actions in response to the SCOPA resolutions;
- *Standing Committee on the Auditor-General* - a parliamentary oversight body to oversee the activities of the Auditor-General and also ensure his independence, impartiality, dignity and effectiveness.

The National Assembly and the NCOP review the Division of Revenue Bill and the Budget Proposal. Under the current law the role of the Legislatures in the budget process empowers them to pass or reject but not amend the budget. There is currently a Money Bill on the floor which if passed will provide the legislature powers to amend the budget.

Executive

The Government apparatus in South Africa is composed of 10 constitutional bodies, 36 national departments, 9 independent provinces and 283 local authorities. The president is both the chief of state and the head of government. The Cabinet is appointed by the President. The executive is accountable for its actions and policies to the Parliament. In the provinces, Premiers are elected in each province and represent the highest authority of the executive.

Judiciary

The Judiciary of South Africa is an independent branch of government. Its independence is guaranteed by the Constitution. The South African court structure consists of the Constitutional Court, the Supreme Court of Appeal, High Courts, Magistrates Courts and other courts established by an Act of Parliament. The Bill of Rights (Chapter 2 of the Constitution) provides for the access to courts and the right to a fair trial. The judicial system of South Africa, as part of the magistrate's court system, includes a number of appeal courts amongst which are Courts for tax disputes, and also for the referral of procurement complaints.

Auditor-General

The office of the Auditor-General is the supreme audit institution in South Africa. It is an independent constitutional body, accountable to the National Assembly. The Auditor-General derives its independence, powers and mandate from the Constitution (Section 188) and the Public Audit Act (PAA), 2004. The Auditor-General is appointed by the President on the recommendation of the National Assembly and approval by the National Assembly with a supporting vote of at least 60% of the members of the Assembly (Section 193 and 194 of the Constitution) for a fixed, non-renewable term of between five and ten years (Section 189). He may be removed from office only with a supporting vote of at least two thirds of the members of the Assembly on the ground of misconduct, incapacity or incompetence (Section 194). The Auditor-General is empowered to audit any and all government entities including security agencies. It must report on its activities and the performance of its functions to the Assembly at least once a year.

Audit Committees

The responsibilities of the Audit Committees are outlined in Section 38(1)(a) of the PFMA and in Treasury Regulation 3.1.13. It consists of four independent members who are required to meet each quarter and ensure that accounting officers have fully responded to the findings of internal audit, external audit and SCOPA. It is also responsible for ensuring that the internal accounting controls are operating to ensure that financial records may be relied upon. It must report on any material breakdown in the functioning of expenditure and accounting controls, procedures and systems that may occur.

The Minister's Committee on the Budget (MinComBud)

The MinComBud is a political committee made up of cabinet ministers that considers key policy and budgetary issues that pertain to the budget prior to their submission to Cabinet for deliberation and approval.

The Medium Term Expenditure Committee (MTEC)

The MTEC is a technical committee which is responsible for evaluating the MTEF budget submissions by the National Departments and making recommendations regarding their allocations to the Minister of Finance.

The Ministers and Members of the Executive Council (MinMEC)

The MinMEC is a political forum where national and provincial departments within a given sector discuss sector policy issues pertaining to the budget prior to the budget being tabled before cabinet. MinMEC is comprised of the Minister of Finance, supported by key Departmental Officials, and the nine provincial Members of Executive Councils.

The Budget Council

The Budget Council coordinates financial relations between national and provincial government. It is comprised of the Minster and Deputy Minister of Finance along with the nine provincial Members of Executive Councils for finance.

The National Treasury

The functions of the National Treasury are detailed in the PFMA. The Minister of Finance is accountable to the Cabinet and Parliament for ensuring compliance of the National Treasury with its responsibilities under the PFMA. The Minister is empowered to delegate the day-to-day operations of the Treasury. The National Treasury is empowered to develop the overall macroeconomic and fiscal framework, co-ordinate intergovernmental fiscal relations and the budget preparation process, manage the implementation of a budget and promote and enforce revenue, manage the government's assets and liability. It also plays a financial oversight role over other organs of state in all spheres of government.

The *Budget Office* is responsible for fiscal policy, public finance statistics (including managing the chart of accounts), and for fiscal policy including the development of the three-year fiscal framework. It is responsible for expenditure planning and guiding the budget formulation process and leads the budget reform programme. It is responsible for policy relating to public service wage bargaining and critical infrastructure planning and budgeting. The Budget Office is also responsible for the *Public Private Partnership* Unit. This is a unit which facilitates and enhances the quality of the public service delivery through offering efficient, effective and value-for-money best practice solutions. In particular, it regulates PPPs, identifies project opportunities, and provides technical assistance in carrying out feasibility studies, procurement and management of the project. Another unit within the Budget Office is the *International Development Cooperation* which coordinates the relationship between the Development Partners and the government recipients. It establishes the policy and strategic framework for the utilisation of ODA, facilitates the establishment and strengthening of ODA co-ordination and management mechanisms, and manages donors' portfolios.

The *Accountant General* is responsible for the accounting of the National Revenue Fund (NRF) and Reconstruction and Development Programme (RDP) Fund, arranging banking services for national Government, developing and implementing accounting policies, and preparing consolidated financial statements.

The *Intergovernmental Fiscal Relations Division* is responsible for coordinating fiscal relations between national, provincial and local government as well as promoting sound provincial and municipal financial planning, reporting and management.

The *Economic Policy Division* is responsible for macroeconomic policy and economic modelling and forecasts.

The *Asset and Liability Management* (ALM) division manages government's asset and liability portfolio. In particular, the division is in charge of asset management, debt and conditional liabilities management, cash management, and financial management and reporting. It is also responsible for oversight of public enterprises. In contrast to many countries where debt management operations is the responsibility of the Central Bank, in South Africa the government's domestic and foreign debt portfolio is managed directly by the ALM division. This division, as part of its cash management operations, trades financial instruments in the money market. The division is in charge of developing and updating a government Funding Strategy which addresses both Loans and Guarantees. A specialised unit deals with risk management; it assesses the credit risk and invests government money.

To describe the division of responsibility between the ALM and the SARB, the decision-making on borrowing and investment is done by the ALM division while the SARB is instructed to implement the decision.

The *Public Finance* Division holds the specific role of liaising with the National Departments on expenditure policy, expenditure monitoring and financial management compliance. It is organised to provide oversight across the different clusters. The PF Division also advises the Minister on the departmental policies.

The *Specialist Functions* is a Division of the National Treasury which regulates and oversees public-sector supply chain management and standardises the financial systems of national and provincial government.

Financial Systems

The National Treasury is responsible for the development of financial management systems for the central and provincial governments. The *State Information and Technology Agency* (SITA) is responsible for hosting systems and managing the network services to the government. It also provides on-going user support to all of the financial management systems. The current system focuses on four main functional areas:

- Payroll and Human Resource Management at national and provincial levels (using PERSAL software);
- Supply Chain Management (using LOGIS software);
- Accounting (using BAS and Safetynet software);
- Business Intelligence Platform.

These systems are based on older technologies and so are rather cumbersome to use, especially with respect to on-line queries and the ease of use of report writers. At the moment about 90% of government network is serviced by SITA while about 10% are localised wide area networks (e.g. the North West province operates a separate data network). Defence and police have their own stand alone networks for security reasons but these are also operated by SITA. In South Africa, all cost centres are on-line; there are no manual transactions. All expenditure data are centralised.

There are extensive private data network across the country that provides for real time banking operations. As a result, cash book data can be reconciled with banking data and so managed efficiently. This is part of the basis for South Africa's impressive cash and debt management. SITA's network is secured and on financial system there is no access to external networks except access to the banks through Safetynet.

The National Treasury's policy towards the use of proprietary rather than off the shelf software packages has provided a certain independency with respect to maintenance, the upgrading and the development of its financial management systems. A disaster data recovery process is in place.

Currently there are ongoing efforts to implement an integrated financial management system (IFMS) which modernises and extends the functionality of the existing systems. It should become fully operational by 2012. The achievements to date include functional specifications of the systems which have been developed.

National Departments

PFMA establishes the Minister as the political head of the department, and the Director-General, the head civil servant and the accounting officer. The Minister or a provincial MEC is responsible for setting policies and is accountable for the achievement of departmental outcomes. This includes seeking legislature's approval and adoption of the department's budget vote. The Director-General of a National Department is responsible for the management of the implementation of the budget and achievement of departmental outputs for which he is accountable to Parliament.

Public Enterprises

A wide spectrum of autonomous government agencies and public enterprises exist in South Africa including in such sectors as energy, communication, transport, health, education, social protection and pensions. The PFMA defines "public entities" as Major Public Entities and National Government Business Enterprises[19]. The PFMA distinguishes 10 Constitutional Institutions (see PFMA, Schedule 1), 20 major public entities (see PFMA, Schedule 2), and another 47 national public entities, 26 national government business enterprises, 100 provincial public entities, 11 provincial government business enterprises (see PFMA, Schedule 3)[20].

The Department of Public Enterprises is the shareholder representative for government. It has the responsibility to oversee the 9 major State-Owned Enterprises (SOEs): Alexkor, Broadband Infraco, Denel, Eskom, Pebble-Bed Modular Reactor (PBMR), South African Airways (SAA), South African Express Airways (SAX), South African Forestry Company (Safcol) and Transnet. Public Enterprises are required to submit to the National Treasury their annual budget and corporate plans prior to the start of the financial year, as well as annual reports and financial statements. The Auditor-General may investigate or audit any government business enterprise or public entity.

South Africa Reserve Bank

The South African Reserve Bank (SARB) has operational independence which is constitutionally guaranteed. As part of its activities, the SARB performs international banking and international treasury services, acts as banker and funding agent of the government and facilitates the effective functioning of the domestic financial markets. It keeps track of all public sector borrowing. The Reserve Bank publishes fiscal statistics and information in its Quarterly Bulletins and Annual Economic Reports.

[19] In this report national government business enterprises and commercial public enterprises are used interchangeably.

[20] The number of public entities at the time of writing of this report may differ from the number referred to in the PFMA.

Table 2.5 Matrix of Institutional Responsibilities for PFM Functions

PFM Function	Cabinet	BC	MinMEC	MTEC	MCB	National Treasury										SARS	National Departments						AG	Parliament					Donors
						MF	DG	BO	PF	IGR	EP	ALM	IA	AccG	SCM		DM	DG	CFO	AO	IA	PU		NA				NCOP	
																								NA	JBC	PCF	SCOPA		
Policy Elaboration and Planning																													
Policy Debate & Budget Preparation		x	x	x	x	x		x	x								x	x	x										
Policy & Budget Approval	x				x																			x					
Loan Approvals						x																							
Supplemental Budgets				x	x			x	x															x					
National Development Plan (NDP)	x																x	x	x										
Sector Strategic Plans						x	x		x		x						x		x										
Annual Corporate Plans						x	x										x		x										
Budget Formulation/Preparation																													
Budget Speech						x																							
Macroeconomic & Fiscal Framework	x				x	x		x			x																		
Estimates of National Expenditure (MTEF)	x				x	x	x	x	x								x	x	x					x					x
Budget Review	x				x	x		x		x		x																	
Medium Term Budget Policy Statement	x				x	x		x																					
Division of Revenue Bill	x				x			x		x														x				x	
National Adjustment Estimates	x	x				x		x	x								x	x						x					
Revenue Administration/Collections																													
Tax Revenue																x													
Grants/Loans						x																							x
Budget Execution																													
Debt Management												x																	
Budget Allocation/Cash Management												x								x									
Virement - votes																		x						x					
Virement - programme level							x																						
Establishment Control																	x	x											
Personnel Rolls																		x											
Payroll																				x	x								
Procurement policy & regulation															x														
Common user items Procurement contracts															x														
Procurement/Supply Chain													x	x				x			x	x							
Non-Salary Recurrent Expenditure													x	x						x	x								
Capital Expenditure								x											x	x	x								
Payments														x						x									
Financial Reporting						x				x			x	x			x			x	x								x
Accounting														x						x									
Internal Audit													x			x					x		x						
External Scrutiny/ Budget Oversight																													
External Audit																							x						
Budget Oversight																								x	x	x			
Procurement oversight															x														
Expenditure/Audit Oversight																									x		x		
PFM Reform																													
Reform Policy/Approval	x					x																							
PFM Reform Coordination/Monitoring						x		x								x							x						

Abbreviations: MF - Minister of Finance, DG - Director General, PF - Public Finance Division, BO - Budget Office, IGR - Intergovernmental Relations Division, EP - Economic Policy Division, ALM - Assets & Liability Division, SCM - Supply management Unit, AccG - Accountant General, IA - Internal Audit, SARS - South African Revenue Service, DM - National Department Minister, CFO - Chief Financial officer, AO - Accounting Officer, PU - Procurement Unit, MCB - Ministers Committee on Budget, BC - Budget Council (Minister & Provincial MECs for Finance), MinMEC - Minister & Provincial MECs of a particular portfolio, MTEC - Cabinet Medium Term Expenditure Committee, JBC - Joint Budget Committee, PCF - Portfolio Committee on Finance, SCOPA - Standing Committee on Public Accounts, NA - National Assembly, NCOP - National Council of Provinces.

2.3.3 The key features of the PFM system

The financial year for central government and provincial governments in South Africa is April 1st to March 31st. For local government it is from July 1st to June 30th. The PFM Act prescribes a concurrent role for central and provincial governments. The central government is responsible for policy, regulation, oversight and monitoring and evaluation. The provincial governments are principally responsible for the implementation of policy and for efficient service delivery. The budget process begins in June. Usually the draft budget, based upon a medium term budgetary framework, is submitted in mid February after the Budget Speech. The annual appropriations law is typically passed by parliament in June or July and enacted into law by the signature of the president. Authority to incur expenditure is facilitated through a draw down schedule agreed between the Departments and the National Treasury.

South Africa has a distributed payments and accounting system operated out of a single National Revenue Fund account set up in the South African Reserve Bank. The country coverage of revenue and expenditure bank accounts is facilitated through the use of bank accounts in one of four commercial banks - ABSA, Nedbank, First National and Standard Bank. There is a country wide data network upon which the financial management software (including payroll management software) systems operate. The payroll systems are managed and operated independently by each of the Departments.

The Government of South Africa adopts a modified cash accounting basis for the preparation of its accounts. The final accounts are prepared by the Departments and a consolidated financial information report by the Accountant General.

The Office of the Auditor-General is independent and has jurisdiction over all government entities including public enterprises. The Constitutions and Public Audit Act authorise the Auditor-General the requisite independence and jurisdiction to receive all documentation necessary to carry out his work and places no restrictions on the publication of his findings. The Accounting Officer is responsible and held accountable for implementing all recommendations emanating out of an audit and SCOPA recommendations. The Audit Committees are responsible for ensuring that there is systematic follow up on Auditor-General findings and SCOPA recommendations.

South Africa is a member of the customs union SACU. Members consolidate all customs revenues and share them on the basis of a formula; paying out custom revenue allocations quarterly. The net effect of the application of the customs revenue sharing formula is the substantial subsidies paid out to other SACU members by South Africa.

3 Assessment of the PFM systems, processes and institutions

3.1 Budget credibility

3.1.1 PI-1 Aggregate expenditure out-turn compared to original approved budget

This PEFA assessment covers the fiscal years 2005/2006, 2006/2007 and 2007/2008; 2007/2008 being the most recent fiscal year for which final appropriations accounts [21] were available at the time of the assessment. The reporting formats of the budget documentation permit an identification of debt service elements. The only donor funds reported in the budget documentation is that which is channelled through the Reconstruction and Development Program (RDP) Fund account. This includes budget support as well as programme and project support. The donor funds[22] managed through the RDP account are identified separately within the financial reporting documentation and so make it possible to identify and measure primary expenditure estimates as well as primary expenditure achievements. The original approved expenditure estimates presented in Table 3.1 were obtained from the promulgation notices of the Appropriations Acts for 2005, 2006 and 2007. The actual expenditures were obtained from the Consolidated Financial Information for 2005/2006, 2006/2007 and the draft financial statements for 2007/2008.

The Government of South Africa has adopted modified cash accounting for its central government accounts with the fiscal year being defined from April 1 to March 31. Outstanding commitments for goods, works and services (i.e. open purchase orders) not delivered by the end of the fiscal year are rolled over to the next budget year and payments are then completed for all outstanding bills (i.e. verified invoices) in the following fiscal year. Outstanding payments that remain so for more than 30 days into the following fiscal year become expenditure arrears. Any uncommitted funds at the close of the fiscal year are returned to the Treasury[23] and are lost by the Department. One

[21] At the time of the field missions only draft final appropriations accounts were available for 2007/2008 and so these were employed in making the computations.

[22] There is a large amount of donor activity managed outside of the budget (see D2). The RDP Fund account represents only a portion of the donor funds expended for which the central government is beneficiary. There is a mix of budgetary support, programme and project funds that are managed through the RDP Fund account. For the three years considered in the PEFA Assessment the expenditure through the RDP fund measured approximately 0.2% of primary expenditure of which only a proportion was budget support. Given that the breakdown of project and programme versus budget support relied upon secondary sources and given the very small proportion of expenditure managed through the RDP account these amounts were not segregated out from the primary expenditure estimates and outturns. This approach allowed for ready reconciliation of the primary expenditure data with budget documentation without materially affecting the scoring.

[23] The PFMA has provisions for the roll over of unspent funds in the case of capital expenditure with appropriate justification and up to 5% in the case of current expenditure. Transfer payments may also be rolled over.

consequence of this implementation of the end of year procedures is that a number of Departments tend towards increased expenditure rates in the last month (referred to informally as the *March spike*) as Departments seek to avoid having to return unspent funds to the National Treasury (see PI-20). This pressure on spending may contribute to the accrual of expenditure arrears, as well as contribute to an increased incidence of direct procurement during the last month. Opportunities are missed to mitigate the pressures that lead to a rush to spend at the end of the fiscal year. The first is the absence of the adoption of procurement plans to inform cash draw-down schedules and consequently expenditure forecasts in a number of Departments, and the second is the absence of the in-year commitment reporting (see PI-24) to better gauge and forecast the rate of budget implementation and thus avoid a rush to spend at the end of the year. Suppliers to the central government appear to be aware of this rush to spend at the end of the year. The Steel and Engineering Industries Federation of South Africa (SEIFSA) tell of its membership lodging complaints on delayed payments from the central government especially at the end of the year and at the beginning of the new fiscal year.

It should be noted though that the central government's role of policy formation, regulation and oversight, and monitoring and evaluation with the consequent domination of expenditures through transfers of grants and subsidies, rather than through payroll and procurement based expenditure does not make these weaknesses readily apparent in aggregate expenditure data considerations. For example the Department of Education spends only approximately seven percent (7%) of its budget through payroll and procurement systems. So accrued arrears or direct procurement purchases, even where significant in terms of the proportion of funds expended through procurement mechanisms pale into insignificance when considered as a proportion of total expenditure. These circumstances become important when considering the significance of arrears levels measured (see PI-4).

The adoption of a cash accounting standard does not strictly match expenditure periods to budget estimate periods as would be the case for say a modified cash accounting that facilitated continuing payments for a limited period extending into the next fiscal year. This would contribute to a tendency for measured actual outturn to be less than budget estimate unless careful procurement planning was taken into account both with budget preparation as well as cash flow planning.

Table 3.1 Comparison of Budget Estimates against Actuals (Primary Expenditure, million R)

	2005/06	2006/07	2007/08
Primary Original Estimate	364,694	420,676	480,957
Primary Outturn	365,848	418,000	487,802
Aggregate Expenditure Deviation, million R	1,154	-2,676	6,845
Aggregate Expenditure Deviation, %	0.3%	-0.6%	1.4%

Source: Estimates of National Expenditure for 2005/2006, 2006/2007, 2007/2008 and Draft Financial Statements 2007/2008.

For all three fiscal years reviewed, the aggregate actual expenditures match the budget estimates to within 5%. In all three budget years, revenues exceeded budget estimates (see indicator PI-3). These results point to South Africa achieving a key pre-requisite to the attainment of both the credibility of the budget as well as aggregate fiscal discipline.

The appropriate interpretations of the result of a comparison of primary expenditure estimates to actual primary expenditure are premised upon the availability of accurate financial data. There are many elements of the PEFA assessment that suggest such accuracy is achieved as demonstrated by the quantum of arrears (see PI-4), the regular and timely reconciliation of bank accounts (see PI-22), the timely and comprehensive financial reporting (see PI-25) and comprehensive external audit (see PI-26).

The RDP account provides an opportunity to match budget estimates to actual expenditure for donor funds. When this is done actual expenditures reflect a small proportion of budget estimates indicating that for such funds, the comparison leads to substantial deviations. This, while an important observation, does not have a significant impact on overall budget credibility because of the very low ratio of RDP funds to overall central government expenditure.

In the three fiscal years reviewed there were no substantive major exogenous factors that significantly impacted on budget expenditure. A significant unforeseeable adjustment of customs revenue emanating from the arrangements of the Southern African Customs Union (SACU) occurred in 2006/2007; however there was no significant impact of expenditure over original approved estimates observed for that year.

No.	Credibility of Budget	Score	Justification
PI-1	Aggregate expenditure out-turn compared to original approved budget	A	Actual primary expenditure deviated from expenditure estimates below 5% for three of the years considered. Deviations were 0.3%, -0.6% and 1.4% respectively.

3.1.2 PI-2 Composition of expenditure out-turn compared to original approved budget

To obtain a measure of how much the reallocations between budget votes have contributed to variance up and above the deviations in the overall levels of expenditure, an analysis of budget deviations between budget estimates and actual out-turns by budget head was performed for the years 2005/2006, 2006/2007 and 2007/2008. The budget to expenditure deviations for each Budget Vote is presented in Table 3.2. An analysis of this table shows that the average weighted deviations improved over the three year period reducing from 5% to 2%.

The low variances up and above the expenditure deviation at the aggregate level and shown in Table 3.3 suggest a strong coupling between the budget formulation and preparation process, and in turn between budget estimate and implementation. It demonstrates that the budget releases are very closely aligned with the vote and that the commitment control procedures are largely effective. While the PFMA accommodates for a supplementary budget process, this does not appear to introduce significant adjustments to the original budget estimates.

The results clearly demonstrate that South Africa's PFM systems have achieved remarkable budgetary discipline, and have the expenditure management systems in place to assure that outcomes are in line with budgetary intent. It should be noted though that the increasing pattern of accrued expenditure arrears observed (see PI-4) serves to undermine the top down budgetary discipline efforts, through weaknesses in expenditure control (see PI-20) arising out of a lack of focus on commitment reporting to facilitate improved expenditure management at the commitment level (see PI-24) and the absence of procurement planning across a number of Departments.

Table 3.2 Comparison of Budgeted and Actual Expenditure (Rand 1,000)

	2005/06		2006/07		2007/08	
	Estimates	Actuals	Estimates	Actuals	Estimates	Actuals
Central Government Administration						
The Presidency	215,456	192,103	258,000	238,428	256,900	267,800
Parliament	885,561	1,713,940	1,011,300	978,325	1,078,100	1,076,000
Foreign Affairs	2,595,071	2,687,711	3,042,100	2,944,679	3,856,400	3,890,100
Home Affairs	2,972,711	3,172,075	2,800,400	2,546,915	3,314,600	3,316,300
Provincial and Local Government	15,580,777	15,976,128	24,903,400	24,575,672	28,844,200	29,959,600
Public Works	5,554,051	2,354,255	3,080,200	3,025,788	3,693,100	3,759,500
Financial and Administrator Services						
Government Comm. & Information	249,130	253,573	288,000	293,108	375,800	38,400
National Treasury	151,218,899	148,392,359	169,424,100	166,923,948	193,979,600	192,171,200
Public Enterprises	91,983	2,671,483	683,500	2,589,835	1,064,000	4,604,100
Public Service Administration	167,726	332,299	325,600	429,354	357,300	382,800
Public Service Commission	82,050	91,054	96,300	96,068	105,400	106,500
SA Management Development Institute	57,047	55,387	58,900	58,268	71,100	131,100
Statistics South Africa	691,257	643,917	1,074,500	1,096,605	1,100,300	1,129,900
Social Services						
Arts and Culture	1,082,699	1,121,025	1,318,500	1,329,934	1,608,000	1,581,000
Education	12,397,064	12,436,807	14,129,200	14,249,805	16,000,900	16,377,700
Health	9,825,237	9,937,084	11,270,000	11,338,047	12,655,100	12,744,900
Labour	6,313,977	6,179,239	7,012,700	6,781,967	8,032,900	8,818,800
Social Development	56,549,127	55,067,840	62,005,460	61,676,087	67,232,100	67,024,900
Sport & Recreation SA	203,628	436,842	352,153	886,548	3,157,200	5,050,600
Justice and Protection Services						
Correctional Services	9,234,085	9,631,216	10,630,712	9,251,186	10,742,300	10,754,400
Defence	22,459,432	23,510,541	23,830,105	23,817,584	25,922,300	26,148,700
Independent Complaints Directorate	49,522	54,506	65,906	65,271	80,900	80,900
Justice & Constitutional Development	5,922,038	5,365,257	7,312,580	7,104,505	8,541,300	7,238,900
Safety and Security	28,456,995	29,360,784	32,557,731	32,521,230	35,917,500	36,386,100
Economic Services and Infrastructure						
Agriculture	1,684,738	1,906,831	1,957,648	2,223,956	2,285,000	3,223,500
Communications	1,017,503	1,034,425	1,280,194	1,319,597	1,423,500	1,881,100

	2005/06		2006/07		2007/08	
	Estimates	Actuals	Estimates	Actuals	Estimates	Actuals
Environmental Affairs and Tourism	1,723,111	1,775,686	2,018,053	2,059,664	2,590,800	2,790,500
Housing	5,191,712	5,248,753	6,860,883	7,165,962	8,877,600	8,080,900
Land Affairs	3,881,513	2,876,896	4,852,196	3,720,489	5,674,600	5,718,900
Minerals and Energy	2,117,585	2,191,613	2,548,272	2,607,675	2,966,100	2,924,900
Science & Technology	1,986,639	2,041,272	2,614,093	2,612,999	3,142,500	3,137,200
Trade and Industry	3,076,331	3,056,440	3,665,912	3,804,720	4,845,600	5,346,000
Transport	7,602,159	10,409,892	12,870,458	13,360,442	15,857,900	16,324,400
Water Affairs & Forestry	3,557,412	3,803,965	4,476,545	4,305,650	5,306,300	5,334,500
Total	364,694,226	365,983,198	420,675,601	418,000,311	480,957,200	487,802,100

Source: Financial Statistical Tables Budget Review 2006, 2007, 2008, Draft Consolidated Financial Information 2008.

Table 3.3 shows the results of the analysis of the expenditure variance by vote. It indicates that the variance in excess over total deviation was 5% or less for all three years reviewed.

Table 3.3 Expenditure composition variance in excess of total expenditure deviation

	2005/06	2006/07	2007/08
Total Primary Expenditure Deviation	5.5%	2.6%	3.3%
Total Primary Expenditure Variance	0.4%	0.6%	1.4%
Variance over Expenditure Deviation	5%	2%	2%

Source: Author's calculations derived from the data presented in Table 3.1 and Table 3.2.

No.	Credibility of Budget	Score	Justification
PI-2	Composition of expenditure out-turn compared to original approved budget	A	Variance in primary expenditure composition exceeded overall expenditure deviation by no more than 5% in any of the years considered. Variance in expenditure composition exceeded overall deviation primary expenditure by 5%, 2% and 2% respectively.

3.1.3 PI-3 Aggregate revenue out-turn compared to original approved budget

The principal sources of domestic revenue were from taxes on international trade and transactions, income tax, and taxes on domestic goods and consumption. In 2006/2007 tax revenue constituted approximately 98% of total government revenue. Customs, Income Tax and VAT constituted 5%, 50% and 27% respectively for a total of 82% of government revenue. Other smaller but significant tax revenue contributions include the general fuel levy (4%) and the taxes on property (2%). Non tax revenue is principally departmental revenues which are approximately 2% of total central government revenue.

A comparison of budgeted versus actual revenues demonstrates actuals exceeding revenue estimates in 2005/2006, 2006/2007 and 2007/2008 by up to 11% but showing a decreasing trend of outturns over estimates over the three years reviewed (see Table 3.4 below).

The Economic Policy Unit of the National Treasury is responsible for the preparation of macroeconomic forecasts. The process of estimating revenues involves the careful consideration of macroeconomic indicators prepared by the Treasury but that also considers independent estimates prepared the South Africa Reserve Bank. Revenue forecasts are prepared by the Revenue Analysis Committee with membership from the Fiscal Policy Unit, the South African Revenue Service (SARS), the South African Reserve Bank (SARB) and headed by the Deputy Minister of Finance. Three year as well as annual revenue projections are made. These are updated on a six monthly basis and incorporated into the adjustment budget. In recent years revenue rates have grown at twice the rate of GDP growth. Of particular challenge to accurate revenue forecasts have been the cyclical dynamics of both the domestic and global markets. In the three years under consideration the South African economy, and consequently its revenue achievements, has outperformed projections. A significant portion of tax revenue is derived from corporate taxes which in turn have been dramatically impacted positively by record high commodity prices. Further, the ramifications of any new Tax policy initiatives are factored in to develop three year revenue forecasts. Revenue forecasts are updated bi-annually as part of the budget process and also feed into the adjustment budget process held in October.

All of that said, the robust revenue performance experienced in recent years has also been due the result of effective tax payer education (see PI-13) and effective tax collections (see PI-15). In recent years the global movements in commodity prices coupled with improvements in tax collections have led to revenue outturns in excess of estimates. These robust revenue profiles have contributed to ensuring credible debt profile forecasts which have positively impacted the cost of money to government (see PI-17) as well as ensured a stellar performance in cash management (see PI-16). Further, the revenue performance has provided the fiscus for meaningful bottom-up participation in the budget preparation process (see PI-11). However, it should be noted that such excess over projection has narrowed fairly dramatically during the period of review.

For the most part the excess of revenues over budget estimates is applied to debt reduction which has shown a steady decline as a ratio of GDP over a number of years. Total debt at the end of 2007/2008 was 26% of GDP.

Table 3.4 Comparison of Budgeted and Actual Revenue Receipts (Domestic, Rand million)

	2005/06	2006/07	2007/08
Revenue Estimates	369,869.50	446,361.70	556,562.00
Revenue Outturns	411,747.90	481,200.70	562,083.45
Deviation, R million	41,878.40	34,839.00	5,521.45
Deviation, %	11%	8%	1%

Source: Estimates from Estimates of National Expenditure 2005/2006, 2006/2007 and 2007/2008; Actual Revenue for 2007/2008 was from draft financial statements.

No.	Credibility of Budget	Score	Justification
PI-3	Aggregate revenue out-turn compared to original approved budget	A	Domestic revenue collection exceeded 97% in all three of the last three budget years. The ratio of aggregate revenue out-turn to original approved budget were 111%, 108% and 101% respectively.

3.1.4 PI-4 Stock and monitoring of expenditure payment arrears

According to Section 8.2.3 of the Treasury Regulations "*all payments due to creditors must be settled within 30 days from receipt of an invoice*" hence an unpaid bill outstanding for more than 30 days after verification of the invoice is deemed to be a payment in arrears. The relatively low levels of indebtedness and the effective commitment control mechanisms might suggest that the accrual of significant levels of arrears does not pose a significant risk. It would further require continuing careful procurement planning and commitment control monitoring and management of in year expenditure to ensure that such risk does not become significant. The Steel and Engineering Industries Federation of South Africa (SEIFSA) state that its membership reports a significant number of cases of late payments on supplies and services made to the central government towards the end of the FY[24].

The BAS system appears to effectively address commitment control. All purchase orders are initiated within the BAS system and controlled by the draw down schedules. In the case of utility payments the Department of Public Works payments for all of the Departments which is then reimbursed. However even the statutory Section 32 in-year reports do not include information on committed expenditure to facilitate effective forward expenditure planning. Neither is such information included in internal in-year implementation reports across all Departments[25]. In spite of the effective commitment controls, the rush of commitments made at the end of the year (with the corresponding rush of supplies to ensure that payment can be made, rather than the unspent funds being returned to the National Treasury) leads to payments being carried over to the next fiscal year as outstanding payments. The component of such outstanding payments that remains unpaid after 30 days are accounted for as expenditure arrears.

The Department-wide and country-wide implementation of the financial management software system, BAS, facilitates the comprehensive tracking of arrears by each spending unit. The annual Consolidated Financial Information disclosure on payables is presented within the financial notes. These are aged (30 days, and plus 30 days[26]) and segregated between current and non-current payables. The current payables are classified as the amounts owed other government entities, clearing accounts and advances received, and other. Through discussions with the office of the Accountant General it was ascertained

24 It should be pointed out that SEIFSA states that this practice is much more rampant at the provincial and local levels, but insist that it remains significant at the central government level.

25 The Department of Education provided evidence that it prepares monthly expenditure returns that include expenditure information both at the time of commitment as well as payment. But this is not the case across all departments.

26 There are also graphs included in the Consolidated Financial Information that show the aging of the expenditure arrears classified as less than 1 year, between one and two years, and over two years.

that the other category covered principally amounts owed vendors and pension and salary arrears.

Table 3.5, shown below, measures the ratio of expenditure arrears to total expenditure; for the three years 2005/2006 to 2007/2008. In all of the three years considered the ratio is considerably lower than 2%. However we note that the year on year change is substantial for the two years shown.

Table 3.5 Stock of expenditure as a ratio of total expenditure (Rand, 1,000)

	2005/06	2006/07	2007/08
Expenditure Arrears	1,676,890	3,054,906	4,610,786
Total Expenditure	365,848,000	418,000,311	487,802,100
Ratio, %	0.46%	0.73%	0.95%
Year on Year Change		59%	29%

Sources: Consolidated Financial Information Report 2005/2006, 2006/2007 and Draft Consolidated Financial Report 2007/2008.

Given the concurrent arrangements of the central government with the provincial governments, and its principal role of providing policy direction, regulation, oversight, and monitoring and evaluation versus service delivery for the provincial governments, the expenditure of the central government is dominated by debt service, transfers and subsidies rather than expenditure managed through payroll and procurement systems. For the central government PFM systems then, it would therefore be more revealing to measure expenditure arrears as a ratio of expenditure arrears to Departmental expenditure rather than as prescribed in the PEFA methodology; namely expenditure arrears to total expenditure. When this is done the ratios are all above 2%. This along with their increasing profile would have translated to a sub indicator (PI-4(i)) score of C. It should be noted that Departmental Expenditure includes substantial conditional grants made to the Provincial Governments and so even Table 3.6 may understate the level of the problem. This analysis therefore reveals some weakness in the area of expenditure arrears management not captured in the prescribed PEFA ratios.

Table 3.6 Stock of expenditure arrears as a ratio of Departmental expenditure (Rand, 1,000)

	2005/06	2006/07	2007/08
Departmental Expenditure	77,327,501	86,891,231	98,437,759
Recurrent Expenditure	70,108,047	80,335,992	90,423,005
Capital Expenditure	7,219,454	6,555,239	8,014,754
Expenditure Arrears	1,676,890	3,054,906	4,610,786
Ratio of Expenditure Arrears, %	2.2%	3.5%	4.7%

Sources: Consolidated Financial Information Report 2005/2006, 2006/2007 and Draft Consolidated Financial Report 2007/2008.

This weakness in arrears management may suggest that there may be important consequences to the absence of procurement planning and commitment reporting (PI-24). The presence of high levels of arrears would typically suggest that a Government is not achieving full value for money with its procurement, as the market would naturally tend to price in the cost of delayed payments. While the Auditor-General has initiated value for money audits, there is at the present time little direct evidence to establish whether or not South Africa at the level of its central government suffers low value for money in its procurement as a direct result of the level of arrears. In discussions with the SEIFSA it was suggested that it was common practice for members to price in the cost of money in response to the anticipated delays in payment especially at the end of the fiscal year.

No.	Credibility of Budget	Score	Justification
PI-4	Stock and monitoring of expenditure payment arrears	A	
(i)	Stock of expenditure payment arrears (as a percentage of actual total expenditure for the corresponding fiscal year) and a recent change in the stock	A	The ratio of expenditure arrears to total expenditure for all three years considered was lower than 2%.
(ii)	Availability of data for monitoring the stock payment arrears	A	Reliable complete consolidated expenditure arrears data is provided as part of the Consolidated Financial Information. The reported expenditure arrears include an aging profile presented graphically.

3.2 Comprehensiveness and transparency

3.2.1 PI-5 Classification of the budget

The Estimates of National Expenditure (ENE), the MTEF budgetary framework, is structured on the basis of administrative, economic, programme and sub-programme classifications. The revenue budget is classified into recurrent and capital revenues, with each segregated by tax type and further by administrative head. Further, revenues are classified as tax and non-tax revenue and by own sources and external grants. This classification is used for formulation, execution and financial reporting of the budget. The programme and sub-programme classifications employed for the budget are used to produce documentation consistent with COFOG at both the functional and sub-functional levels. The chart of accounts for the Central Government budget monitoring is derived from, and is an extension to the GFS 2001 standard and so facilitates ready monthly reports based upon that standard. Since 2008 the chart of accounts has included a field to track the source of funds, and so donor funds can now be individually reflected directly in the budget and financial reporting documentation.

The Public Finance Statistics and the Office of the Accountant General are responsible for evolving and maintaining the chart of accounts and for providing support to Departments and Provinces on the proper assignment of expenditure. Since 2005 the consolidated budgetary account has been extended to allow the incorporation of public enterprises and autonomous government agencies into a single consolidated financial reporting framework. This has been achieved in spite of the difference in accounting reporting standards; modified cash basis for budgetary entities and the accrual accounting standard in the case of extra-budgetary institutions. At this time 70 entities including all major commercial public enterprises constituting approximately 90% of commercial public enterprise expenditure are reflected in the consolidated financial reporting framework.

The institutional arrangements of government reflect the programme/sub-programme structure and so permit clear lines of accountability for delivering on the budgetary programmes. Budgetary reports include presentations using a functional classification based upon 5 clusters and 16 functions. It should be noted that there is very close alignment if not coincidence of the programme structure with a functional structure. The advantages include relative simplicity, and the facilitation of the incorporation of posts directly into programmes. The disadvantages however appear to be a pressure to institute new administrative structures with the introduction of new programmes, and the special challenges that are sometimes presented in defining meaningful output and outcome indicators.

No.	Comprehensiveness and transparency	Score	Justification
PI-5	Classification of the budget	A	The budget formulation and execution is based on economic, administrative, programme and sub-programme classification that can produce consistent documentation according to GFS/COFOG standards at the functional as well as sub-functional level. The chart of accounts is derived from and is an extension to the GFS 2001 standard.

3.2.2 PI-6 Comprehensiveness of information included in budget documentation

The budget documentation presented to parliament includes comprehensive information on the budgetary context, intent and recent financial achievements. The budget is set against a Medium Term Expenditure Framework of the Government's strategic objectives. Only proposed budget estimates are prepared and published in the budget documentation. The approved votes, which never differ from the proposed allocations, are gazetted and promulgated as appropriation acts of parliament. These are made available to Departments and are the basis for the preparation of draw-down schedules (cash flow projections) against which cash management is focused and expenditure is controlled. The MTEF format includes forward estimates (budget year plus two forward years), revised estimates for the year prior to the budget year, actual audited outcomes from three years previous to the budget year.

Budget documentation (2007/2008) is comprehensive, and consists of the following main components:
- The Budget Speech by the Minister of Finance which outlines all new tax policy initiatives and an explanation of their impacts on revenues as well as proposed policies along with the explanation of allocation shifts and expenditure consequences;
- The Budget Review which includes:
  - The economic policy and outlook;
  - The fiscal policy framework;
  - Three year forward revenue estimates;

  - The summary of debt stock and guarantees with one year forward estimates and a profile of contingent liabilities;
  - The division of revenue and intergovernmental transfers;
  - The Macro-economic Framework (three year forecast);
- The Estimates of National Expenditure which contain the votes, programme and sub-programme appropriations with three year forward estimates, as well as the adjusted appropriation of the year previous to the budget along with the audited outcomes for the previous three years. It separately highlights any public-private partnerships that are being undertaken by any of the Departments.
- Also presented to parliament are:
  - The Department Annual Reports that incorporate the audit report and the audited financial statements including statement of financial assets and liabilities, a cash flow statement and the SCOPA resolutions; and the
  - The Medium Term Budget Policy Statement which is submitted to parliament at the beginning of the budget cycle.

The budget speech underscores the policy priorities for the respective budget year. The Budget Review contains the information pertaining to the overall macroeconomic and fiscal framework within which the medium term expenditure framework has been developed. These then form the basis for the Estimates of National Expenditure which contains a range of aggregate data for both three year forward projections for the budget and actual expenditures from three previous years. The Estimates of National Expenditure presents a breakdown by programme and sub-programme of proposed expenditure. The table below summarises the availability of budget information.

Elements of budget documentation	Availability	Notes
Macro-economic assumptions, incl. at least estimates of aggregate growth, inflation and exchange rate	Yes	Estimates for GDP growth, inflation, interest rates, population growth, the exchange rate, and balance of payments position among a host of other assumptions are presented in the macro-economic framework
Fiscal deficit, defined according to GFS or other internationally recognised standard	Yes	Fiscal deficit defined according to GFS is presented in the Macroeconomic Framework
Deficit financing, describing anticipated composition	Yes	The composition by way of domestic versus foreign debt is presented and further the breakdown of domestic debt instruments t be used for financing the debt is described.
Debt stock, incl. details at least for the beginning of the current year	Yes	There is statement of outstanding public debt segregated between foreign and domestic debt which details type of debt.
Financial assets, incl. details at least for the beginning of the current year	Yes	Information on financial assets segregated as current and non-current assets is included in the budget documents which details the categories of financial assets.
Prior year's budget out-turn, presented in the same format as the budget proposal	Yes	Yes, prior year's budget (budget year -2) out-turn is included.
Current year's budget (revised budget or estimated out-turn), presented in the same format	Yes	The estimates of expenditure show the current year's revised budget (budget year -

Elements of budget documentation	Availability	Notes
as the budget proposal		1) in the same format as the budget proposal.
Summarised budget data for both revenue and expenditure according to the main heads of the classification used, incl. data for current and previous year	Yes	The budget includes summarised data according to the main heads of classification for both revenue and expenditure.
Explanation of budget implications of new policy initiatives, with estimates of the budgetary impact of all major revenue policy changes and/or some major changes to expenditure programs	Yes	The Budget Speech outlines all new tax policy initiatives and an explanation of their impacts on revenues as well as proposed policies along with the explanation of allocation shifts and expenditure consequences.

No.	Comprehensiveness and transparency	Score	Justification
PI-6	Comprehensiveness of information included in budget documentation	A	Budget documentation fulfils all 9 benchmarks. The Budget documents are comprehensive.

3.2.3 PI-7 Extent of unreported government operations

One element of government operations which affects fiscal discipline and the efficient allocation of resources is reflected by unreported government expenditure. In general, given their nature, it is difficult to ascertain the full extent of unreported government operations, but every indication suggests that only very insubstantial, if any, unreported extra-budgetary expenditures occur excepting of donor funded programmes and projects.

The Government operates a single treasury National Revenue Fund account controlled by the Treasury. All Departments revenue estimates are reflected in the budget; funds are deposited in the National Revenue Fund and reported on within the budget. This makes unreported expenditure of directly managed Department accounts quite difficult and also unlikely.

While the Government subsidises a number of commercial public enterprises it addresses all subsidies through the budget. It also reports on guarantees. For instance where subsidies are unforeseen, the Government may issue guarantees which allow the cash strapped commercial public enterprises to raise short term funds in the financial markets until the adjustment budget or next fiscal year when the subsidy can be accommodated through a budget process. Officials state that promissory notes, repurchase agreements, sell-backs and other off balance sheet financial instruments are never used to finance subsidies. Consequently, all subsidies are (by the next fiscal year) reflected in the budget.

Intelligence and security activity funds are all reported in the budget even if all the details of expenditure are not disclosed. The Auditor-General reviews and reports on these expenditures. Further the amounts are a very insignificant proportion of the budget.

Convertible IOUs have been employed to cover foreign exchange losses of the South African Reserve Bank in the past to cover debt/equity ration requirements. However, this process when it occurred in 2001 was disclosed on the books of the Reserve Bank, budgeted for and fully reported on as well as being closely monitored by the Auditor-General.

Public Private Partnerships (PPPs) are included at the time of the preparation of sector strategies and are presented within the votes of the Departments that engage in this mechanism for funding projects during the development stage of the PPP. Further quarterly bulletins are published that include the entire list of PPPs along with their Net Present Values. We note though, that while there is disclosure of PPP operations in budget and other fiscal reports, the long term characteristics of the PPP commitment are not yet fully captured.

Finally the process of aggregating the financial Departmental statements into the consolidated financial information includes the application of an aggregate reconciliation mechanism on the sources and uses of funds. This process would reveal any gaps if funds were being diverted to extra budgetary activity.

There is very limited income/expenditure information on grant financed donor projects that operate outside the RDP account held with the South Africa Reserve Bank. Estimates indicate that at least triple the amount disbursed through the RDP account is operated without being reported upon within the budget (see D2 and D3). However, with the donor funded project expenditures measured through the RDP representing significantly less than 0.2% of expenditure it is highly unlikely therefore that total donor funded projects even if several times the amount measured through the RDP account exceeds 1% of total expenditure. For this reason, in spite of very significant proportions of unreported extra-budgetary donor expenditure, this sub-indicator is scored an A.

No.	Comprehensiveness and transparency	Score	Justification
PI-7	Extent of Unreported government Operations	A	
(i)	Level of unreported extra-budgetary expenditure	A	All revenues generated directly by the Departments are transferred to the National Revenue Fund. Intelligence and security agency budgets are reported on, if not in detail. There is no evidence of off balance sheet debt instruments being used to finance subsidies and deferred financing arrangements such as incorporated into public private partnership transactions are reported on within the budget. The consolidation process of the Departmental final accounts includes an aggregate reconciliation process that would reveal any gaps in the sources and uses of funds. The level of unreported extra-budgetary expenditure remains insubstantial.
(ii)	Income/Expenditure information on donor-funded	A	Complete income/expenditure data of donor funded grant projects are not included in budgetary

No.	Comprehensiveness and transparency	Score	Justification
	projects		information. However, reasonable extrapolations of how much donor grant funded expenditure occurs beyond expenditure channelled through the RDP account still suggests the total amount to be less than 1% of total expenditure.

3.2.4 PI-8 Transparency of inter-governmental fiscal relations

There is a two tier structure to Sub National Government (SNG) in South Africa. There are 9 provinces, and 283 local authorities. The Sub National Governments are regulated by the PFMA, the Municipal Finance Management Act (MFMA) and the Division of Revenue Act (DORA). The fiscal year for provinces is April 1st to March 31st coincident with Central Government, and for the Local Authorities July 1st to June 30th. The transfers to the Sub National Government is summarised in Table 3.7 shown below. The Provincial Government transfers in 2006/2007 were 88% of total Central Government transfers to the Sub National Governments. The funds transferred from central government to Sub National Government represent 49% of the Central Government budget.

Table 3.7 Division of national revenue between central and sub national government (R, million)

	2004/2005		2005/2006		2006/2007	
National Departments	167,289	52%	194,723	53%	212,629	51%
Provinces	138,511	43%	154,368	42%	178,871	43%
Local Government	13,808	4%	16,682	5%	26,501	6%
Total	319,608	100%	365,773	100%	418,001	100%

Source: Budget Review 2008.

The transfers to both provinces and local authorities are rule based and transparent. There are conditional and unconditional grants whose allocations are enacted into law through the annual Division of Revenue Act which is always enacted into law prior to the Estimates of National Revenues (ENE) and so can inform the vertical allocations between the tiers of government reflected in it. The conditional grants are based upon sector indicators but based upon past performance indicator achievements and so though conditional remain predictable. The transfers to the local authorities, corresponding to approximately 10% of the SNG transfers are applied solely to capital expenditure. Disbursements are made by the Department of Provincial and Local Government according to a pre-announced schedule of disbursements to all 283 local authorities. The successful cash management implemented by the National Treasury assuring predictable disbursements to provincial government and departments, coupled with the strict implementation of transfers based upon allocations by the Department of Provincial and Local Government results in completely predictable disbursements by the SNG entities. Disbursements to provinces are made monthly. Recently the disbursements to Local Authorities for capital expenditure have been made quarterly because of the high variability in cash requisitions in spite of submitted business and project implementation plans.

The MTEF framework provides firm guidelines for the early preparation of budgets by the Provinces, though minor adjustments may be made after cabinet approval of the bid allocations (up and above the base lines). In the case of the local authorities their later fiscal year calendar (July 1st to June 30th) provides an opportunity to base their budget preparation on the tabled proposed if not approved budgets well ahead of their own budget submittals.

Provincial Governments prepare budgets and financial reports consistent with the National Budget and which is consolidated into a financial report within 5 months of the end of the fiscal year. Local Authorities also prepare financial statements even though there have been some delay in the issuance of audited financial statements for some Local Authorities. The timeliness of the submittal financial statements for audits have improved significantly in recent years. The local authority financials have been consolidated into an annual report (Local Government Budgets and Expenditure Review) consistent with central government fiscal reporting.

The provincial governments submit monthly expenditure returns to the National Treasury that report on the execution of the disbursed funds. The timely and complete submission of these reports is ensured by their submissions by the 15th of the month following the close of the quarter serving as a pre-requisite for subsequent disbursements. Local Authority fiscal information (ex-ante and ex-post) is consolidated into annual reports within 18 Months of the end of the fiscal year. Consequently 58% of SNG fiscal information is consolidated into annual reports within 10 months of the close of the fiscal year and 100% within 18 months (see table below).

The Local Authority entities prepare financial statements based upon a standardised reporting format consistent with central government fiscal reporting which are individually audited by the Auditor-General and submitted to the SCOPA.

Table 3.8 Division of national and own revenue between sub national government (R, million)

	2004/05		2005/06		2006/07	
Provinces	138,511	59%	154,368	58%	178,871	58%
Local Authorities	97,162	41%	112,882	42%	128,106	42%
Total SNG revenue	235,673	100%	267,250	100%	417,380	100%

Sources: Budget Review 2008. Local Authorities – Local Governments Budgets and Expenditure Review 2003/04 – 2009/10.

No.	Comprehensiveness and transparency	Score	Justification
PI-8	Transparency of Inter-governmental fiscal relations (M2)	A	
(i)	Transparent and objectivity in the horizontal allocation among SN government	A	The transfers to Provincial and Local Governments are classified as unconditional equitable share transferred directly to the Provinces, and the conditional share transferred through the Departments. Both components are transparent and rule based and embodied into the annual Division of Revenue Act.
(ii)	Timeliness of reliable information to SN government on their allocations	A	All SNGs are provided reliable guidelines on the budget ceilings through the MTEF process prior to the start of their detailed budget procedures even though, minor adjustments may be made after the budget hearings. While the capital transfers are not made available to Local Authorities at the start of the budget preparation process, their later fiscal years (July 1st to June 30th) allow them ample time to prepare their detailed budgets after their individual allocations have been agreed in the National Budget
(iii)	Extent of consolidation of fiscal data for government according to sectoral categories	B	58% of SNG fiscal information (ex-ante and ex-post) is consolidated into annual reports within 10 months of the close of the fiscal year and 100% within 18 months (see table below)

3.2.5 PI-9 Oversight of aggregate fiscal risk from other public sector entities

The fiscal oversight of public enterprises is carried out by the Assets and Liability Management Division of the National Treasury. The Division assesses the risks to the Government arising from exposure to the Major Public Entities and National Government Business Enterprises[27]. The Division has established an internal ratings scheme which categorises these public enterprises according to their respective risk profiles. The risk analysis incorporates both quantitative as well as qualitative criteria. The qualitative aspects include industry prospects, market position, corporate governance and the quality of management. The quantitative dimensions for establishing risk level rely upon such key financial ratios as return on equity, cost to income ratio, debt to equity, interest cover and EBITDA[28] as well as financial characteristics like turnover and assets.

The Department of Public Enterprises, as shareholder, is responsible for management and operational oversight of the nine largest commercial public enterprises including ESKOM, TRANSNET, ALEXKOR, DENEL, BROADBAND INFRACO, PBMR, SAA, SAX and SAFCOL. The role of the department is to ensure management efficiency for

[27] National Government Business Enterprises are commercial public enterprises.

[28] Earnings Before Interest, Taxes, Depreciation and Amortisation.

these firms to meet domestic and international industry operational standards; ensure the continuing capitalisation to accommodate sustainable healthy growth as a way to contribute to national economic development in a way that supports government policy.

All Public Enterprises submit audited financial statements to the Asset and Liability Management Division and the Office of the Accountant General of the National Treasury annually. At this time 70% of public entities, including all major ones, representing 90% of government resources controlled by Public Entities are consolidated into the Consolidated Financial Information. Hence the budget documentation submitted to parliament includes, in addition to the dividends paid to government and subsidies paid out, the consolidated financial performance of the commercial public enterprises.

The Assets and Liability Management Division require that all Public Entities submit quarterly performance reports that include in year financial implementation figures. However, while the percentage of major commercial public enterprises that submit in-year financial reports has been steadily improving it does not yet cover all major Autonomous Government Agencies (AGAs). Major Public Entities and National Government Business Enterprises may borrow from the financial markets on the authority of their boards of directors but without a written authority issued by the Ministry of Finance. However, National Government Business Enterprises (commercial public enterprises) require explicit approval by the Minister of Finance to borrow (see Section 66(3) of the PFMA).

The Assets and Liability Management Division is also responsible for the oversight and risk assessment of PPPs. It issues a quarterly bulletin that includes a listing of all PPPs. Risk of the PPPs is assessed under the categories of design, finance, build, operate and the transfer of assets back to Government in the cases of a build, own, operate and transfer (BOOT) arrangement. Officials suggest that while risk assessment considerations are comprehensive during the development stage of the PPPs, there is more work to be done to better monitor risk during the operational stage. That bias is partially reflective of PPPs being a relatively new phenomenon in South Africa and so at this time there are very many more that are under development than are operational.

The Sub National Governments cannot generate fiscal liabilities for central government. As stipulated in the PFMA the Government may only borrow money that binds the National Revenue Fund with the authorisation of the Minister of Finance. The issuance of a guarantee requires the authorisation of the responsible Cabinet minister with the concurrence of the Minister of Finance. The Central Government (Section 31 of the Municipal Finance Management Act) may not issue guarantees to Local Authorities.

By this clause in the act, while both Provinces and Local Authorities may borrow money, fiscal liabilities that emanate out of such arrangements cannot generate fiscal liabilities for the central government. Of course this would not constrain the central government from intervening in a Sub National Government entity for political reasons; but this would be a policy choice rather than a response to a liability transfer to the central government.

Provincial financial reports are consolidated into budget statistical tables (See Annexure B, Budget Review). All local authorities issue audited financial statements. In 2008 the second Local Government and Expenditure Review was published by the National Treasury. This report includes a consolidation of financial and debt information, and also provides an assessment of fiscal risk. In addition to directly integrating provincial budget performance into National Treasury Reports, the National Treasury issues the Provincial Budgets and Expenditure Review that summarises the provincial finances.

No.	Comprehensiveness and transparency	Score	Justification
PI-9	Oversight of aggregate fiscal control	B+	
(i)	Extent of central government monitoring of AGAs/PEs	B	All Public Enterprises submit audited financial statements to the central government. All Major Public Entities are consolidated into the Consolidated Financial Information. While there is a requirement for the submission of quarterly fiscal reports, this is not yet being adhered to by all Major Public Entities.
(ii)	Extent of central government monitoring of SN governments' fiscal position	A	SNGs cannot on their own authority generate fiscal liabilities for the central government. Any loan that binds the National Revenue Fund requires the written approval of the Minister of Finance. The fiscal position including the level of outstanding debt is consolidated into the Local Governments Budgets and Expenditure Review, and the Provincial Budgets Expenditure Review.

3.2.6 PI-10 Public access to key fiscal information

Fiscal transparency will depend on whether information on the budget and its execution by the government is easily accessible to the general public or at least the relevant interest groups. Such transparency requires that the Government makes relevant information widely available in a comprehensive, understandable and timely fashion.

Public access to key fiscal information is underpinned by the *Constitution* (1996)[29]. It also stipulates that this information should be timely, accessible and accurate to foster transparency of public administration[30]. The *Promotion of Access to Information Act* (2000) lays down the procedures for accessing information from government as well as from private bodies. It seeks to promote transparency, accountability and effective governance of all public and private bodies. With the view of protecting state interests or the privacy of a natural person the Act properly places some restrictions. Restrictions are in particular on information relating to private individual tax records maintained with the South African Revenue Service and information pertaining to the security services, and

[29] See Chapter 2 Bill of Rights, Section 32.
[30] See Section 195.

the economic and financial welfare of the Republic[31]. Nevertheless, the Act provides for the disclosure of this information when public interest prevails[32].

The information available to public covers the entire budget cycle i.e. budget formulation and planning, budget execution, and external scrutiny and audit. Public access to key fiscal information in South Africa is transparent, generally comprehensive, user-friendly and timely. The main source of information is the internet[33], though relevant information is also made available through other means such as university libraries and printed media. Further to promoting public access, the website of the National Treasury offers the possibility for the public to comment on draft documents. It also includes a section "*Tips for Trevor*" where the public can send their direct comments/tips to the Minister of Finance. The importance of dissemination of fiscal information is recognised by both the government as well as the public.

Budget documents are made available to the public at the time they are tabled by the Minister of Finance in the Parliament. Parliamentary sessions on budget discussions are open to the public and are broadcasted on national TV and radio. The budget is also broadly discussed in the printed media. Following the Budget Speech in the Parliament, a succinct and easy to read version of the Budget called "*People's Guide to the Budget*" is published in print and on the National Treasury website in five languages.

In-year execution reports and audit reports are routinely made available through the National Treasury and Auditor-General Office website. The Auditor General's Manual on the Promotion of Access to Information Act (PAIA)[34] provides guidelines on the provision to the public, free of charge, of a number of reports including annual reports of the AG, audit reports of national departments, public entities, provincial departments, general reports on provincial, national and local government audit outcomes and others. Resolutions on audit report findings are also made available to the public.

With regards to public information on procurement, there is a Tender Bulletin published weekly where bids for procurement are announced. This is accessible via National Treasury website or with subscription. There is a Tender information Centre located in the National Treasury and also a helpdesk for telephonic inquiries. The Supply Chain Management Unit of the National Treasury publishes the awarded contracts on its website.

Elements of information for public access	Availability and means
Annual budget documentation when submitted to the legislature	Yes - these are made available to the public through the internet and public libraries when it is submitted to the legislature. The annual budget documentation includes all elements mentioned in PI-6.

31 See Sections 35, 41.
32 See Section 46.
33 See the following websites: National Treasury - www.treasury.gov.za; Auditor-General Office - www.agsa.co.za; Parliament - www.parliament.gov.za; SARB - www.reservebank.co.za; South African Revenue Service - www.sars.gov.za.
34 See Section 2.

Elements of information for public access	Availability and means
In-year budget execution reports within one month of their completion	Yes - the public has ready access to regular and reliable information on budget implementation. These are made available to the public within one month (15 days) of their completion.
Year-end financial statements within 6 months of completed audit	Yes - these are made available immediately upon completion. Departmental information is made available within three months after the end of the year; consolidated information within 5 months.
External audit reports within 6 months of completed audit	Yes - The Consolidated Financial Statement and the Audit Report are made available typically within 7 months after end of fiscal year and within 1 month of completed audit. Other audit reports are made available upon their completion.
Contract awards (app. USD 100,000 equivalent) published at least quarterly	Yes - contract awards above R 80,000 are published on the National Treasury website. Nevertheless, the information is not segregated by contract amount and there is no overall list of awarded contracts but rather individual contracts. The information is published once the contract has been awarded.
Resources available to primary service unit at least annually	Yes - these are made available to the public through the Provincial Budgets and Expenditure Review (see PI-23).

No.	Comprehensiveness and transparency	Score	Justification
PI-10	Public access to fiscal information	A	All of the six listed elements of information are made available to the public access via the web and other means. The exception is the information on resources available to primary service units.

3.3 Policy-based budgeting

3.3.1 PI-11 Orderliness and participation in the annual budget process

South Africa's budget process adopts a medium term expenditure framework (MTEF). The role of the medium term expenditure framework, premised upon a three year rolling macro-fiscal framework, is programme prioritisation, the efficient re-programming of resources and programme implementation control. Further it serves as a firm budget allocation guideline for the management of departmental revenue collection and expenditure. The chart of accounts is fully aligned with the budget structure. Both the recurrent and capital budget preparation is integrated into a single budget process managed by the National Treasury.

The budget procedures are guided by a definite budget calendar and budget circulars submitted in July which are clear and serve as useful preparation guidelines that are generally adhered to. The calendar allows for the meaningful completion of Departmental budgets. The top-down budget process is disciplined by the macro-fiscal framework which emerges out of careful economic as well as policy considerations, as well as a bottom-up process based upon sector strategy priority considerations. The bottom-up process may also take into account the Apex priorities highlighted in the State of the

Nation address as was done specifically for the 2008/2009 fiscal year. Some officials suggest though, that these introduce too much of a "*flavour of the year*" aspect to the justification of Departmental bids for additional funds up and above the previous year's MTEF estimates for the current year.

It should be noted that in South Africa the budget never gets its final approval until after the fiscal year has begun even though the budget is always presented four to six weeks prior to the end of the fiscal year. In practice approval of the budget occurs three to four months after the start of the fiscal year. For the fiscal years 2005/2006, 2006/2007, 2007/2008 the Appropriations Act was signed into law in July. All expenditure must be preceded by an authority to incur expenditure through the issuance of a General Authorisation Warrant upon approval of the appropriations bill. Pending the General Authorisation Warrant a continuation warrant for up to 33% of the previous year's budget is issued to facilitate on-going expenditure.

No.	Policy-based budgeting	Score	Justification
PI-11	Orderliness and participation in the annual budget process	B	
(i)	Existence of and adherence to a fixed budget calendar	A	A clear annual budget calendar exists that is generally adhered to and the calendar allows six to eight weeks for Departments to meaningfully complete their detailed estimates of revenue and expenditure. There is also sufficient time for Departments to re-programme approved bids (up and above the base line) after the approval by cabinet of the bid allocations.
(ii)	Guidance on the Preparation of budget submissions.	A	The National Treasury issues comprehensive and clear budget circulars for an integrated recurrent and capital budget process. The previous MTEF allocations serve as firm budget allocation guidelines but may be subject to usually relatively minor adjustments through a bid process up and above these allocation guidelines. The bid allocations are approved by Cabinet. Such approval of finalised ceilings allows Departments about a further 4 weeks to incorporate any amendments.
(iii)	Timely budget approval by the legislature.	D	In the three years reviewed under this assessment, the budget was signed into law after two months after the start of the fiscal year.

3.3.2 PI-12 Multi-year perspective in fiscal planning, expenditure policy and budgeting

South Africa has adopted a multi-year perspective to its budget formulation process which accommodates a direct integration of some elements of strategic content into the budget through the linkage to the five year Medium Term Strategic Framework using Sector Strategies and Annual Operation Plans. The MTEF is based upon three year rolling aggregate forecasts. The forecasts are allocated on the basis of cluster, economic and program classifications. These multi-year estimates are directly linked to the annual budget ceilings and are updated annually on a rolling basis. Forecast sector and cluster expenditures estimates serve as budgetary ceilings in the budget preparation process.

The Government has evolved a very careful debt portfolio and funding strategy that establishes a fixed versus floating rate domestic debt ratio; has been extending and smoothening the maturity profile of its debt instruments; sought to minimize debt service costs (subject to acceptable risk levels) and limiting the foreign debt to total debt ratio. The Government articulates its debt management strategy as part of its broader fiscal policies in the Budget Review where it sets, under the Assets and Liability Management chapter, its net borrowing targets over a three year prospective frame. Such projections detail the domestic and foreign components as well as the breakdown between short term and long term debt. Debt sustainability analysis is carried out by the National Treasury annually and the risk benchmarks and debt portfolio projections presented in the Budget Review. Debt sustainability is assessed in terms of the risk benchmark range of 20% to 25% of GDP for the foreign loan component (currently at 14.4%). In the case of domestic debt, a risk benchmark of 70:30 for fixed to non-fixed debt is adopted with a current performance of 75:25. Two other risk factors are considered and assessed. These are currency compositions of the debt and contingent liabilities. The calculus of debt sustainability is also addressed through considerations of international investor service sovereign credit ratings such as by Moody's, Standard and Poors and Fitch.

The implementation of the debt management strategy has led to a number of positive outcomes including declining budget deficits (as a % of GDP), declining government debt (as a % of GDP), declining debt service costs, increased diversification of funding instruments, a smooth redemption profile of domestic bonds and increasing sovereign credit ratings.

The South Africa Reserve Bank also carries out Debt Sustainability Analysis on an ongoing basis, and publishes its assessment of debt sustainability on both external and domestic debt in its Annual Report. According to bank officials the low debt to GDP ratio currently at 22% makes the calculus of debt sustainability straight forward and almost obvious.

The Medium Term Strategic Framework with a five year planning horizon, aligned with the political election cycle, defines the national strategic direction. All of the Departments prepare Sector Strategies (5 year planning horizon) aligned with the national strategic framework. Departments also prepare annual operational plans. However, the preparation of sector strategies does not generally occur within aggregate fiscal forecasts and for at least several major sectors are not costed. Even where they might be costed they exclude forward linked recurrent expenditure impacts. As noted below the sector strategies guide the inclusion of programmes and projects into the three year medium term expenditure framework. This link appears to be qualitative rather than quantitative.

In contrast, the National Treasury managed MTEF process involves the inclusion of investments that take into account forward linked recurrent cost implications. The Capital Committee, responsible for overseeing the inclusion of new investments in the MTEF, requires full life cycle cost considerations and focuses particularly on maintenance costs.

It is also responsible for removing completed projects from the base line to facilitate the reallocation of resources within the MTEF.

The Departments select projects based upon program priorities that are determined by the Sector Strategies. The Medium Term Budget Policy Statement defines the broad national policy direction over a five year horizon that shapes the prioritisation schedule of sector strategy programmes that are incorporated into the MTEF. The Apex priorities announced in the State of the Nation's address may, as was done for the 2008/09 FY, define the political areas of focus that also inform the prioritisation process for inclusion of sector strategy programs and projects into the MTEF.

No.	Policy-based budgeting	Score	Justification
PI-12	Multi-year perspective in fiscal planning, expenditure Policy and budgeting	B	
(i)	Multi-year fiscal forecast and functional allocations	A	Forecasts of fiscal aggregates are prepared for three years, including the budget year. The forecasts are directly linked to subsequent budget ceilings and include functional/sector classifications.
(ii)	Scope and frequency of debt sustainability Analysis	A	DSA for external and domestic debt is carried out every year by both the National Treasury as well as the South Africa Reserve Bank.
(iii)	Existence of costed sector strategies	D	Sector strategies exist for all Departments. These though are not developed within a broad fiscal frame and even where costed never include forward linked recurrent cost implications.
(iv)	Linkages between investment budgets and forward expenditure estimates	A	The selected investments have links to the National strategy framework through the linked sector strategies even though such links are qualitative. The selection of investment is based upon sector and program priorities; however they may also be influenced by the political objectives expressed for example through the Apex priorities included in the State of the Nation address as was done for the 2008/09 FY.

3.4 Predictability and control in budget execution

3.4.1 PI-13 Transparency of taxpayer obligations and liabilities

The South African Revenue Service was created as a government department in 1996 by the SARS Act. It incorporates all tax administration into a single entity. The SARS Act brought SARS into existence as an administratively autonomous entity in 1997. The principal acts governing SARS are: Customs and Excise Act, Estate Duty Act, Income Tax Act, Skills Development Levies Act, Stamp Duties Act, Transfer Duty Act, Unemployment Insurance Contributions Act and Value Added Tax Act. South Africa is a member of the Southern Africa Customs Union (SACU). The member countries pay their customs proceeds to an account held with South African Reserve Bank and then on the basis of a formula funds are allocated and disbursed each quarter. The net effect of the formula is a subsidy by South Africa to other SACU members.

SARS seeks to ensure that taxpayers are properly educated about tax liabilities and obligations, supported to register and comply and only where that fails do they take any necessary administrative enforcement measures. This, it would seem, has enabled SARS to consistently perform well on revenue collection. There is evidence of increasing compliance reflecting a society's maturing attitudes towards taxation.

Income Tax and VAT
SARS's Legal and Policy Division facilitates the uniform and correct application of the legislation through the issuance of Interpretation Notes, drafts for public comments and the introduction of an Advance Tax Ruling (ATR) system that aims at promoting clarity, consistency and certainty in the interpretation and application of the tax laws. The South African Chamber of Commerce and Industry (SACCI) confirms this process and considers it important that civil society is provided the opportunity to comment, however it believes that insufficient time is allowed for full and complete commentary.

SARS organises annual tax information campaigns. During 2006/2007 a total of 2,755 workshops were run; of which 910 were for income tax and 359 for VAT. It also carries out comprehensive consultative processes prior to introducing any new laws and regulations. These campaigns are also aimed at non registered tax payers and demonstrate the rationale, benefits and consequences for not complying. The complete set of tax legislation is available on the Internet. There are also publications, forms and tools to educate and to assist on filing tax returns that provide practical information on tax liabilities and administrative procedures, including the procedures for administrative dispute resolutions. A Help Desk, on-line support and mobile offices are available during the tax return period to ensure that taxpayers receive clear guidance and support for filing. SARS also makes use of all available means of communication such as print media, radio, television, text messaging and billboards. The principal language for the large corporate payers is English. SARS has translated tax return forms into five of the eleven official languages of South Africa to facilitate tax filing. The selection of languages is the result of balancing considerations of expressed needs with considerations of cost effectiveness against the acknowledgment of all eleven official languages. The South African Chamber of Commerce and Industry (SACCI) describes the tax information available on SARS website to be comprehensive, accessible and helpful.

While there are some discretionary powers provided to SARS in the waiving of application of rates and waivers on penalties these in practice are strictly limited by policy documents and procedures. In the cases of penalties they are either applied automatically or the highest penalty permitted by the law (200%) is applied. Any lower rates can only be accessed by a tax payer in default by way of a pre-assessment submission for consideration by the Penalty Committee or through an objection and a full appeal process. There are currently efforts to encode these administrative penalties into law. For Income tax, penalties are automatically applied for late filing. Any debt due and penalties (other than late payment penalties) accrue interest. No principal owed or interest accrued between the assessment and the date of dispute settlement can be waived. The taxpayer may lodge an objection and present a case to reduce the penalties. For VAT, penalties are applied for late filing automatically and the debt due and penalties (other than late payment penalties) accrue interest. Similar to income tax no interest accrued between the assessment and the date of dispute settlement can be waived off and no tax principal can be waived. All waivers of tax as part of the settlement of a dispute have to be reported to the Auditor-General, to the Minister of Finance and to the National Assembly to ensure full transparency and external and public scrutiny of tax waiving and dispute settlement.

Where there are objections to assessments and penalties applied dispute resolution may be pursued. This is strictly controlled by written policies and procedures and a hierarchical referral mechanism. The administrative tax appeal is a two stage process: objection and alternative dispute resolution. An objection can be submitted directly by a taxpayer to SARS. SARS has internal procedures to determine whether an objection can be immediately allowed (as in such cases as calculation error or clear error in law) or if it is to be disallowed. If disallowed, the taxpayer may appeal through the Alternative Dispute Resolution (ADR) process. All tax assessments include a notice that the taxpayer has the right to object and appeal. Where the taxpayer does not accept the resolution of the ADR process the case is referred to a judicial process through the Tax Court. The SARS publish a guide to the objection and appeal for taxpayers. Data on objections and appeals lodged are maintained and permit disaggregating the information by period, procedures and tax type. The table below shows the appeals processed.

Table 3.9 Statistics on Appeal Cases (number of cases)

Appeals stage	2006/07	2007/08
Opening Balance	615	687
Received	1,199	428
Settled	1,127	345
Closing balance	687	770

Source: SARS internal reports.

Customs

There is clear legislation and procedures with respect to Customs duties and excise tax. The complete set of customs and excise legislation is available on the Internet. There are limited discretionary powers with respect to the application and waiving of penalties and interest. In the case of determining customs duties the Customs Officers have no discretion on how duties are set and very limited discretion in how duties are applied. The tariffs are clearly specified for different classes of goods, supported by publicly available manuals. Values are based upon a self declaration process based upon commercial invoices. The values are compared against a standard pricing database. The volumes and item specifications are verified on a sample basis using x-ray scanners and physical inspection. There are post clearance procedures that use separate inspectors to check on volumes and item specifications after the goods have been cleared. The combined procedures do not provide for much discretion in the application of duties.

The clearing of goods may only be done by registered accredited clearing agents and direct importers and exporters. The accreditation process involves extensive education on customs procedures including the procedures for administrative dispute resolutions.

Customs forms are available on the SARS' website. There is also information on clearing procedures and requirements.

Where there are objections to assessments on imported goods the importer may submit an internal administrative appeal to SARS. The appeal mechanism in the case of customs includes appeals on the application of tariff classifications and the penalties applied. The appeal is to separate panels at the customs branch office where the decision was taken, the relevant regional office, or the Head Office of SARS, depending on the nature and value of the dispute. Where the taxpayer does not accept the resolution of the internal administrative appeal process the taxpayer may appeal through the Alternative Dispute Resolution (ADR) process. If the ADR process does not resolve the dispute the case may be referred to a judicial process through the High Court.

No.	Predictability and control in budget execution	Score	Justification
PI-13	Transparency of taxpayers obligations and liabilities	A	
(i)	Clarity and comprehensiveness of tax liabilities	A	For all major taxes the obligations are well specified in the Acts and in regulations. The SARS issues specific public information that ranges from general guidance to detailed sector, entity and tax specific documents. Waiving of tax, penalties and interest is subject to policy notes and rules detailed in manuals and any waiving has to be reported to the Auditor-General, the Minister of Finance and the National Assembly.
(ii)	Taxpayer access to information on tax liabilities and administrative procedures	A	For all major taxes SARS provides education and support to taxpayers and has made it a priority to provide information that is as accessible and clear as possible. The website contains a set of useful regulations, documentations, guides and tools. A help desk and call centres during the filing period are also in place to respond to public demand for information. SARS also makes use of all available mass communication means such as print media, radio and television, text messaging and mobile offices. All new legislations and regulations are subject to a wide consultative process.
(iii)	Existence and functioning of a tax appeals mechanism	A	For all major taxes SARS applies an administrative appeal mechanism referred to as the Alternative Dispute Resolution process. Clear policies and rules have been developed. A guide on the appeal system has been published by SARS and data available demonstrates that the system is operational and that appeals receive due attention.

3.4.2 PI-14 Effectiveness of measures for taxpayer registration and tax assessment

Income Tax and VAT

There are three main registry files within the complete tax database system. These are the Income Tax file registry, the VAT file registry and the Customs file registry. There are direct links between the customs database and the VAT database based upon Customs IDs and VAT IDs. Customs was responsible for the collection of 50% of net VAT revenue during the 2006/07 fiscal year. There are also direct links between Income Tax and the VAT databases. These separate links facilitate a link between the Customs Registry files and the Income Tax Registry files. All registered tax payers require bank accounts whose account numbers serve as direct links between the government registration systems and the financial sector. All foreign investments by individuals require the issuance of tax clearance certificates and hence provide an indirect link to individuals investing offshore to the tax registration databases. The Income Tax Registry file is linked to the Registrar of Companies database. Further, SARS maintains a strong linkage with the Financial Intelligence Centre to enable the bidirectional flow of reports on suspicious transactions. The refund on VAT payments is always subject to checks against third party databases. While these arrangements constitute a set of comprehensive direct links, they are not integrated into a single set of control index files and still remain convoluted. SARS as part of its modernisation programme shall integrate all of the tax registration databases to increase efficiency. It is planned that the systems' integration shall be finalised before year-end, 2008.

In South Africa tax evasion, whether through fraudulent declarations or non-registration is a criminal offence with the associated penalties including fines and prison terms. The Penalty Committee that reviews decisions with respect to penalties may refer a case to the Enforcement Unit for criminal investigation if there is evidence of a deliberate attempt not to disclose information honestly. However where there are mitigating circumstances such as where the person is unaware of the tax infraction the penalties are limited to administrative penalties. In the case of employees tax, provisional tax and VAT the penalty applied for late payment is 10% and for non payment of Income Tax and VAT up to 200%. Interest is automatically applied to the unpaid amounts including the penalty component. The interest rates applied are tied to Treasury Public Finance Management Act rates. These are not set to further penalise but to compensate SARS for deferred collection. Although these penalties act as deterrence and are consistently administered the legislation empowers SARS to seize the monies held by non compliant taxpayers. The links of the tax registries to bank accounts makes it practical to seize whatever monies are paid into the tax payer's account. SARS has a clear policy to enforce payment and has developed the capacity to do so thus providing a strong disincentive for taxpayer to contravene the regulations. In the opinion of SACCI the tax penalties and the consistency with which they are applied serve as an effective deterrence to non-compliance with registration and tax declaration.

The planning and monitoring of tax audit programs have been segregated into two separate functions. The selection of entities to be audited carried out through an independent Business Intelligence function and the audit of the tax paying entities carried out by the Tax Audit Unit. The Business Intelligence function addresses selection on the basis of risk assessment. The Tax Audit Unit is required to audit all and only the entities selected through independent Business Intelligence considerations. This ensures separation of duties and independent selection of auditees. The risk assessment is informed by such factors as volume, history of company, information derived from previous audits, assessment of likely legal loopholes for a given industry, liquidations as well as on the basis of random sampling. A hotline also allows leads from the public to be investigated.

The Audit Unit establishes an annual audit work plan based upon the selections made by the Business Intelligence. The annual audit plans are prioritised by sectors and tax type. Targets are clearly set against which monitoring can be carried out. The audit work is very structured and relies on assessment of the necessary skills required to adequately perform the audit and then on an allocation of resources to Team Leaders. Each assessment is subject to an independent review to control quality and correctness. Fraud investigations are carried out by the Enforcement Unit in reaction to audit triggers and thus rely on the audit findings. Enforcement campaigns are also designed to focus on specific sectors. All tax audit assessments are reviewed by the Business Intelligence to utilise the information and feedback for their risks assessment.

Customs

As stated above, the customs registration database is linked to the other tax databases through its integration with the VAT database. In this way it is directly linked to other government registration systems and to the financial sector through the inclusion of bank accounts for all entries. Only registered importers and exporters can import and export. Specific procedures exist for foreign operators.

In South Africa customs fraud through such means as under-declaration is a criminal offence with the associated penalties including fines and prison terms. The penalties for underpayment (in terms of the internal penalty policy guideline) range from a fixed amount to 25% of the underpayment or value of the goods depending on the categorisation of the offence. Interest is automatically applied to the unpaid amounts excluding the penalty component. Although these penalties act as deterrence and are consistently administered the legislation empowers Customs to detain, seize and render goods held by non compliant taxpayers liable to forfeiture. Where under-declarations are found, claims may be made against the Clearing Agent.

Customs carries out post clearance inspections and audits within 24 hours of clearing, except where post clearance inspections of goods cleared on the high seas must await landing of the goods. Similar to Income Tax and VAT, the Business Intelligence is also responsible for the selection of importers to be subjected to audit. The selections are both targeted focusing on particular sectors, history as well as random. The Post Clearance Audit Unit establishes an annual audit work plan based upon the selections made buy the Business Intelligence. The audit work plans are detailed and comprehensive. Each assessment is subject to an independent review to control quality and correctness.

No.	Predictability and control in budget execution	Score	Justification
PI-14	Effectiveness of measures for taxpayer registration system	A	

No.	Predictability and control in budget execution	Score	Justification
(i)	Controls in taxpayer registration system	A	Taxpayers are registered in databases for income tax, VAT that have direct links with each other and with the Registrar of Companies and through the inclusion of bank accounts with the Financial Sector. The Customs database is linked to the Income Tax through VAT.
(ii)	(ii) Effectiveness of penalties for non-compliance with registration and declaration obligations	A	Penalties for all major taxes are set high enough to deter against non compliance with registration and filing. In addition SARS is empowered to bond the businesses revenues and bank accounts to cover any unpaid tax liabilities.
(iii)	(iii) Planning and monitoring of tax audit and fraud investigation programs	A	Tax audit and fraud investigation are based upon clear risks assessment criteria undertaken independently by the Business Intelligence. Audits are carried by the Audit Unit on the basis of cases prepared by the Business Intelligence. Reports are used to provide feedback from audits to risks assessment and for fraud investigation. The Customs post clearance inspections and audits are also selected independently by the Business Intelligence.

3.4.3 PI-15 Effectiveness in collection of tax payments

Income Tax and VAT

The level of tax arrears in South Africa is high but has been steadily decreasing as a percentage of tax revenues. In absolute terms it has stayed relatively constant in recent years suggesting that current collections are fully effective; but that historically there have been tax arrears collection difficulties. It is anticipated that a portion (maybe as much as a half) of these tax arrears are to be written off. The table below shows a computation of the gross tax collection to the debt stock at the start of the year. This ratio is low and remains less than 60% (the threshold for a D rating) for all the fiscal years presented. In contrast though, a measure of the current arrears collection rate (defined as the ratio of actual tax arrears collected to the gross increase in tax arrears) is also presented in the table and shows that SARS current arrears collection rates to be high and averages approximately 90%. SARS debt collection utilises specialised teams for cases older than 24 to 48 months, 49 months and large cases (i.e. greater than R 1 million). In spite of this performance on its current collections PEFA scores a D for sub-indicator PI-15(i).

There are a number of factors that affect the stock of tax arrears that impact upon the scoring. First, officials report that approximately half the debt stock is uncollectible old arrears and should be written off. Maintaining uncollectible tax arrears on the books contribute a very significant distortion to the measure of debt collection when coupled with the automatic interest that accrues even on uncollectible arrears. With historical accrued interest rates high, currently 15%, the arrears stock rises faster than revenue increases. Consequently without regular write-offs of arrears deemed uncollectible the arrears stock would continue to rise faster than tax arrears collections. Second, the stock of tax arrears include amounts in dispute. The basis for classifying payments as in arrears is largely automatic and includes immediate entries on the completion of audits without a dead period to ascertain whether an objection by the tax payer is to be made with resolution to be different from the auditor's assessment. Given the long periods for the resolution of tax objections, a compliment to the thoroughness of the tax appeals system, any adjustments to the debt stock are delayed while the unadjusted amount continues to accrue interest. Third, the booking of VAT arrears is done retrospectively to a date prior to the date of establishing the VAT arrears. This interpretation arises due to the tax entity merely collecting on behalf of SARS. The upshot of which is that the opportunity to collect VAT arrears is delayed and allows, in a given year, a shorter period to collect the booked tax arrears.

Table 3.10 Current Accumulated Debt Collection Ratio

	2005/06	2006/07
Due Debt (R, billion)	60	64
Revenue Collected (R, billion)	417	495
Debt: Revenue Ratio (%)	14%	13%
Gross Change in Debt Stock, (R, billion)	18.5	21.7
Actual Collection in year (R, billion)	20.5	17.7
Collection ratio	111%	82%
Ratio of collected debt arrears/ debt stock	33%	30%

Source: Calculations based on data from SARS Annual Report 2006/07[35].

The transfer of revenue collected is reliant on the national data network and benefits from an efficient and well developed country wide banking system. Revenue collection is facilitated by the four major banks in South Africa namely ABSA, Nedbank, First National and Standard. These banks participate in the cash management function of central government. All balances at these participating banks are cleared to the National Revenue Fund on a daily basis. SARS operates in excess of 180 bank accounts.

For Income Tax and VAT there are a number of ways for filing and paying taxes:
- To any one of the four banks' branches that deal with SARS;
- Payment to a SARS branch office;
- Mail to a SARS Branch;
- Using a drop box;
- E-filing.

Irrespective of the filing method, the processing remains the same. Payments are processed separate from filings but linked by tax payers ID and bank details. Payments are processed immediately and cash deposited into the SARS bank account for same day transfer to the Treasury. Payment deposits and transfers are done daily on the next business day. All direct deposits and office deposits are processed and transferred to

35 Note that for the purpose of the computation the gross change in debt stock is calculated as the difference between successive years debt stock plus actual collections during that fiscal year.

Treasury for same day value at the end of each business day. The filings are entered into the SARS database, but may require two to three days for completion of data capture. Electronic reconciliation between assessment as filed and payment received can then be done against payments received. Returns are processed separately and accounted as a debit until reconciliation with the payment. In practice the reconciliation between the payment made (credit) and the return filed (debit) occurs on average within three days. SARS capacity enables processing of approximately 300,000 returns per month.

E-filing treatment is similar to the manual process but facilitates direct access to the SARS system for generating the assessment debit and recording in the SARS G/L the electronic payment transfer simultaneously for real time reconciliation. Approximately 55% of income tax filings employ e-filing. The payment is processed by the banking systems that are recorded on SARS: the two processes are then reconciled. The process is real time.

Customs
In the case of customs tax arrears are very low and only arise as a result of internal audit findings of payment discrepancies for which recovery procedures have been initiated and for any fines levied by Customs arising from improper or incomplete customs declarations. Customs arrears are stated to be a very small proportion of custom's revenue collection. No segregated collection data on customs tax arrears collection was available during the field assessment.

The transfer mechanism of revenue collected by Customs is efficient and has effective controls. It is reliant on the national data network and benefits from an efficient and well developed country wide banking system. All customs outposts are directly on line and are able to deposit cash on a same day, daily basis to a bank branch.

Customs revenue collection is done using four banks in South Africa: ABSA, Nedbank, First National and Standard Bank. Their selection is based on appropriately high net worth to reduce risk. The Treasury Single Account (TSA) incorporates a mirror account bank mechanism which places a TSA mirror account in the headquarters of each of the four banks. Thus transfers of revenue from a branch reduced to same day transfers of cash from branch accounts to headquarter accounts of the same bank. The mirror account of the Treasury Single Account is then immediately credited. SARS controls 180 bank accounts directly over the country through their special agreement with the four banks and can access all bank transactions on its computer systems (SAP).

The reporting and reconciliation mechanisms are based upon computerised receipting and cash book systems. For customs, two separate systems are used for the cash book and receipts: CAPE is used for nearly all ports and where CAPE has not been deployed the CCA is utilised. On a daily basis the cash book entries are submitted electronically to the centralised systems and reconciliations made with cash payments received. This mechanism allows the system reconciling between receipts and deposits recorded by the Banks as well as between deposits and transfers to the Treasury Single Account. Reconciliations are done on a daily basis but reporting is monthly.

No.	Predictability and control in budget execution	Score	Justification
PI-15	Effectiveness in collection of tax payments (M1)	D+	
(i)	Collection ratio for gross tax arrears, being the percentage of tax arrears at the beginning of a fiscal year, which was collected during that fiscal year	D	Although the collection of current debt is strong and well managed, historical debt is significant and not reduced. The total debt stock stands at 13% of revenue collection in 2006/07 and the collection ration is less than 30% in the last two years.
(ii)	Effectiveness of transfer of tax collections to the Treasury by the revenue administration	A	SARS operates a very efficient collection system that enables an effective transfer of tax collection to the Treasury Single Account daily.
(iii)	Frequency of complete accounts reconciliation between tax assessments, collections, arrears records and receipts by the Treasury	A	Reconciliations between tax assessment and collections and between collections and receipts by the Treasury are done daily. Reporting is done monthly in Section 32 within 30 days of the close of the month.

3.4.4 PI-16 Predictability in the availability of funds for commitment of expenditures

The strict top-down discipline imposed on the budget by the fiscal framework, the very successful debt management and cash management, coupled with the implementation of BAS across all Departments has provided the basis for achieving substantial predictability with respect to budget releases and the commitment of expenditures. An annual general authorisation warrant (authority to incur expenditure) is issued by the Minister of Finance on the authority of and in accordance with the appropriations bill. The annual General Authorisation Warrant is informed by Draw-down schedules which are annual pro forma cash flow statements submitted to the National Treasury at the beginning of the fiscal year but which may and are updated on a monthly basis to take into account actual expenditure rates. The so informed Draw-down schedule is used to set expenditure ceilings at the vote and programme level on an annual basis within the BAS. The cash management carried out by the Asset and Liability Management Division of the National Treasury (see PI-17) in addition to the draw-down schedules considers the revenue collection profiles (SARS and Departmental) and the debt forecast based upon forecast new borrowings and debt maturity profiles meets the requirements of the draw down schedule. This near perfect predictability in disbursements therefore serves as the basis for sound commitment control.

South Africa’s budget operates under a reasonably broad fiscal space and so has been able to carry out its budget releases without cash constraints. While debt management and cash management are stellar it should be pointed out that given the very high proportion of predictable transfers and subsidies complimented by highly predictable salary payments within the central government budget, including within the Departments, the disbursement schedules remain for the most part very steady and thus allows for better cash planning even where procurement planning and commitment control reporting remain absent. The Accountant General is responsible for making payments against the agreed payment schedules.

All receipts are made directly out of the National Revenue Fund held with the South African Reserve Bank. The Treasury also maintains a Reconstruction and Development Program (RPD) Fund account through which donor grant funds that are to be managed by the Government are placed. Funds managed directly by Development partners are maintained in Commercial Bank accounts but in accordance with the PFMA require authorisation of the National Treasury prior to being opened. In practice though this is largely ignored which leaves the government with not knowing the status of many of its accounts (though not managed by it) not being reconciled or regularly being reported on to the Government.

There are no facilitation accounts. Departments deposit all revenues in the National Revenue Fund and all payments are based upon a centralised system that is managed by the Accountant General. The Treasury has daily access to the National Revenue Fund bank account balance and reconciles the balance with the cash book twice a day to facilitate both its disbursements commitments as well as to support its money market trading activities.

The single National Revenue Fund bank account not only facilitates accurate and timely information on the daily status of the account, it also ensures that the Government does not have to borrow money while it has idle cash sitting in its accounts. All Departmental cash balances are swept into the National Revenue Fund and are traded by the National Treasury on the money market using a variety of deals including switches and repurchase agreements in addition to primary issues. This diversity of deals provides for the requisite liquidity to facilitate cash management in perfect response to the Departmental requisitions.

Adjustments to budgetary allocations should be made by normal ex-ante virement procedures; or possibly by issuing a Supplementary Budget, once or so within the year; or alternatively it may occur by ex-post regularisation of unauthorised spending. In South Africa, virements between programmes for less than 8% of the programme allocation do not require ex-ante approval beyond the Department Minister. Above 8% it requires ex-ante supplemental budgetary approval. There is an annual adjustment (supplementary) budgetary process in October. Given the built in expenditure controls in the BAS financial management system spending ceiling rules cannot be exceeded (without a misallocation of expenditure). Hence virements are always applied ex-ante subject to the authority of budgetary allocations.

No.	Predictability and control in budget execution	Score	Justification
PI-16	Predictability in the availability of funds for commitment of expenditures (M1)	A	
(i)	Extent to which cash flows are forecast and monitored	A	Draw down schedules (cash flow forecasts) are prepared annually by the Departments. The Treasury informed by the pro forma cash flows and cash availability projections allocates funds on an annual basis by entering Draw Down Schedules at the vote,

No.	Predictability and control in budget execution	Score	Justification
			and programme level. These are updated monthly based upon updated cash flow projections. It is not clear that across all Departments the pro forma cash flows are prepared on the basis of detailed procurement plans.
(ii)	Reliability and horizon of periodic in-year information to Line Ministries on ceilings for expenditure commitment.	A	Departments are provided with an annual Draw-down schedules that reflect the annual Budget Forward Plans. These allocations are updated on a monthly rolling basis.
(iii)	Frequency and transparency of adjustment to budget allocations, which are decided above the management of Line Ministries	A	Due to effective budgetary allocation controls, all programme virements must be made subject to the approval of the National Treasury not exceeding 8% of programme estimate. Any re-allocations above this requires the approval of parliament .Typically an Adjustment Budget is submitted once a year in October.

3.4.5 PI-17 Recording and management of cash balances, debt and guarantees

According to the PFMA the Minister of Finance is the sole authority for the contracting of loans that bind the National Revenue Fund. Guarantees may be authorised by the Department's Minister but only at the concurrence of the Minister of Finance. When the Minister of Finance Borrows, he does so within the constraints of the three year fiscal forecasts which set clear debt targets and are published in the Budget Review which is one of the budgetary documents tabled before Parliament. South Africa's stock of debt is low and is currently at 26.4% of GDP.

The National Treasury has evolved a debt strategy over the past decade that has succeeded at integrating debt and cash management; improving transparency with highly positive consequences regarding market risk perception and the subsequent gains with respect to the government's cost of money; establishing a risk management function that has set clear benchmarks for government debt including the domestic debt to GDP ratio, the foreign debt to GDP ratio, the contingent liability to GDP ratio; the fixed versus floating rate domestic debt ratio and extending and smoothing the maturity profile of the debt portfolio to reduce refinancing risk. There has also been a more conscious and clear separation of fiscal policy (managed by the Treasury) and monetary policy (managed by SARB) with separate debt instruments. The result of this effort has been market discernment of the different categories of debt instruments with corresponding price differentiation.

The Assets and Liability Management Division within the National Treasury are responsible for managing debt and do so with a full panoply of debt instruments (bonds, treasury bills, inflation linked bonds, floating rate bonds) and trading deals (primary issues, repurchase agreements, switches). Off the shelf debt management software such as the Commonwealth Secretariat Debt Recording and Management System (CSDRMS) has been considered and found wanting especially with regards to supporting the range of deals managed. At the present time a fairly outdated but robust system ARABAS is employed primarily for recording and data storage, with Excel worksheets used for front end extraction, analysis and reporting. Comprehensive records on domestic and external debt are compiled and are updated and reconciled on a monthly basis. The reconciliation is done on the basis of internal consistency checks as well as reconciliation with the bank statements from the lending institutions. The debt stock and debt service are reported and published on the National Treasury website as part of the PFMA Section 32 reporting requirements. Comprehensive statistical reports providing information on debt stocks, debt service and debt management operations are also prepared quarterly and published by the South Africa Reserve Bank. The Assets and Liability Management Division monitors all domestic and external debt. It reports comprehensively each month on debt stock levels, debt maturity profiles, creditor and currency compositions.

The near real time recording and management of cash balances within the Treasury Single Account held with the South African Reserve Bank provides a critical component both for managing budget disbursements to the Departments as well as serving as an important information input to the trading function for managing borrowings as well as assets carried out by the Assets and Liability Management division within the National Treasury. There is the RDP Fund account which is used for managing donor funded projects. This account is managed in a way similar to the Treasury Single Account with positive cash balances swept into trading accounts to facilitate trading. Interest accrued is applied to the balances of the different donors.

There are a number government accounts, usually held in commercial banks, to facilitate the implementation of donor funded projects which remain outside of this arrangement. These arrangements adopted by most of the Donors operating in South Africa do so without specific authorisations as required by the PFMA of the National Treasury. It should be said that for the most part the donor projects are discussed with the International Development Co-operation (IDC) Division within National Treasury, but these projects remain outside of the formal budget process or the cash management (reconciliation and reporting) arrangements. While progress reports on project implementation are provided to the IDC and annual financial statements are submitted each year, there does not appear to be any regular process for consolidating these accounts into the Consolidated Financial Information.

The contracting of loans and the issuing of guarantees are bound by transparent criteria. Targets are set within the MTEF and the Debt Management Strategy sets clear benchmarks which are monitored and reported on in the Budget Review. The payments system utilises the National Revenue Fund for all payments on Government expenditure (except for grant and loan funded project accounts). This facilitates a monitoring mechanism that reports and reconciles the account on a daily basis.

No.	Predictability and control in budget execution	Score	Justification
PI-17	Recording and management of cash balances, debt and guarantees	A	

No.	Predictability and control in budget execution	Score	Justification
(i)	Quality of debt recording and reporting	A	Comprehensive records on domestic and external debt are compiled and are updated and reconciled on a monthly basis. Comprehensive statistical reports providing information on debt stocks, debt service and debt management operations are prepared on a monthly basis.
(ii)	Extent of consolidation of the Government's cash balances	B	The payments system utilises the National Revenue Fund for all payments on Government expenditure (except for a number of grant funded project accounts). This facilitates a monitoring mechanism that reports and reconciles the account on a daily basis. All other outside of the RDP Fund account do not appear to be reported on even though progress reports and financial statements are submitted to the IDC on the implementation grant funded projects.
(iii)	Systems for contracting loans and issuance of guarantees	A	The contracting of loans and the issuing of guarantees are bound by transparent criteria. Targets are set within the Budget Review. Debt Management Strategy sets clear benchmarks. Debt is monitored and reported on against the strategy targets.

3.4.6 PI-18 Effectiveness of payroll controls

The Department of Public Service Administration is the regulator for human resources. It develops human resources management policy, regulations, and norms and standards for national and provincial governments, relevant ICT infrastructure with the objective to improve service delivery. The Public Administration Act has recently been amended to provide for additional powers for the Department of Public Service Administration in order to more closely control the budgeting and utilisation of public monies for personal management and to perform head counts. The Public Service Commission is an independent oversight body that reports to the National Assembly and carries out annual impact surveys. The Departments are responsible for implementing the policies and enforcing the regulations at national and provincial departments.

It is a requirement of the Public Service Administration Act that new posts established receive ministerial approval and must be reflected in the budget. Temporary posts are subject to budgetary constraints. The establishment is the basis for budget formulation and preparation process pertaining to wages and salaries. New employee recruitment requires Accounting Officer approval. Promotions can only be effected through the transfer of one post to another, thus introducing a degree of control over arbitrary promotions. An employee has to apply for a new post in order to get a promotion. Allowances are also attached to posts which serve as an effective control on. Terminations, especially vacations of post without notice, are effectively controlled by monthly supervisor signed verification sheets and the automatic stoppage of salary payments for any person absent from post for more than 30 days without appropriate notification. Strict links are in place between authorisations and control entries to the payroll management software (PERSAL). Once changes are authorised, only the personnel controller is authorised to effect them on PERSAL, a proprietary software developed in South Africa and used for payroll management of over a million employees across the country for all Departments and Provinces. PERSAL directly links three databases: establishment of posts and personnel database that serve as control files, and the payroll database. All civil servants are registered through PERSAL that include appropriate fields to protect against duplication.

All payments are made directly to bank accounts. No cash payments are made to staff whether permanent or temporary. Each Department directly manages posts and personnel changes. Controls and procedures exist for all changes. Audit trails are built-in in the system. The database is encrypted and cannot be accessed directly outside the application. Personnel Officers have secured access to the database by password controls with three tiers of access recognised; data entry, supervisor and salary. Exception reports are issued each month and used to identify anomalies and any extreme changes from one pay period to the next.

Any changes and updates to the payroll management databases are done monthly, almost always within the next pay period and there is rarely the need for retroactive adjustments, and where so do not extend beyond two pay periods.

The Internal Audit Unit and the Auditor-General performs payroll audits to verify the correctness of the establishment ran on PERSAL for each department. PERSAL allows ad hoc switching from electronic payments to cheques so that specific physical audits may be organised, especially for remote spending units. In the last payroll audit carried out in the Department of Works, out of 5,000 people 5 ghost workers (people who had left, but salary payments had not been stopped) and no double dippers were identified in the past three years. Information Technology audits are performed by the Internal Audit Units and the Auditor-General. This assessment concludes that the likelihood of losses is minimal and that is corroborated by the Auditor-General's opinion as well as the Internal Audit Units interviewed.

No.	Predictability and control in budget execution	Score	Justification
PI-18	Effectiveness of Payroll Controls	A	
(i)	Degree of integration and reconciliation between personnel records and payroll data	A	The application used in South Africa, PERSAL, allows for a direct link between the establishment and personnel and the payroll databases. Salary, promotions and allowances are criteria attached to a post, not to a person thus ensuring effective control.
(ii)	Timeliness of changes to personnel records and the payroll	A	Payrolls are controlled monthly and changes are effected within the next month pay period. Retroactive changes are rare and almost never extend beyond two pay periods.
(iii)	Internal controls of changes to personnel records and the	A	The types of changes that can be made are restricted. Only authorised persons are granted access through

No.	Predictability and control in budget execution	Score	Justification
	payroll		passwords to PERSAL. All entries create an audit trail. All payrolls have to be verified monthly by the employee's supervisor.
(iv)	Existence of payroll audits to identify control weaknesses and /or ghost workers	A	Payroll audits are conducted routinely by the Internal Audit Unit and specific audits are performed by the Auditor-General. PERSAL has features that support physical audits.

3.4.7 PI-19 Competition, value for money and controls in procurement

The Constitution (see Section 217) imposes the core principles underlying public sector procurement as fairness, equity, transparency, competition and cost-effectiveness. The PFMA specifies that the National Treasury has the responsibility for designing policies and regulations on public procurement for all levels of government. Government's procurement policy, legal and regulatory framework also includes the Preferred Procurement Policy Framework and the Broad-Based Black Economic Empowerment Act. The Supply Chain Management Unit provides procurement policy, regulations and oversight.

The Act or Regulations do not clearly establish open competition as the default procurement method, with a requirement to justify less competitive methods when used. Section 16A6 of the Treasury Regulations sets a lower bar for open competition. It merely requires that procurement be constrained by threshold values; and where impractical permits the Accounting Officer to procure the required goods or services by other methods, providing that the reasons be recorded. The National Treasury issues annual instructions on the applicable procurement thresholds. Open Tender is compulsory for all procurement requirements estimated to be equal or greater than 500,000 Rand. It appears that the basis for the use of other methods and the justification requirements are not adequate to curb practices that aims at circumventing competitive methods. Practice Note SCM 6 of 2007/08 issued by the Supply Chain Management Unit aimed at clarifying the application of other means of procurement (See PI-20).

Both the Institute for Democracy in South Africa (IDASA) and the Steel and Engineering Industries Federation of South Africa (SEIFSA) report on a perception of public procurement being fair, responsive to open competition and broadly accessible. Their concerns were about the ability of the central government procurement systems to provide quality works and services. Both highlighted the construction of housing as a case in point. It was not possible to obtain Department wide data on the proportion of tenders above the open tender threshold which were carried out using the open tender method. LOGIS, the transverse system employed for monitoring procurement, is used in less than half of the Departments at central and provincial level and consequently only partial procurement data can be consolidated. A tender register is also maintained manually in each department. The Department of Health provided information for the year 2007/2008 which shows that in the last two fiscal years more than 80% (see Table 3.11) of all tenders above the Open Tender Threshold were procured through an Open

Tender procedure. This would seem to suggest that there is a high level of compliance, however procurement data nationally aggregated could not be obtained and so sub indicator PI-19(i) is scored a D.

Table 3.11 Department of Health: Statistics on procurement requirements for the years 2006/07 and 2007/08

Department of Health Procurement Requirements	2006/07	2007/08
N° of Procurement Requirements	298	117
N° of Procurement Requirements above the Open Tender threshold*	66	34
N° of Procurement Requirements above the Open Tender threshold which were not procured through Open Tender	11	4
% of Procurement Requirement above the Open Tender threshold which were procured through Open Tender	83%	88%

Source: Department of Health.

The administrative complaint mechanism is a two-stage process. First a complaint may be lodged by the vendor to the Accounting Officer of the Department or directly to the Appeal Board of the Supply Chain Management Unit, Specialist Functions Division of National Treasury. A judicial complaint mechanism may also be lodged through the Directorate of Complaints of the Ministry of Justice. The Public Administration of Justice Act gives the right to appeal on any decisions of a Department. Complaints to the Supply Chain Management Unit are recorded and data obtained indicates that 43 complaints were filed in 2006/2007 and 2007/2008 nationally. In all cases, the complaints received a response and had either been closed, referred to a higher authority or were awaiting reply from the complainant. The complaints log is however not accessible to the public.

Public Private Partnerships are regulated by the National Treasury Regulations as a procurement method and are subject to a strict series of control and approval. The PPP Unit of the National Treasury provides support and guidance to the Departments and maintains transparency through quarterly and annual publications on future and on-going PPPs.

No.	Predictability and control in budget execution	Score	Justification
PI-19	Competition, value for money and controls in procurement (M2)	D+	
(i)	Evidence on the use of open competition for award of contracts that exceed the nationally established threshold for small purchases	D	There is no central registry for procurement requirements and awards but the data generated by LOGIS, the procurement proprietary software, is stored in the Business Intelligence Platform of Treasury. Data was not retrieved during the assignment. Evidence submitted by the Department of Health suggests high level of compliance but this is insufficient to draw a conclusion on the national statistic.
(ii)	Extent of justification for use of less competitive procurement	D	The Act or Regulations do not clearly establish open competition as the default procurement method, with a

No.	Predictability and control in budget execution	Score	Justification
	methods		requirement to justify less competitive methods when used. There is some indication that there is occasional abuse of emergency as a reason for circumventing competitive methods without adequate justification at year end when expenditure is rushed in a bid to prevent unspent funds being returned to the National Treasury.
(iii)	Existence and operation of a procurement complaints mechanism	B	A complaints mechanism exits and is functional. The Supply Chain Management Unit keeps a record of complaints and resolutions. Complaints are systematically responded to in order to settle matters or refer the case to a higher authority. Resolutions are not accessible to public scrutiny.

3.4.8 PI-20 Effectiveness of internal controls for non-salary expenditure

Internal control within a Department is the responsibility of the Accounting Officer (See Section 39 and 40 of the PFMA and Chapters 8 and 15 of the Treasury Regulations). He or she must ensure that internal procedures and internal control measures are in place. Further he or she must provide reasonable assurance that all expenditure is necessary, appropriate, paid promptly and is adequately recorded and reported.

The budget execution is initiated by the National Treasury approval of the Draw-down Schedule based upon annual cash flow projections of the Department. These projections are updated monthly and are reviewed by the Public Finance Division within the Treasury. Any deviation in draw down in excess of 5% of the plan has to be explained by the Department. Commitment control is effective and limits expenditure to available cash. The Basic Accounting System (BAS), a transverse system based on proprietary software and operated across the country at the national and provincial levels of government, includes a commitment control function. Procurement is linked to expenditure through LOGIS (another transverse system based upon proprietary software) that requires commitment clearance before a commitment can be made. Specific manual procedures with suitable commitment and fiduciary controls exist for hand written orders to be placed in emergency circumstances such as power outages. There is also the facility for deferred regularisation on BAS. Section 43 of the PMFA limits the virements between programme votes to 8%, subject to Treasury approval but without a priori approval by the legislature. In practice the Treasury has waived its right of approval.

A request memo signed by the Head of Unit authorises procurement initiation. However there is no requirement for procurement plans to serve as a control and link to the budget through the draw-down schedules. Very large procurement requirements are however directly identified in the operational plans of the departments. Other controls on the expenditure chain include: the requirements for VAT Invoices and Tax Clearance Certificate for each vendor prior to signing a contract, thus effectively controlling that the public sector only does business with duly registered and tax compliant businesses; a

Simultaneous Receipt and Issue voucher issued to certify receipt and verify the invoice; and the approval of payment vouchers which require the full range of supporting documentation. The utilities and housing expenditures are controlled by the Department of Public Works. This arrangement has avoided the accumulation of arrears by the central government towards the utility companies.

The integration of other expenditure procedures into the BAS has contributed to a streamlining of expenditure procedures and enhanced the effectiveness of controls. The expenditure management rules and procedures are clear and accessible through Treasury Regulations, manuals and circulars. Interviews with a wide variety of officials left an impression that there was familiarity with the rules and procedures. The expenditure procedures have appropriate documented control procedures employing effective separation of authorities. Department Tender Committees supported by technical specification and evaluation committees are responsible for bid announcement and vendor selection.

The Internal Audit Units met during the review all indicated that compliance to internal controls is generally high although there was also acknowledgement that lapses seem to rise during the "*March spike*". There exists a characteristic increase in February/March when departments increase significantly their procurement and consequently expenditure levels. Rules are generally complied with in a significant majority of transactions but use of simplified situations is an important concern as highlighted in National Treasury Practice Note of 2006/2007, a regulatory note, which states that "*Despite Treasury Regulation 16A6.4 being intended for cases of emergency or where goods and services are available from sole service providers, it has come to light that institutions are deliberatively utilising this provision to circumvent the required competitive bidding process in order to among others, enter into contractual commitments or incur expenditure at the end of a financial year with the view to avoiding the surrender of unspent voted funds to the National/Provincial Revenue Funds*". According to the Auditor-General the extent of the problem for the National Departments appears to be less serious than for the provincial level. The PFMA Implementation Unit indicated the quality and extent of the existing procedures are not considered as adequate in all Departments. Therefore it has initiated a capability assessment practice based on a tool developed in Canada to categorise each department on a scale and determine the necessary support in terms of institutional capacity building.

No.	Predictability and control in budget execution	Score	Justification
PI-20	Effectiveness of internal controls for non-salary expenditure (M1)	C+	
(i)	Effectiveness of expenditure commitment controls	A	Commitment control is a requirement of the PFMA and specific procedures have to be developed by Departments for all internal controls. The accounting software (BAS) provides a sound basis for ensuring an effective commitment control.
(ii)	Comprehensiveness, relevance and understanding	A	Other internal controls are well covered in the PFMA and the Treasury Regulations and manuals.

No.	Predictability and control in budget execution	Score	Justification
	of other internal control rules/ procedures		Integration between the accounting and procurement management software support the application of rules. Departments have developed policies and procedures which are widely understood.
(iii)	Degree of compliance with rules for processing and recording transactions	C	Although compliance to rules is generally considered high according to the Internal Audit Units there are important concerns about the abuse of procurement rules to circumvent the use of competitive methods during what is referred as the March spike.

3.4.9 PI-21 Effectiveness of internal audit

The PFMA (Sections 38(1)(a), 76(4)(d) and 77) and the Treasury Regulations (Chapter 3) specify the internal audit function as a compulsory requirement for all Departments. The oversight of internal audit and assurance of full implementation of audit findings (internal and external) as well as SCOPA recommendations is the responsibility of Audit Committees. The Audit Committees mandate is to review the effectiveness of internal controls and internal audit, to review the risk areas and to ensure that internal and external audit recommendations are duly addressed and resolved to ensure compliance with the legal and regulatory framework. The Audit Committees are composed of independent members selected in the private sector. Further, the Risk Management Division within the Office of the Accountant General provides functional guidance on risk management.

The Internal Audit units are staffed by professionals who have to be qualified accountants and/or members of the Institute of Internal Audit (IIA). Internal Audit adopts the IIA standards and has developed manuals that are aligned with these standards. This is requirement of the National Treasury Regulations. Quality assurance exercises, to ensure compliance with the standards are carried out each year, with independent bodies performing the quality assurances reviews once every five years.

The Internal Audit Units prepare a risk assessment of their Departments and elaborate 3-years audit plans as well as annual operational plans. The plans incorporate a range of audit types including compliance, financial audits, payroll audits, system including information technology audits, forensic and performance audits. Audit work plans suggest that more than 50% of audit time is spent on systems audits.

The Internal Audit present quarterly reports to the Audit Committees and in some instance monthly progress reports. All reports are shared with the Auditor-General whose representative sits in the Audit Committee. The reporting is also to Management Committees in some Departments. The Management Committee, composed of all directorates and the Minister, serves as a useful information and discussion forum to enhance the understanding and compliance to the financial management procedures.

Action by management of internal management is comprehensive across central government entities and generally there were prompt responses to internal audit findings;

however in some cases external audit reports revealed that specifically the prior year's external audit recommendations had not been fully implemented. The members of Internal Audit Units met report that corrective measures are taken by management on their findings. The Audit Committees are responsible for the internal audit findings, the findings highlighted in the Auditor-General's Report as well as the Standing Committee on Public Accounts resolutions. It appears though that follow up on internal audit findings is more complete and prompt than for external audit. There also appears to be some questions about Internal Audit follow up on conditional grants made to the Provinces. There appears to be questions about jurisdiction which has limited the effectiveness of the internal audit follow up on such grants.

The internal audit unit have re-organised to introduce risk management units as part of their efforts to increase the quality of risk assessment and management.

No.	Predictability and control in budget execution	Score	Justification
PI-21	Effectiveness of internal audit	A	
(i)	Coverage and quality of the internal audit function	A	The Internal Audit Function and its supervision by Audit Committees cover all Departments. The Internal Audit Units apply the IIA standards. The Internal audit unit prepare annual works plans that include process/full expenditure chain and procurement audits, payroll, compliance and financial audits, forensic, systems including IT audits and performance audits. At least 50% of the audit time is deemed spent on system audits.
(ii)	Frequency and distribution of reports	A	The audit reports carried out against a work plan are prepared and presented quarterly to the Departments through Audit Committees, the National Treasury and the Auditor-General.
(iii)	Extent of management response to internal audit findings	A	The Department management response to internal audit findings is complete and timely.

3.5 Accounting, recording and reporting

3.5.1 PI-22 Timeliness and regularity of accounts reconciliation

The Ministry of Finance operates a Treasury Single Account held with the South African Reserve Bank that is reconciled to the cash book on a monthly basis and takes place within 10 days of the close of the month. The cash management mechanism maintains a real time status of Departmental sub-accounts within the Treasury Single Account to enable it to trade aggregate swept balances on the money markets. As previously noted in PI-17 there are other government accounts related to donor funded projects that remain outside this arrangement for which no regular bank reconciliations are carried out by the government or reported on by the projects. The National Treasury operates the RDP Fund account which holds donor funds deposited with the government in a similar way as for the Treasury Single Account as it pertains to regular reconciliation and trading cash balances on the money markets.

The BAS system provides an automated basis for assisting in the completion of the reconciliation process. The National Treasury publishes on a monthly basis as part of the PFMA Section 32 requirement, a cash flow statement that aggregates the revenues, Departmental requisitions and net borrowings, reconciled against changes in bank balances within 4 weeks of the end of the month.

Section 40(1)(a) of the PFMA and Section 17.1 of the Treasury Regulations require that all suspense accounts be cleared and correctly assigned to the correct cost centres on a monthly basis. Typically reconciliation and clearance of suspense accounts and advances are done at the end of each month within 30 days of the close of the month, however in the current fiscal year (2008/2009) as a consequence of recent changes to the Chart of Accounts, the Accountant General has instructed that temporarily such reconciliation occurs only on a quarterly basis within a month of the close of the quarter, as a way of building up meaningful transaction statistics. The monthly reconciliation regime of suspense accounts shall be returned to next year.

The main sources of advances booked to suspense accounts are un-acquitted advances made to government officials for the purposes of foreign travel and for claims for vehicle accidents. Specific suspense accounts are reconciled and cleared each month, however the overall position may continue as new suspense accounts are created even as current ones are cleared. In a number of departments, un-acquitted advances pertaining to governmental officials are recovered directly from salary payments. As part of the year end closing procedures all suspense accounts are force closed at the end of each year to facilitate the issuance of the annual financial statements.

No.	Accounting, recording and reporting	Score	Justification
PI-22	Timeliness and regularity of accounts reconciliation (M2)	B+	
(i)	Regularity of Bank reconciliations	B	All treasury managed bank accounts are reconciled to the cash book on a monthly basis within 10 days of the close of the month. There are other government accounts specifically donor funded project accounts which are not reconciled on a regular basis.
(ii)	Regularity of reconciliation and clearance of suspense accounts and advances	A	The reconciliation and clearance of suspense accounts is carried out monthly within 30 days of the end of each month. As part of the year end closing procedures all suspense accounts are force closed at the end of each year to facilitate the issuance of the annual financial statements.

3.5.2 PI-23 Availability of information on resources received by service delivery units

Reporting on the resources (in cash or in kind) disbursed to the front-line service delivery units is facilitated through the BAS financial information management system. The Provincial Governments (along with 5 major metropolitan authorities) are responsible for primary health and primary education service delivery. The administrative structure of the budget as reflected in BAS includes cost centres specified to the level of primary schools and health clinics.

The Provincial Governments provide financial reporting that indicates the resources received in aggregate by primary schools and primary health care clinics. This is possible because the expenditure by the front-line service delivery units is tracked by the transverse BAS accounting system. The front line service delivery units are managed by the nine provinces and five metropolitan authorities and their expenditure reported upon annually. The National Treasury compiles this data and presents it in a consolidated report: the Provincial Budgets and Expenditure Review.

No.	Accounting, recording and reporting	Score	Justification
PI-23	Availability of information on resources received by service delivery units	A	The front line service delivery units are managed by the nine provinces and five metropolitan authorities and their expenditure reported upon annually. The National Treasury compiles this data and presents it in a consolidated report: the Provincial Budgets and Expenditure Review.

3.5.3 PI-24 Quality and timeliness of in-year budget reports

Section 32 of the PFM Act requires that the National Treasury publish in the Government Gazette within 30 days of the close of each month, a statement of actual revenue and expenditure for the period and on a current and cumulative year to date basis. Under the Act, the National Treasury may determine the format of the statement of revenue and expenditure. In practice the Treasury publishes monthly on its website, within 30 days of the close of the month, the consolidation of the Departmental Monthly Expenditure Returns presented in a format by vote and classified by current expenditure, transfers and subsidies, and capital expenditure. This format permits the direct comparison of revenue and expenditure to the original budget allocations which are included in the tables. It also includes a Revenue Statement and a Summary of Cash Flow which highlights Exchequer revenue, Departmental requisitions, projected under-spending, net borrowing requirements, and changes in cash balances.

The format of the Monthly Expenditure Returns reflects expenditure only at the time of payment and does not reflect commitments. There are some Departments (e.g. Department of Education) who prepare budget implementation reports for internal reporting purposes that do include commitments; however this is not a standard practice across all Departments.

The Monthly Expenditure Returns are submitted by the Departments on a monthly basis within 15 days after the close of each month. In practice there have been no delays recorded in the submittal of the reports which has allowed the National Treasury to consolidate the returns and publish them within 30 days of the close of the month in adherence to the law.

The General Ledger entries are reconciled each month and bank statements reconciled with the cash book monthly. There are no major concerns on data integrity or accuracy. As reported by the Auditor-General, there are no material concerns regarding the accuracy of data given the fully integrated implementation of the BAS application.

No.	Accounting, recording and reporting	Score	Justification
PI-24	Quality and Timeliness of in-year budget reports	C+	
(i)	Scope of reports in terms of coverage and compatibility with budget estimates	C	Comparison to the main budget is available at the vote and main economic classifications reported for both the current period and accumulated to date. Information includes all items of expenditure at the payment level but not at the commitment level.
(ii)	Timeliness of the issue of reports	A	Reports are prepared monthly by Departments and submitted to the National Treasury within 15 days of the close of the month. The National Treasury consolidates the submittals and publishes the consolidated report on its website monthly, within 30 days of the close of the month.
(iii)	Quality of information	A	A cash flow statement that reconciles revenue receipts with expenditure and net borrowings against bank balances is included in the consolidated statement. There are no material concerns regarding the accuracy of data given the regularity and comprehensiveness of reconciliation procedures and the fully integrated implementation of the BAS application.

3.5.4 PI-25 Quality and timeliness of annual financial statements

The PFMA and the Treasury Regulations along with an extensive set of published accounting policy guidelines, accounting practice notes and accounting standards define the legal and regulatory framework for public accounting in South Africa. There is a strong tradition of accounting practice; however these are yet to be encoded into specific accounting regulations or an accounting manual. The PFMA authorises the constituting of the Accounting Standards Board (ASB) to set standards of Generally Recognised Accounting Practice (GRAP) for the public sector. In setting these standards the ASB takes into account both local and international best practice. The capacity of the relevant entities to comply with such standards is left to the discretion of the National Treasury. All published financial statements include a detailed outline of the accounting policies applied in the preparation of the statements. The financial statements also take into account the disclosure requirements of the PFMA and the Treasury Regulations.

Section 8 of the PFMA states that in respect of Departments "*the National Treasury must prepare consolidated financial statements in accordance with generally recognised accounting practice for each financial year*". However, not all the processes or systems are in place to effectively facilitate full and complete consolidation. For this reason the consolidated financial reports are termed Consolidated Financial Information. While not strictly speaking consolidated financial statements the level and comprehensiveness of disclosure suggest that the process is well beyond a mere aggregation or summary of accounts. It would seem the main area of shortfall in the consolidation process would be with respect to the treatment of inter-Departmental transactions.

Under the cash accounting system the source document for accounting entries is the payment voucher coupled with the electronically generated cheque or other payment instruction. Entries are dated using the date on the payment instrument. A single paymaster general bank account, within the Treasury Single Account held with the South African Reserve Bank is used for making all Government funded payments out of the Treasury. In practice any open purchase orders (with unsupplied goods, works or services) are de-committed two weeks before the close of the fiscal year. Suspense accounts closely monitored and reconciled on a monthly basis are force closed as part of the end of year closing procedures. Financial statements encompass revenues, expenditures, liabilities including expenditure arrears and financial assets including tax arrears.

Each Department prepares stand alone financial statements that are completed within two months of the close of the fiscal year and submitted to the Auditor-General for audit. The audits of the Departmental Financial Statements are completed within one month and then submitted to the Office of the Accountant General for consolidation. The draft Consolidated Financial Information is submitted to the Auditor-General for Audit no later than mid August or less than five months after the close of the fiscal year. According to officials these deadlines were adhered to in the three years reviewed under this assessment. These statements are corroborated by the General Report of the Auditor-General for the financial year 2006-07 which indicates that 100% of the national departments met the legislated deadlines in respect of the timeliness of financial reporting.

No.	Accounting, recording and reporting	Score	Justification
PI-25	Quality and timeliness of annual financial statements	A	
(i)	Completeness of the financial statements	A	A consolidated government statement, termed consolidated financial information is prepared annually. It includes all revenues and expenditures, liabilities and financial assets.
(ii)	Timeliness of submission of the financial statements	A	While the Departmental financial statements are submitted to the Auditor-General within two months of the end of the fiscal year, the consolidated financial

No.	Accounting, recording and reporting	Score	Justification
			information was submitted within 5 months of the close of the fiscal year to the Auditor-General for each of the three years reviewed during this assessment.
(iii)	Accounting standards used	A	The Accounting Standards Board of South Africa has been constituted to set and promulgate accounting standards. All financial statements disclose the accounting policies that have been employed.

3.6 External scrutiny and audit

3.6.1 PI-26 Scope, nature and follow-up of external audit

The Auditor-General derives its independence, powers and mandate from the Constitution (Section 188) and the Public Audit Act. The Auditor-General must audit and report on the accounts, financial statements of national and provincial departments, municipalities and any other public institutions as well as institutions receiving funds from the General Revenue Fund and must submit audit reports to the legislature. The Auditor-General is appointed by the President on the recommendation of the National Assembly and approval by the National Assembly with a supporting vote of at least 60% of the members of the Assembly (Section 193 and 194 of the Constitution) for a fixed, non-renewable term of between five and ten years (Section 189). He may be removed from office only with a supporting vote of at least two thirds of the members of the Assembly on the ground of misconduct, incapacity or incompetence (Section 194). The Auditor-General is legally, financially and operationally independent from the public sector. The Auditor-General is empowered to audit any and all government entities including security agencies. The Constitution (Section 188) states that "*the Auditor-General must submit audit reports to any legislature that has a direct interest in the audit, and to any other authority prescribed by national legislation. All reports must be made public*". PFMA assures financial independence of the Office of the Auditor-General empowering his recovery of the costs of investigations.

A full range of audits are performed, including systems audits, financial and compliance, procurement, payroll and Information Technology audits and some performance audits. Currently the performance audits are limited to review and assessment of the performance information. This is not accompanied by a formal opinion; findings are reported in the Management letters from the Auditor-General to Departments. It is expected that the Auditor General will provide formal opinions in 2010/11. The standards applied are the International Standards on Auditing (ISA) and the International Organisation of Supreme Audit Institutions (INTOSAI). The Auditor-General uses this combination as the INTOSAI standards do not provide sufficient guidance on specific matters for providing assurance.

Departmental audit reports along with their audited financial statements are submitted to the legislature within five months from the end of the fiscal year which is equivalent to three months from submission to the AG. Step one; Departments submit their financial statements within two months from the fiscal year-end to the Office of the Auditor-General. Step two; the AG audits the statement within two months. Step three; Departments submit their annual reports to the legislature within one month. A Consolidated Financial Information (CFI) report on departmental financial statements is prepared by the National Treasury and submitted to the AG separately within five months from the end of the fiscal year. These are further submitted to the legislature within six months of the end of the fiscal year.

The Auditor-General reports that although formal responses are made by Accounting Officers to audit findings, the corrective measures undertaken and neither carried out in a systematic or timely fashion across all Departments.

No.	External scrutiny and audit	Score	Justification
PI-26	Scope, nature and follow-up of external audit	B+	
(i)	Scope/nature of audit performed (incl. adherence to auditing standards)	A	The Auditor-General audits all Departments and public and constitutional entities every year within the specified period by law. He performs a full range of audits including systems, financial, compliance, procurement, IT and some performance related audits (without formal opinion). The Auditor-General adheres to the ISA and INTOSAI Standards.
(ii)	Timeliness of submission of audit reports to the legislature	B	The Auditor-General combines its audit of the institutions with the audit of their financial statements. As a result, audited financial statements are submitted to the legislature within three months from the receipt of the financial statements by the Auditor-General. The Auditor-General's Reports are submitted to the legislature within five months from the fiscal year-end.
(iii)	Evidence of follow-up on audit recommendations	B	Although a formal response is made in timely manner, there is no systematic evidence of corrective measures taken by the Executive.

3.6.2 PI-27 Legislative scrutiny of the annual budget law

The Constitution (1996) establishes a Parliament composed of two houses at the national level: the National Assembly (NA) and the National Council of Provinces (NCOP). Each of the nine provinces has an elected Provincial Parliament. Members of the National Assembly are designated by their parties for a 5-year tenure.

The National Assembly and NCOP have a clear organisation and set of rules that are adhered to. The National Assembly functions on the basis of a number of committees. The Joint Rules Committee establishes all the rules of the National Assembly and the NCOP. The National Assembly rules are comprehensive, detailed and publicly available on their website. The annual parliamentary programme framework as well as the session and weekly agenda is developed by the Joint Programme Committee. Their agendas are publicly available.

The budget documentation is reviewed by a number of committees. There are Portfolio Committees responsible for reviewing the expenditure policies of each of the 34 Departments. The Portfolio Committee on Finance, responsible for the National Treasury, covers the macro-economic policies of the Government. The Joint Budget Committee is responsible for the in-year monitoring of expenditure and oversight of the implementation of corrective actions in response to the resolutions of the Standing Committee on Public Accounts (SCOPA).

The National Assembly can only approve or reject the Division of Revenue Bill (DORB) and the Estimates of National Expenditures (ENE). The NCOP also vigorously debates the DORB prior to passing the Division of Revenue Act (DORA) and ENEs. An independent body, the Finance and Fiscal Commission, provides policy analysis for the Parliament.

The National Assembly reviews Medium Term Budget Policy Statement (MTBPS) at the beginning of the budget cycle. It also reviews and debates the budgetary documents (see PI-6) during the main budget session. The full scope of the budget review is enshrined in the Constitution (see Section 215). The combined time available to the NA for the review of the budgetary documents referred to above is approximately five months. The debates are public and the media report on them. The MTBPS is presented in October with the Adjustment budget.

Clear rules exist for in-year amendments to the budget without the ex-ante approval of the legislature defined in the PFMA. These adjustments are presented in October to the National Assembly as part of the Adjusted Estimates of National Expenditures. Unforeseeable and Unavoidable Expenditures are funded from the contingency fund.

No.	External scrutiny and audit	Score	Justification
PI-27	Legislative Scrutiny of the Annual Budget Law	A	
(i)	Scope of the legislature's scrutiny	A	The legislative review covers the details of revenue and expenditure estimates, a medium term expenditure framework, a medium term sector and fiscal policies including the impact of the changes in the new tax policy proposals.
(ii)	Extent to which the legislature's procedures are well-established and respected	A	The legislature's powers are enshrined in the Constitution and in the PFMA. The House rules govern a number of Budget Committees whose requirements are adhered to. Rules are generally clear and accessible.
(iii)	Adequacy of time for the legislature to provide a response to budget proposals (time allowed in practice for all stages combined)	A	The Legislature is involved both at the beginning and at the end of the budget cycle. The combined time that the legislature has to review the budget documentation is five months.

No.	External scrutiny and audit	Score	Justification
(iv)	Rules for in-year amendments to the budget without ex-ante approval by the legislature.	A	Clear rules exist for in-year amendments without ex-ante approval. Excessive virements and expenditure over budget ceiling require the approval of the National Assembly of an Adjustment Budget.

3.6.3 PI-28 Legislative scrutiny of external audit reports

The Departments prepare Annual Reports which contain sections on their policy, medium term perspective, audited financial statements, Auditor-General's opinion and Management Letter including his recommendations.

Departments submit their financial statements in a timely fashion. The Auditor-General reports some delays in the submission of the financial statements of other PMFA organisations. These delays do not appear to affect the work of the Standing Committee on Public Accounts. The Standing Committee on Public Accounts examines the Annual Reports. SCOPA is comprised of 17 members and is traditionally chaired by a member of the opposition.

The examination process is subject to specific rules and procedures which are well documented and segregate the scrutiny process into clearly identifiable steps. The scrutiny process starts with the review of the audit report and a classification of the reports according to the type of the audit opinion (adverse disclaimer qualified and other). There are three main kind of follow-up procedures depending upon the type of the audits opinion. These are: A - where public hearings are carried out, B - where there is follow-up without hearings, C - no further action.

This review process is typically done within two months after the annual report submissions in September. Irrespective of the follow-up procedures applied to a given audit report, SCOPA summons each Department at least once every three years. The hearings are open to the public and media. The process is thorough and supported by preparation work sessions and briefs by the Auditor-General. They typically end between seven to eight months after the receipt of the audit reports.

The Internal Audit Units and the Auditor-General report that although correctives measures are taken by the Executive, resolutions are not systematically addressed across all Departments. SCOPA presents its reports to the plenary which passes the resolutions. These are communicated to the Executive by the Speaker with copies to the National Treasury and Auditor-General. Corrective measures are then implemented by the Departments with implementation responsibility with the Accounting Officer and oversight responsibility with the Audit Committee. The Joint Budget Committee follows-up on the resolutions. SCOPA and the Joint Budget Committee as well as the Auditor-General report that Departments lack capacity to take effective corrective measures.

No.	External scrutiny and audit	Score	Justification
PI-28	Legislative scrutiny of external audit reports (M1)	B+	

No.	External scrutiny and audit	Score	Justification
(i)	Timeliness of examination of audit reports by legislature (for reports received with the last three years)	A	A review of all departments' Annual Reports is done within two months from submission prior to the start of the formal in depth hearings.
(ii)	Extent of hearings on key findings undertaken by legislature	A	Public Hearings are conducted for the departments where serious concerns are identified e.g. adverse or qualified opinion. The hearings are thorough and are publicly accessible. In addition to this process, SCOPA has rules to ensure that each department is summoned at least once every three years.
(iii)	Issuance of recommended actions by the legislature and implementation by the executive	B	Actions emanating out of the SCOPA hearings are always recommended to the Departments, but these are not systematically implemented which leads to some implementation delays and omissions.

3.7 Donor practices

3.7.1 D-1 Predictability of Direct Budget Support

In the period considered, the EU, the Netherlands and Ireland were the only donors providing Budget Support (BS) to South Africa. The specific modality of budget support adopted by these donors is Sector Budget Support (SBS). The conditionalities and modalities of the budget support are outlined in specific donor-government Financing Agreements which spell out the mechanisms for disbursement[36].

As further elaborated in D-2, the South African government maintains a single account, Reconstruction and Development Programme (RDP) Fund account, for all donor funds including budget support. However, not all funds flowing through this account is budget support. Funds also include projects and programmes and are labelled as such.

The disbursement of the BS is guided by the Financing Agreements which specify the conditions for disbursement. Disbursement is generally agreed for the life of the Agreement and is based on yearly plans (e.g. the Netherlands and Ireland). In the case of the EC quarterly forecasts are included in most instances. A careful planning of the disbursements is compromised by the difficulty in aligning the Donor Fiscal Years to the South African FY. Further, disbursement forecasts will generally not be available prior to the government submitting its proposals to the legislature. There is no evidence to ambiguously conclude that all BS forecasts were approved at least six weeks prior to the submittal of government budget.

[36] Some donors have suggested that given the way "sector budget support" is implemented it rather be considered as project/programme support. This interpretation however contravenes the language, terminology and articles of the Financing Agreement, as well as the way the funds are treated and managed by the South African government.

The total amount forecast for EC sector budget support in 2005/06 was 54 Million Euro, of which 57.7 % was disbursed. In 2006/07 38.15 Million Euro was forecast and 85.9% was disbursed, while in 2007/2008 44.15 Million Euro was forecast and 26.1 % disbursed. Consequently for the two years considered the actual disbursement fell well below 15% of the forecast amounts (see Table 3.12).

Table 3.12 EC Budget Support for the period 2005/06 to 2007/08 (million Euro)

	2005/06				2006/07				2007/08[37]			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Forecasts[38]			34	20			25	13.15			31	13.15
SWEEPII			15				10					
RCFII				20				13.15				13.15
MasibambaneII			19				15					
MasibambaneIII											31	
Disbursements[39]			31.2				32.7				11.5	
SWEEPII			13.4								10.3	
RCFII							19.0					
MasibambaneII			17.8				13.7				1.2	
MasibambaneIII												
% disbursed	57.7%				85.9%				26.1%			
Weighted delay[40]	111%				290%				170%			

Source: Data on disbursements from the IDC unit (National Treasury). Data on forecasts based on Financing Agreements.

The Financing Agreements for Dutch BS are not aligned with the South African FY nor is the disbursement or reporting. Based on the data corresponding to the calendar years, for the period considered, it can be concluded that the budget support outturn was below forecast by more than 15% (see Table 3.13).

Table 3.13 The Netherlands Budget Support for the calendar years 2005 to 2008 (million Euro)

	Forecasts				Disbursements			
	2005	2006	2007	2008*	2005	2006	2007	2008*
Education Sector Budget Support	65	90	120	35	63	105	84	24.4
Education Centres KZN - DoE	26	30	42	20	26	0	50	0
Education Centres NW - DoE	15	20	25	23	15	0	10	20
Total	106	140	187	78	104	0	144	44.4
% disbursed					98%	75%	77%	57%

Source: The Dutch Embassy.

37 For the calculation of the weighted delay, the disbursements which were planned for 2007/08 but were not made in 2007/08 are assumed to be delayed at least until Q1 of 2008/09.

38 Data on forecasted disbursements are based on the original Financing Agreements.

39 The disbursement amount included in this table may differ with the amounts transferred by the EC to RDP Fund account. Data on EC disbursements is based on information from IDC. The corresponding amounts were converted from Rand to Euro based on the Euro exchange rate on the first date of the next month (Source: info EURO).

40 The weighted disbursement delay is calculated as the percent of funds delayed multiplied by the number of quarters of the delay.

With respect to the timeliness of EC BS disbursements, the disbursements were neither predictable nor timely. The data in Table 3.12 on EC budget support shows that actual "*weighted disbursement delays*" were well in excess of 50 % for each of the years reviewed. For the Dutch BS the "*weighted disbursement delays*" cannot be determined. However, it is still possible to conclude that disbursements were neither timely nor predictable. The available information for the Irish sector budget support does not allow a proper calculation of the actual outturn vis-à-vis the forecasts nor the "weighted disbursement delays". Nevertheless, the data point out to a full disbursement although with big delays at least for the first tranche[41]. Given that the Irish sector budget support represent only about 8% of the overall sector budget support (see Table 3.15) the overall conclusion regarding the scoring on the predictability and timeliness of the sector budget support is not affected.

No.	Donor practices	Score	Justification
D-1	Predictability of direct budget support (BS)	D	
(i)	Annual deviation of actual BS from the forecasts provided by the donor agencies at least 6 weeks prior to the government submitting its budget proposals to the legislature	D	In at least two of the three years considered the actual budget support outturn fell well below 15% of the forecast amounts. The forecasts are provided only at the time of signing the FA which does not necessarily occur at least 6 weeks prior to the submittal of the budget to the legislature.
(ii)	In-year timeliness of donor disbursements (compliance with aggregate quarterly estimates)	D	The actual "weighted disbursement delays" are well in excess of 50% for each of the years reviewed.

3.7.2 D-2 Financial information provided by donors for budgeting and reporting on project and program aid'

There are a variety of banking modalities that are available for the management of donor funds. However, the PFMA requires that government bank accounts have prior authorisation by the National Treasury. For donor funds managed directly by the government, including budget support, these are placed in a single bank account (at the SA Reserve Bank), the Reconstruction and Development Programme (RDP) Fund account. The operation of the RDP Fund is regulated by the *Policy Framework and Procedural Guidelines on ODA Management* (2003). The Donor Support is not part of the Revenue Fund and therefore it is considered extra-budgetary. However, it still requires full budgeting, fiscal disclosure and financial reporting. In the ENE only the funds managed through he RDP are included[42].

Aid delivery modalities to South Africa can be classified as follows:

- *on-budget* funds channelled *through RDP* Fund account (including budget support, projects and programmes);

41 The first tranche which represent about 30% of the total amount has been delayed with 11 months.
42 An exception is the fiscal year 2007/08 when such estimates were not included due to poor quality of data.

- *on-budget* funds agreed directly with departments or government agencies which are *not directed through the RDP* Fund, but are held in National Treasury authorised bank accounts, either domestically or internationally;
- *off-budget* funds, which contravene the PFMA;
- *in-kind* contributions.

Donor funds channelled through NGOs for projects not implemented on behalf of departments are not and should not be included in the budget documents.

Donor funds flowing through the RDP fund account represents only a small fraction (about 0.2 percent) of overall budget expenditure. Table 3.9 depicts the share of budget support and other project/programmes flowing through the RDP Fund. There is also substantial off budget donor assistance. The precise volume of this assistance however is unknown. At the moment the government of South Africa does not have reliable and comprehensive information on the actual value and composition of all donor assistance provided to the Government. According to officials the total amount of aid is to two to three times of what flows to RDP. This assessment has identified approximately three times the amount of donor funds flowing in contravention to the PFMA.

Table 3.14 Funds channelled through RDP Fund (Rand)

	2005/06	2006/07	2007/08	Average
Budget Support	320,009,869	497,009,940	279,653,297	22.9%
Other RDP Funds	760,214,477	862,107,344	970,997,587	77.1%
Total	1,080,224,346	1,359,117,284	1,250,650,884	100%
Share of Budget Support	29.6%	36.6%	22.4%	-

Source: IDC, National Treasury.

Some donors argue that their aid modalities do not contravene with the PFMA with respect to opening up bank accounts without National Treasury authorisation. They state that during the implementation of the projects/programmes the funds remain theirs. However, such an interpretation would require that what is contributed to the government be considered an in-kind contribution rather than a cash contribution. Providing reports on cash disbursements is however inconsistent with that argument.

In respect to the choice for channelling the funds, some donors and departments point to the flexibility offered by operating funds off-budget and claim that aid effectiveness is more likely through off budget arrangements. However, such practice undermines sound public finance management.

Although donor funds represent only a very small fraction of the budget expenditure at the aggregate level, their importance remains high with respect to specific areas of participation. Further, the lack of close coordination with budget estimation, execution and reporting directly affects the management of the budget and the efficiency of budgetary projects/programmes implementation.

Very few provide meaningful budget estimates for disbursement of project aid in a timely fashion at least three months before the start of the fiscal year. Information on donor funding in budget documents is missing. For the last budget 2007/08 donor funds including estimates channelled through RDP Fund were not included in the Budget Estimates due to their poor quality. Most of the budget estimates provided by donors do not distinguish between pledges, multi year versus single year commitments, and available funding. In addition, in many cases donors base their projections on their own fiscal year rather than specifically taking into consideration the South African fiscal year. In few cases estimates take into account absorptive capacity of the implementing agency and procurement plans. On the other hand, the National Treasury provides donors no clear requirements and guidelines as to budget estimate submissions. The up-shot of this is no budget estimates are provided and financial reporting remains ad-hoc[43]. The South African budgetary process follows a strict schedule of preparation (see PI-11) and so there should be an opportunity to align Donor budgets with that cycle.

Donors generally do not provide quarterly reports on the disbursements within two months of the end-of the quarter. Financial reporting does not generally happen, exception being for the RDP funds which represents approximately less than 25%. In this case the government prepares these reports. Reporting on other funds is generally ad-hoc and the compliance to the National Treasury reporting requirements varies across donors. When provided they do not reflect the fiscal year nor take into account the national accounting standards.

No.	Donor practices	Score	Justification
D-2	Financial information provided by donors for budgeting and reporting on project and program aid	D	
(i)	Completeness and timeliness of budget estimates by donors for project support	D	The Government of SA does not have comprehensive and reliable information on the value and composition of all donor assistance provided to the Government. While all major donors channelling funds through the RDP Fund (which represent less than 25% of all donor funds) provide data on pledges, commitments or available funding, they do not provide actual budget estimates informed by fully developed procurement plans and absorptive capacities pertaining to realistic schedules of project implementation. These budget estimates are not aligned to the SA budget cycle.
(ii)	Frequency and coverage of reporting by donors on actual donor flows for project support	D	A few donors provide data on actual disbursements to national departments and/or National Treasury (IDC). Most donors however do not provide any financial quarterly reports. In some cases annual financial reports are provided.

3.7.3 D-3 Proportion of aid that is managed by use of national procedures

Budget support follows the national procedures. According to the figures provided by the National Treasury for the period 2005/06 – 2007/08, less than 30 percent of the total

43 Some donors point out that financial reporting is requested for prior to such events as international conferences.

donor funds channelled through RDP constituted budget support and consequently, by definition, used national procedures. The other funds channelled through the RDP Fund account used national payment and accounting procedures since they are transferred from the RDP account to departments' accounts and are captured in the BAS system. Some donors require additional financial reporting for the use of their funds and carry out their own audit even for the funds channelled through the RDP Fund account. This is mainly due to the restrictions placed on donors by their own legislature and regulations. The procurement practices also vary across donors. Some donors require that their own procurement procedures are used. This is permitted by the Treasury Regulations on ODA.

Table 3.15 shows the proportion of funds using government systems. As the table depicts, from the funds channelled through RDP about 72% follow the national procedures. Funds channelled outside RDP Fund do not follow national procedures. Thus, for the total donor funds the estimate for the share of funds using national procedures is about 21%.

Table 3.15 Donor Funds and the Use of National Procedures (Rand, million)

	2005/06	2006/07	2007/08	Paym. Acc.	Proc.	Audit	Fin. Rep.
RDP non Budget Support							
Belgium	5,180,077	27,041,450	6,685,243	1	1	1	1
Canada	1,978,378	10,304,147	11,410,669	1	1	1	1
Denmark	12,249,151	65,588,665	30,924,747	1	1	1	1
Finland	16,061,730	36,318,278	8,095,757	1	1	1	1
Flanders	22,034,724	42,820,499	32,784,777	1	1	1	1
France	1,353,846	1,428,571	1,740,385	1	0	0	0
EC	343,041,446	555,502,746	509,655,743	1	1	0	0
Global Fund	105,704,688	23,374,780	219,380,757	1	1	0	1
Ireland	16,892,322	14,658,910	616,041	1	1	1	1
Netherlands	31,250,000	136,694	46,150,245	1	1	1	0
New Zealand	1,927,647	0	0	1	0	0	0
Norway	16,361,760	19,166,582	53,956,788	1	1	1	1
Sweden	19,149,496	43,069,623	10,079,400	1	1	1	1
Switzerland	2,505,442	3,200,000	5,999,600	1	0	0	0
UNDP	0	954,000	0	1	0	0	0
UNEP	0	0	1,786,985	1	0	0	0
UNESCO	209,287	0	0	1	0	0	0
UNICEF	0	541,700	0	1	0	0	0
UK	76,230,739	7,562,113	27,900,653	1	0	0	0
Other	88,083,744	10,438,587	3,829,799	1	1	1	1
Subtotal	672,130,733	851,668,757	967,167,788	100%	96%	21%	39%
Average				64%			
EC SBS	239,592,000	318,693,950	112,231,047	1	1	1	1
NL SBS	55,999,479	151,667,150	138,354,000	1	1	1	1
Ireland SBS	24,418,390	26,648,840	29,068,250	1	1	1	1
Subtotal - BS	320,009,869	497,009,940	279,653,297	100%	100%	100%	100%
Average				100%			

	2005/06	2006/07	2007/08	Paym. Acc.	Proc.	Audit	Fin. Rep.
Total RDP	1,080,224,346	1,359,117,284	1,250,650,884	100%	97%	38%	52%
Average				72%			
Funds outside RDP	-	-	> 3* billion	0%	0%	0%	0%
Grand total	-	-	> 4 billion	29%	29%	12%	16%
Average				21%			

Source: Development Budget 2006/07; (*) - The amount of donor funds outside RDP is an estimate based on data provided and interviews with donors and IDC portfolio managers.

Note: 1 - national procedures are used; 0 – national procedures are not used.

Key: Paym. Acc. – Payments and Accounting, Proc. – Procurement, Fin. Rep – Financial Reporting

No.	Donor practices	Score	Justification
D-3	Proportion of aid that is managed by use of national procedures	D	
(i)	Overall proportion of aid funds to central government that are managed through national procedures	D	Donor funds channelled through the RDP Fund amounted to approximately 1 billion Rand in 2007/08 which according to verified estimates represent about 25% of the total estimated donor funds. So, 75% of the funds did not use national systems.

4 Government reform process

4.1 Description of recent and on-going reforms

South Africa has evolved its reform approach away from a comprehensive integrated approach centred on a single integrated strategy, with emphasis on sequencing and coordination, to a more incremental one. Implicit in the approach of PFM reform in the first decade or so was a focus on three broad stages or platforms. These were achieving fiscal discipline, the efficient delivery of services, and the strategic allocation of resources. This appears to work because the main fundamental changes to the PFM have already been achieved and the focus is now more on capacity development rolled out to the provinces and municipalities. It can remain effective in delivering on improvements because it has already made the major transition to a reformed PFM system and is now focusing upon continuing improvements of the reformed systems informed by the lessons learned through the decade long reform experience.

The Government of South Africa has embarked upon a number of very successful PFM reforms since the mid 1990s. The reform agenda focused upon:

- The establishment of a legal and regulatory framework to strengthen and improve upon the transparency, comprehensiveness and credibility of the budget, debt management and external scrutiny and oversight;
- A focus away from input controls to delivered outputs supported by improved financial reporting and public and parliamentary access to budget and fiscal documents, and the introduction of Audit Committees to better hold budget managers accountable. Responsibility was devolved to spending departments for spending choices and use of funds within approved ceilings and against policy commitments;
- A better alignment of policy, planning and budgeting. The South African system recognises this and structures the integration of political and administrative practices to ensure that funding choices align with the priorities of government, and that political oversight is reinforced;
- A move to a multi-year budgeting framework to allow the re-allocation of resources to new priorities. The budget process includes various mechanisms to manage uncertainty and maximise funding and policy predictability over the medium term, while promoting alignment with policies at the margin, through the use of rolling baselines, a contingency reserve and a disciplined budget process, amongst other measures;
- The improvement of debt management through the introduction of suitable institutional arrangements; taking over the responsibility for funding decisions from the South African Reserve Bank; reforming the money market; integrating cash a

debt management, diversifying the debt portfolio and restricting the proportion of foreign debt; and establishing a risk management function;
- The revenue administration with respect to the improvement of revenue collections and promoting education, service and enforcement; and
- Strengthening the independence and the effectiveness of the office of the Auditor-General;
- The main national budget framework coordinates, integrates and disciplines policy and budget processes for the country at national, provincial and, increasingly, at local level. The reform initiative in the local government sphere was implemented through the Municipal Finance Management (MFMA), which became effective in July 2004 and whose implementation is supported by the annual Division of Revenue Act. The National Treasury has developed a phased implementation strategy of financial and technical support for local government based around the MFMA, including conditional grants, subsidies, technical guidelines, policy advice and the placement of international advisors with various municipalities. This strategy takes into account the diverse capacity of municipalities for implementing the reforms.

The early phases of reform were premised upon the issuance of detailed reform strategy, which while largely adhered to was never passed as a white paper. With the substantial achievements in PFM reform over the last decade and a half, as attested to by the results of this PEFA assessment, continuing PFM reform is probably better characterised as a process of strengthening and improving rather than a process of full reform. In this maturing phase, the centralised reform coordinated approach is deemed to be less effective. The current approach allows departments to get on with building capacity and improving their reformed systems. Quite distinct from the early period of reform which saw the introduction of new laws, changes in institutional arrangements, the introduction of new budget systems; the current phase of reform is characterised by amendments to the law, the improvement (and replacement) of existing computerised systems, continue to improve upon programme structure and descriptions, improving the specification, measurement and monitoring of output targets and continue broadening the scope of the consolidated financial statements.

There are five main areas of PFM reform activity planned that involve principally the National Treasury, SARS and the Office of the Auditor-General. These are:

- Amendments to the Legal and Regulatory framework, which includes the introduction of a Money Bill Amendment Procedure and Related Matters Bill;
- The Financial Management Improvement Programme;
- The improvement, upgrading and integration of the transverse computer systems;
- The revenue modernisation programme, and
- The improvements in external scrutiny and PFM performance monitoring.

Amendments to the Legal and Regulatory Framework

There are three major pieces of legislation that are currently being amended. These are:

1. A Money Bill which has been tabled before the National Assembly. It aims at providing the legal framework for the National Assembly to amend money bills. The members of Parliament interviewed indicated that such legislation would

necessitate the National Assembly building additional capacity to review, undertake research and more effectively debate economic and finance issues;

2. A revised PFMA bill that has been approved by Cabinet. The amended PFMA is a partially a response to the past ten years implementation experience to incorporate lessons learned into the act which has led to a requirement to strengthen the National Treasury's role at national and provincial levels as a way to better ensure efficient delivery of service and a closer alignment of the PFMA with the Municipal Finance Management Act. It is anticipated that the new bill will be tabled during the next fiscal year; after a new government has been installed;
3. A revised SARS legal framework which seeks among other things to codify the policies now used to limit the discretionary powers of the government entities involved in the application of penalties and waivers on tax arrears payments.

The Financial Management Improvement Programme II (FMIPII)
FMIP II builds on the experiences of the first FMIP by extending the work on developing policies and standards, as well as human capacity in areas of governance like budgeting, accounting, reporting systems and control mechanisms (internal and external audit) and providing more flexible support. The overall objective of FMIP II is to raise the SA Government's financial management performance and accomplish this on a sustainable basis. The EC has allocated 7.95 Million Euro to the support of the FMIP. The purpose of the program is to strengthen the finance management capacities (in management, human resources and IT) at national, provincial and municipal levels through supporting the implementation of the PFMA and the MFMA and from there initiate the development of professional cadres and capacity-building process in all governmental financial units.

As a consequence the main emphasis is placed on the strengthening of operational capacity at municipal and provincial government levels. This will mainly be achieved through capacity building interventions and creating institutional mechanisms to sustain these interventions. The purpose of the program is to strengthen the finance management capacities at national, provincial and municipal levels in support of the implementation of the Public Financial Management Act and Municipal Financial Management Act. Two related programs are the Municipal Finance Management Technical Assistance Programme and the Consolidated Municipal Transformation Programme.

South Africa is currently engaged in a major budget reform around performance. A framework for managing performance has been developed and at the moment work is being done to improve the Strategic Planning Framework, amongst others. This comes out of the awareness that often strategy and budgets are not effectively linked. The National Treasury is currently developing national guidelines to improve processes to ensure that when plans are developed, there is an explicit requirement to link this to the budget. It should be noted though that in South Africa there is a belief that while planning should be linked to the budget, some plans may need to be made even if there is no budget link at the present time.

The Municipal Finance Management Technical Assistance Programme (MFMTAP) seeks to assist in the strengthening of operational capacity at municipal levels. It provides technical assistance in implementing municipal financial management reforms. Through the programme about 30 advisors are currently placed in municipalities for a period of 2 years. Additionally, roving advisors are allocated to five provincial treasuries to assist provinces in performing their role in respect of the MFMA. This programme is financed by an IBRD loan to South Africa. The World Bank is supporting the government in the management of the emerging municipal bond market, the establishment of a Municipal Financial Recovery Service, an analysis of local government pension funds, and the strengthening of the government's oversight role in municipal public/private partnerships.

The Consolidated Municipal Transformation Programme (CMTP) aims to support the emergence of municipalities that offer democratic participation and wider, affordable and financially sustainable service delivery. This requires support for the development of a well-structured, informed local municipality, which complies with the legislation and encourages citizen participation and ensures that it reflects citizens' needs and priorities. The programme funds Integrated Service Facilitators and Financial Advisors appointed by National Treasury in the municipalities to assist in key areas. This programme is funded by DFID.

The Financing Agreement for FMIP II aims at impacting 7 areas:

1. Diagnostics Study implemented;
2. PFM Policies, standards and procedures developed;
3. A change management strategy implemented involving HR development and strengthening of organisational capacity;
4. Roll-out of improved PFM to provinces;
5. Roll-out of improved PFM to municipalities;
6. CABRI-Establish local and international networks;
7. Strengthen capacity of the Auditor-General's Office in PFM assessment. The Auditor-General seeks to develop and employ performance measurement tools to provide a measure of PFM performance. It is considering adapting parts of the PEFA framework in its endeavour to develop a set of suitable performance indicators. The Auditor-General has also indicated that it is seeking to increase the relevance of its reports to support management in taking corrective measures.

Improvements in transparency and information available to users

Further to the PFM improvements agenda outlined in the FMIP II, the National Treasury aims at providing information for all service delivery units for the education and health sectors rolled out over the next three years. It is anticipated that information on the resources received by front line service delivery units will be made available. In Year 1: hospitals and secondary and tertiary education institutions will be addressed; in Year 2 all other health facilities and in Year 3 all other schools.

Improvements to the Financial Management Systems

The, the State Information Technology Agency (SITA) is responsible for IT networks, systems operations and security for all levels of government. The Financial Systems section of the Special Services Division in the National Treasury responsible for the central and provincial government systems provides procurement, payroll and accounting software. It also provides a Business Intelligence Platform that integrates both central and provincial level and serves as a repository of financial data. The existing systems are deemed robust and appear to capture financial information as required but their use is cumbersome in terms of reporting and data querying and mining.

Thus, the National Treasury has initiated a reform effort that aims to upgrading and modernise all financial software and integrating them to serve as a single Integrated Financial Management Information System. The 7 year implementation plan was approved in 2006/2007. The National Treasury has decided to employ standard platforms customised to meet the needs of the PFM systems and procedures. This should properly address the issue of cost involved in proprietary software developed from scratch as well as meet the requisite functionality not addressed by standard ERP applications. Further the approach should assure the necessary independence to provide for ready report writing, application maintenance and upgrades.

Improvements in the Revenue Administration

SARS is undergoing a fairly comprehensive improvement programme articulated within its 5 to 7 year Modernisation Strategy. Under this strategy it seeks to address a number of areas of operations and management. These include:

- Enhance core operations and build core capabilities;
- Develop differentiated operating model through segmentation;
- Improve service, outreach and education;
- Develop an integrated risk management approach to improve compliance;
- Create capacity and knowledge to support government in delivering on overall national objectives (including proposed National Social Security initiative);
- Strengthen Border control (lead agency and security at ports);
- Further professionalize management processes and systems;
- Transform culture and further enhance capabilities;
- Improve infrastructure;
- Effective communication and change management.

4.2 Institutional factors supporting reform planning and implementation

The commitment to continuing improvements in PFM in South Africa has political championship at the very highest levels through the Minister for Finance. Implementation oversight and monitoring is the responsibility of the National Treasury's Heads of Division. Coordination of the reform efforts is the responsibility of the Budget Office. The Special Functions Division that includes the PFMA Implementation Unit has been playing a particularly important part in drawing lessons from experience on the legal and regulatory framework and coordinating its evolution.

This approach to system improvement is consistent with the adopted philosophy of allowing managers to manage and holding them accountable for results. Hence specific improvements are carried out by divisional heads with fewer requirements for careful coordination with other divisions since the improvements at this stage are mainly incremental. As a change management practice, the PFMA Implementation Unit and the Auditor-General are now developing tools to assess the readiness of institutions in embracing new rules, standards and practices. The following section describes the activities that aim at improving the efficiency and effectiveness of the PFM system in critical PFM components.

By way of donor participation and support of PFM improvements, this would require a broader dialogue within the budget formulation process of the National Treasury, the Parliament and the Office of the Auditor-General which serve as the main drivers of PFM improvements. Such dialogue would identify within their sector strategies and budgets reform improvement programmes and projects that could be flagged for support from donors.

Annexes

Annex 1 Terms of Reference: South Africa PFM Assessment based on the PEFA Methodology

1 Background

1.1 State of development in South Africa

South Africa has experienced strong economic growth over the past three years with real GDP increasing at around 5% annually, resulting in per capita income growth of 4.6% per annum. With GNI per capita of $4,960, South Africa is one of the few African countries to have joined the group of middle-income developing countries. The country's fiscal position has been strengthened: previous years' budget deficits have been turned into surplus in 2007/08, employment is rising and public debt has decreased from 60% of GDP to 50% during the last decade.

However, such tangible economic growth and the stable macro-economic situation have not produced a sustainable solution to unemployment, the country's key economic and social problem. The fact that the workforce is growing faster than the number of employment opportunities also contributed to unemployment. South African's economy is by far the largest in Sub-Saharan Africa – about 40% of total sub-Saharan African GDP – exerting major influence on total output, trade, and investment flows of the African continent.

Since about 45% of the population lives in rural areas and a fairly large proportion of the urban population reside in township areas and informal settlements, support should provide added value to these areas. In 2004, Government presented its ten-year vision for South Africa for the second decade of freedom and democracy. Five key goals are contained in the Government's Contract with the People of South Africa: (i) reduce poverty by half through economic development, comprehensive social security, land reform and improved household and community assets; (ii) provide the skills required by the economy, build capacity and provide resources across society; (iii) reduce unemployment by half through new jobs, skills development, assistance to small businesses, opportunities for self-employment and sustainable community livelihoods; (iv) massively reduce cases of TB, diabetes, malnutrition and maternal deaths, turn the tide against HIV and AIDS, strive to eliminate malaria and improve services to achieve a better national health profile; (v) reduce preventable causes of death, including violent crime and road accidents.

These goals were incorporated into government's Programme of Action 2007 which *inter alia*, focuses government action into a series of integrated clusters in order to synergise policy approaches and implementation. In his recent State of the Nation Address the President of SA announced 24 Apex Priorities which further refine these goals and which in turn will be incorporated into government's next Programme of Action. It should be noted though the statement of "Apex priorities" is not a standing practice in SA, and describes a practice for this financial year, which is the closing year of the current government.

The macro-economic stability has been achieved resulted in government having the scope to increase its expenditure, and fiscal policy has become more expansionary, while keeping within prudent limits. Strong economic performance has allowed public spending to grow by more than 9% per year in real terms over a last 5 year period. The consolidated national government fiscal framework projects an increase of government expenditure from 484 billion Rand in 2006/07 to 749 billion Rand in 2010/2011.

1.2 Fiscal situation and Public Finance Management (PFM)

The achievement of macro-economic stability is also due to the strict monetary policy followed since the late 1990s. This reduced inflation to 3.9% in 2005, ensuring that it stayed within the South African Reserve Bank's 3-6% target range. However, recent inflation figures have risen above this target, up to 8%. This and the almost structural current account deficit are the biggest current macro economic challenges in South Africa next to the looming energy crisis, the worsening international economic context, oil and food prices, as well as the unstable situation in neighbouring Zimbabwe and recent xenophobic-related violence in the country.

In terms of PFM, the 1994 transition in Government to a democratic state brought the realisations that an overhaul of the system of budget management was required, not only to fulfil the demands of the new constitutional framework, but also as a tool to bring about the improved substantial outcomes sought in terms of fiscal sustainability, improved alignment of spending with the new national priorities and the maximisation of existing resources towards these priorities.

The South African public expenditure management system has undergone substantial reform since the mid-1990s. While the early reforms shaped macroeconomic stability and strengthened public spending, the more recent emphasis of the reform programme has been on efficient resource allocation and effective service delivery. The highlights of the reform programme have been: the roll-out of a new intergovernmental system that requires all three levels of government to formulate and approve their own budgets; the introduction of 3-year rolling spending plans for all national and provincial departments under the Medium Term Expenditure Framework (MTEF); new formats for budget documentation that include a strong focus on service delivery information; and the enactment of new financial legislation. In addition, changes to the budget process have allowed role-players to deliberate on key policy choices and on the matching of available resources to plans, rather than item-by-item cost estimates.

Underlying the reforms were the following principles:

- *Comprehensiveness and integration* – The main national budget framework coordinates, integrates and disciplines policy and budget processes for the country at national, provincial and, increasingly, at local level;
- *Political oversight and a focus on policy priorities* – Choices between priorities are political in the final instance. The South African system recognises this and structures the integration of political and administrative practices to ensure that funding choices align with the priorities of government, and that political oversight is reinforced;
- *Using information strategically* – The reform process systematically set out to improve the timeliness, quality and usefulness of information on the allocation and use of funds, both internally and externally, to improve public policy and funding choices and to enable accountability;
- *Changing behaviour by changing incentives* – Responsibility was devolved to spending departments for spending choices and use of funds within approved ceilings and against policy commitments;
- *Ensuring budget stability and predictability while facilitating change at the margin* – The budget process includes various mechanisms to manage uncertainty and maximise funding and policy predictability over the medium term, while promoting alignment with policies at the margin, through the use of rolling baselines, a contingency reserve and a disciplined budget process, amongst other measures.

At present, the MTEF and Medium Term Policy Frameworks form an integral part of the budgeting process, enforced by a comprehensive legislative environment. Strengthening of the budget and expenditure cycle are continuing through initiatives aimed at training and the development of professional skills for all segments of the PFM process, the implementation of growth-enhancing policies and processes, as well as the assessment and application of benchmarks. All relevant legislation is in place and the oversight and control functions of the Parliament and the Office of the Auditor-General are considered to be mature and independent. The reform agenda focuses on the challenges of the roll out of the Public Finance Management Act to the Provincial and Local Governments.

Due to faster growth and improved revenue collections and base-broadening efforts, higher tax revenue has allowed for an improvement in the fiscal balance, and part of this revenue has gone to fund higher public spending. Government now realises the importance of policy initiatives to place increasingly greater emphasis on growth and development, as substantial progress has been made in reversing the inequalities of the previous political dispensation. Nevertheless, the realisation of socio-economic rights remains a key challenge.

Significant improvements in the tax base and the functions of SARS were evident and tax-to-GDP ratio has increased by nearly 5% of GDP over the past six years. As a consequence, since 2000, the budget deficit has remained between 1.4% and 2.3% of GDP and for 2006 and 2007 a budget surplus of about 0.8% of GDP has been achieved. Overall public debt amounts to 30.8% of GDP and public expenditure remains at an affordable and sustainable level equal to 27% of GDP. The created fiscal space in the 2008 budget framework aims to give greater impetus to the AsgiSA and the priorities set in government's Programme of Action. Transforming public service delivery in keeping with the country's reconstruction and development challenges remains the central organising principle of public expenditure planning.

Apart from increased forecasted tax income to 2010, the Medium Term Budget Policy Statement focused on service delivery and government savings, emphasising the importance of putting money aside in good times to cushion the economy in down cycles. The Minister emphasised that that revenue overruns due to cyclical factors should be spent on elements that will increase economic growth over the long period, such as infrastructure, education and institutional capacity. Strengthening of the budgeting and expenditure cycle have continued throughout 2007 through initiatives and projects aimed at training and the development of professional skills for all segments of the PFM process, the implementation of growth-enhancing policies and processes, as well as the assessment and application of benchmarks.

The policies and legislation currently in place for public finance management are indicated in Box 1.

Box 1 – PFM Legal Environment

The South African Government commenced with major financial management and budget reforms through the introduction of the Medium Term Expenditure Framework (MTEF) in 1998, which was aimed at advancing and promoting growth and development. Legislation that was subsequently developed governing PFM in South Africa includes:

- The Public Finance Management Act in 2000 (PFMA) and the Local Government: Municipal Finance Management Act (Act 56 of 2003) (MFMA).
- The Local Government: Municipal Systems Act (Act 32 of 2000) and the Municipal Systems Amendment Act (Act 44 of 2003)
- Other, which include:

✓ The Preferential Procurement Policy Framework Act (Act 5 of 2000)
✓ Broad Based Black Economic Empowerment Act (Act 53 of 2003)
✓ Division of Revenue Act (DoRA) This act is passed by Parliament annually.
✓ Appropriation Act, which is also passed annually, makes provision for the withdrawing of money from the National Revenue Fund in terms of the appropriation done by Act of Parliament.
✓ Intergovernmental Relations Framework Act (Act 13 of 2005)
✓ Public Audit Act (Act 25 of 2004)
✓ Taxation Laws and Revenue Laws

The main donors involved in PFM development and reform in the country include the following:

Programme	Donor(s) / Funder(s)	Description	Value
Financial Management Improvement Programme II	European Commission	The overall objective of FMIP II is to raise the SA Government's financial management performance and accomplish this on a sustainable basis. The purpose of the program is to strengthen the finance management capacities (in management, human resources and IT) at	€ 7,95 million

Programme	Donor(s) / Funder(s)	Description	Value
		national, provincial and municipal spheres through supporting the implementation of the PFMA and the MFMA and from there initiate the professionalisation and capacity-building process in all governmental financial units. As such a high emphasis is placed on the strengthening of operational capacity at municipal and provincial government's PFM abilities. This will mainly be achieved through capacity building interventions and creating institutional mechanisms to sustain these interventions. The programme is intended to contribute to the improved performance by National Treasury, to improve the performance of selected provinces in terms of especially monitoring and supporting municipalities in their quest for PFM and to deliver a road map for future interventions to improve PFM at provincial and municipal levels.	
Municipal Finance Management Technical Assistance Programme (MFMTAP)	International Bank for Reconstruction and Development, World Bank	A programme focused on the provision of technical assistance in implementing municipal financial management reforms in terms of the Local Government Financial Management Grants. Through the programme, which has entered phase 3, about 30 advisors are currently placed in municipalities for a period of 2 years. Additionally, roving advisors were allocated to five provincial treasuries to assist provinces in performing their role in respect of the MFMA. This is the only active IBRD loan to South Africa. The World Bank country office is supporting the government in (a) the management of the emerging municipal bond market, (b) the establishment of a Municipal Financial Recovery Service, (c) an analysis of local government pensions funds, and (d) the strengthening of the government's oversight role in municipal public/private partnerships	Included in the 2005 MTEF Cycle: R 200 million for each of the three years (Total US$15 million)
Consolidated Municipal Transformation Programme (CMTP)	DFID	The programme is aimed at making a real difference in eight municipalities in three South African provinces - Limpopo, KwaZulu-Natal and the Eastern Cape. The goal of the CMTP is the consolidation of accountable local democracy and pro-poor service delivery. The purpose is to support the emergence of municipalities that offer democratic participation and wider, affordable and financially sustainable service delivery. Simply put, this translates into support for the development of a well-structured, informed local municipality, which complies with the legislation and encourages citizen participation and ensures that it reflects citizens' needs and priorities. The programme funds Integrated Service Facilitators - many with an international background - along with	This is a five-year, £11 million programme funded in terms of a bilateral agreement between UK DFID and the South African Government

Programme	Donor(s) / Funder(s)	Description	Value
		Financial Advisors appointed by National Treasury in the municipalities to assist in key areas. The Programme also funds activities in the areas of municipal journalism, anti-corruption and HIV/AIDS.	
Various	GTZ	Under the “Local Governance and Development” programme of the GTZ, the following affects PFM reform: • Strengthening Local Government Programme • Business development Services & Local Economic Development • Municipal Finance Management Capacity Programme	
Housing & Municipal Services Programme	USAID	Project: Support democratic Local Government & Decentralisation This project is aimed at supporting SA’s efforts to roll-out a new municipal budget profess to 175 municipalities through technical assistance on capital investment planning, improved budget information management, monitoring and training.	$1.612 million
Democracy & Governance Programme	USAID	Project: Anti-Corruption Reforms During 2006, USAID has funded operations of the Department of Justice’s forensic audit unit to prosecute embezzlement, training to 500 corruption prosecutors and establishing 2 commercial crime courts. Plans are to assist 20 additional municipalities to institute transparent hiring procurement and complaint resolution systems	$500,000

DFID has additionally initiated a limited Fiduciary Risk Assessment (FRA) in February 2008 to allow the donor to contribute financially to ASGISA through the EC’s Employment Creation Sector Budget Support Programme.

1.3 Public Expenditure and Financial Accountability (PEFA)

The PFM Performance Measurement Framework is an *integrated monitoring framework* that allows *measurement of country PFM performance over time*. It has been developed by the PEFA partners, in collaboration with the OECD/DAC Joint Venture on PFM as a tool that would *provide reliable information on the performance of PFM systems, processes and institutions over time.*

Overall, the goals of the PEFA Programme are to strengthen recipient and donor ability to (i) assess the condition of country public expenditure, procurement and financial accountability systems, and (ii) develop a practical sequence of reform and capacity-building actions, in a manner that:
- Encourages country ownership;
- Reduces the transaction costs to countries;
- Enhances donor harmonisation;

- Allows monitoring of progress of country PFM performance over time;
- Better addresses developmental and fiduciary concerns;
- Leads to improved impact of reforms.

The information provided by the framework would also contribute to the government reform process by determining the extent to which reforms are yielding improved performance and by increasing the ability to identify and learn from reform success. It would also facilitate harmonization of the dialogue between government and donors around a common framework measuring PFM performance and therefore contribute to reduce transaction costs for partner governments.

The Framework could ideally be used as a tool to assess the improvement in PFM systems in the country over a 3-5 year period.

The PEFA PFM Performance Measurement Framework (PMF-PMF) has been developed as a contribution to the collective efforts of many stakeholders to assess and develop essential PFM systems, by providing a common pool of information for measurement and monitoring of PFM performance progress, and a common platform for dialogue.

The PEFA PFM Performance Measurement Framework incorporates (i) a *PFM performance report*, and (ii) a set of *high level* indicators which draw on the HIPC expenditure tracking benchmarks, the IMF Fiscal Transparency Code and other international standards. It forms part of the *Strengthened Approach* to supporting PFM reform, which emphasizes country-led reform, donor harmonization and alignment around the country strategy, and a focus on monitoring and results. This approach seeks to mainstream the better practices that are already being applied in some countries.

The PEFA Framework is applied to assess PFM *systems* and not on budget *policy* issues. The PMF identifies the critical dimensions of performance of an open and orderly PFM system as follows:

1. *Credibility of the budget* - The budget is realistic and is implemented as intended;
2. *Comprehensiveness and transparency* - The budget and the fiscal risk oversight are comprehensive, and fiscal and budget information is accessible to the public;
3. *Policy-based budgeting* - The budget is prepared with due regard to government policy;
4. *Predictability and control in budget execution* - The budget is implemented in an orderly and predictable manner and there are arrangements for the exercise of control and stewardship in the use of public funds;
5. *Accounting, recording and reporting* – Adequate records and information are produced, maintained and disseminated to meet decision-making control, management and reporting purposes;
6. *External scrutiny and audit* - Arrangements for scrutiny of public finances and follow up by executive are operating.

Against the six core dimensions of PFM performance, the set of high-level indicators measures the operational performance of the key elements of the PFM systems, processes and institutions of a country central government, legislature and external audit. In addition, the PFM-PR uses the indicator-based analysis to develop an integrated assessment of the PFM system against the six critical dimensions of PFM performance and evaluate the likely impact of PFM weaknesses on the three levels of budgetary outcomes.

It is expected that the repeated application of the indicator tool will provide information on the extent to which country PFM performance is improving or not. In addition, the PFM-PR recognizes the efforts made by government to reform its PFM system by describing recent and on-going reform measures, which may not have yet impacted PFM performance. The report does not, however, include any recommendations for reforms or assumptions as to the potential impact of ongoing reforms on PFM performance.

For more information, please consult the websites:
- PEFA Secretariat: http://www.pefa.org;
- OECD on PFM: http://www.oecd.org/department/0,2688,en_2649_15587066_1_1_1_1_1,00.html.

2 Rationale

The rationale for conducting a PEFA assessment in South Africa is twofold:
- In the short-term, the PEFA assessment will be used as baseline data, and a basis for information and monitoring so as to: (i) facilitate and update the dialogue on PFM between Government and donors; (ii) help donors assess the eligibility of a country for a new sector budget support (GBS) programmes, and to verify whether general or specific PFM conditions of an ongoing SBS programmes have been met;
- In the medium-term, the outcomes of the PEFA assessment will be utilised to feed the reflection on: (i) measuring the progress made with regards to PFM improvement (and related action plan); and (ii) informing and guiding the Government's PFM capacity development programme, in coordination with the donor community;
- This assignment is furthermore important as it will serve the purpose of donor coordination, harmonisation and involvement, firstly in terms of reducing the duplication of studies required to support donor funding to South Africa and, secondly, to provide a uniform platform from which donor involvement in PFM reform and improvement could be initiated in a joint manner.

3 Objective

The objective of this assignment is as follows:

To compile a comprehensive[44] "Public Financial Management – Performance Report" (PFM-PR) prepared according to the PEFA methodology, so as to provide an analysis of the overall performance of the PFM systems of the Republic of South Africa, as well as to

[44] This PFM PR is composed of the detailed analysis of the 31 indicators of the « PFM Performance Measurement Framework » and of the performance report itself which summarises this analysis of the indicators and includes other elements relevant for the assessment.

provide a baseline situation that permits the measuring over time of changes in performance.

4 Purpose

The purpose of the assignment is to:

1. Conduct the first PFM assessment for the Republic of South Africa on a *central level* based on the PEFA methodology, including:
2. Analyse objectively the existing PFM sector in the country in terms of the 31 high-level indicators that covers the six essential dimensions for the performance assessment of public finance management (inclusive of donor practices);
3. Compile an objective assessment report aimed at providing an exhaustive and overall evaluation of the performance of the public financial management of the country under review on the basis of the indicators, to identify the main PFM weaknesses and the country, and to evaluate to what extent the institutional mechanisms set up by the partner country contribute to planning and the implementation of the reforms of the public financial management. This Summary Assessment of PFM performance and the impact of PFM weaknesses are of highest importance to the Commission, the government and other donors. It is an important part of the basis of future reform discussions;
4. Provide a shared information pool for donors with regards to overall public finance management performance in the country. This should lead to increased donor coordination and harmonisation, as well as a basis for policy dialogue in the PFM sector.

5 Specific Tasks/Results

In order to meet the objective of the assessment mission the following specific tasks shall be carried out in accordance with the PEFA methodology:

- <u>Training workshop</u>. The mission on the spot will start with a 1/2 day information/training workshop gathering all the stakeholders and enabling the latter to understand the challenges and the modalities of the PEFA assessment. This workshop will be run and facilitated by the experts and its organisation will be taken care of by the European Commission and National Treasury. The pedagogical material used by the experts will be that worked out by the PEFA Secretariat and posted on its website. This workshop will comprise: (i) a general session with all the stakeholders aiming at providing a general understanding of what a PEFA assessment is about; (ii) a technical session with the national authorities (government and external control body) to explain the indicators;
- <u>Documentation</u>. A representative from the European Commission Headquarters will be in South Africa at the time of the assignment's start. Arrangements will be made for the provision of all basic documentation deemed necessary for the mission's work on the spot. The experts should also let the Government know, through the local representation of the European Commission, any need for additional information. The experts will specify the time-span they deem necessary between the date of reception of this basic documentation and the actual start of the analyses phase of the

assignment. The lead donor will particularly follow up this issue with the national authorities so as to minimize the risk of disrupting the mission which could be entailed by an important delay in providing this basic documentation. Specific attention should be given also to previously conducted PFM assessments by the different donors and the national authorities;

- Work-plan: Within 1 week after arrival the experts will submit to the national authorities and the European Commission a work-plan describing the main steps of the mission, notably specifying the list of the interlocutors to meet, the tentatively scheduled meetings and the list of required information not yet collected and to be provided on the spot. This work-plan may foresee a mid-term meeting gathering all the stakeholders so as to report on the work's progress and possible difficulties faced;
- Assignment: After the inception phase, and based on the agreed action plan and timetable, the experts will continue with the analyses, fieldwork and reporting required to achieve the indicated results, based on the PEFA methodology. This includes (but are not limited to):
    - Further collection of documentation not previously analysed;
    - The organisation of the required workshops and working sessions;
    - Analyses of documentation and interviews with administration. This includes the drafting of an Aide Mémoire;
    - Compilation of draft final report;
    - Analyses of comments/verification and compilation of final report.
- Facilitation of a final debriefing session with the involved stakeholders.

A detailed indicative work plan is included in Annexure A of this TOR.

6 Methodology

The following methodology will be followed:

1. Document of reference: The experts, in close coordination with government services involved, will undertake the required analysis while rigorously following the structure, the methodology and the guidelines of the document adopted by the PEFA Steering Committee and entitled "Public Financial Management – Performance Measurement Framework". This document can be found on the website www.pefa.org. The original version of this document is in English. Should any uncertainty arise in the interpretation of the text of the translated versions (French, Spanish, Portuguese, Russian) the experts will refer to the original English version to avoid any misunderstanding of the methodology to apply;
2. Differences in Methodology. If the particular situation of the country requires the addition of specific indicators and/or, for some indicators, to diverge from the prescribed methodology, this shall be duly justified by the experts and require the agreement, during the mission, of the European Commission. In any case, only a very limited number of additional indicators would be acceptable. In this case, as well as for any possible proposed difference in methodology, the experts will ask for the written opinion of the PEFA Secretariat;
3. Interpretation. Any question on the interpretation of the guidelines, which the experts cannot resolve with the available documentation, should be addressed to

the PEFA Secretariat and/or to the Headquarters of the European Commission (namely EuropeAid Unit E1);

4. Supporting information. In the report the experts will justify the scoring and describe, in an annex, for each indicator, the analytical work which has been carried out mentioning the sources of information and documentation used. Furthermore, for each indicator, the experts will mention any possible difficulties encountered during the assessment, the approach used to overcome these difficulties, and, as appropriate, the additional investigative work judged necessary to complete the analysis carried out.

7 Stakeholders: Donors and National Authorities

The following stakeholders will be involved in this assessment:

- The lead donor: This will be the European Commission (represented by the Delegation to South Africa). The EC's role will be, inter alia:

(i) to make the first contact with the government and officially informs them of the timetable and TOR of the PEFA assessment;
(ii) finances the PFM assessment and recruits the experts;
(iii) responsible with the South African Government for the organisation and the follow-up of the mission;
(iv) checks the quality of the report in consultation with the other donors involved, the PEFA Secretariat (where required) and the government;
(v) consolidates the comments of donors and the PEFA Secretariat and forward them to the experts and the government;
(vi) disseminates the draft and final report. The lead donor will indicate the names of its officials who, in the HQs and on the spot, will be the contact point for the experts.

- The other donors involved: The other donors, as well as the EU Member States, will be involved on a strategic level during this assignment. This will include strategic direction, provision of information regarding donor funded activities and verification of information and reports.
- The South African Government:
  1. will indicate the names of the officials (Ministry of Finances / National Treasury) who will be the interlocutors of the experts and of the donors during the assessment;
  2. will indicate whether a service of the administration will accompany the experts during the mission;
  3. will comment the draft and final reports and send its comments to the experts and the lead donor.
- Other State structures: Other structures that will form part of this assignment will include, but are not limited to:

  ✓ The Auditor-General's Office (as Supreme Audit Institution) and its established networking structures AFROSAI-E and ESAAG;
  ✓ South African Reserve Bank;
  ✓ South African Revenue Service (SARS);
  ✓ Office of the Presidency;

- ✓ CABRI (Collaborative Africa Budget Reform Initiative), National Treasury;
- ✓ Parliamentary Monitoring Group and the Standing Committee on Public Accounts (SCOPA);
- ✓ Accounting Standards Board;
- ✓ Public Services Commission;
- ✓ Financial and Fiscal Commission;
- ✓ Financial Intelligence Centre;
- ✓ Office of the Presidency;
- ✓ Advisor to the Minister;

This list will be refined in cooperation with National Treasury: International Donor Coordination Unit (IDC).

8 Experts Profile

The team will be composed of the following experts:
- One (1) Category I expert (Team Leader and PEFA Expert), for a total of 50 working days (69 calendar days);
- Two (2) Category II experts for 50 working days each (69 calendar days each).

The experts will have the following profiles:

8.1 Team Leader / PEFA Expert

Expert Qualifications / Experience
- At least a recognized Master Degree or recognised equivalent level in the fields of public financial management, fiscal policy, accounting, economics and/or public sector auditing;
- At least 15 years working experience in the various disciplines of public financial management, PFM reform, research and PFM/fiscal policy formulation and dialogue;
- Proven experience in the application of the PEFA methodology and assessment of PEFA indicators and reporting.

Skills / Knowledge-Base
- Working and research experience in assessing all aspects of PFM systems, policies and procedures;
- Knowledge of international practices with regard to PFM systems, policies, procedures and practices;
- Understanding of and experience in working in the South African public finance management sector and environment will be advantageous;
- Understanding of the aid effectiveness debate and experience in the ODA environment related to financial management performance measurement and policy dialogue will be advantageous.

8.2 PFM Analyses Experts

Expert Qualifications / Experience

- At least a recognized Master Degree or recognised equivalent level in the fields of public financial management, fiscal policy, accounting, economics and/or public sector auditing;
- At least 10 years working experience in the various disciplines of public financial management, PFM reform, research and/or PFM/fiscal policy formulation.

Skills / Knowledge-Base

- Working and/or research experience in assessing all aspects of PFM systems, policies and procedures. The experts must offer work/research experience in at least a combination of the main fields covered by the PEFA indicators, which include:
  - Budget transparency and allocation (including budget formulation, preparation and oversight);
  - Budget management;
  - Intergovernmental relations;
  - Multi-year fiscal planning;
  - PFM and expenditure policy and legislation;
  - Taxation systems and policies;
  - Public procurement and treasury functions;
  - Internal controls and auditing;
  - External auditing and performance auditing;
  - ODA incorporation on budgets;
  - Accrual accounting;
  - Classification;
- Understanding of and experience in working in the South African public finance management sector and environment will be advantageous;
- Understanding and/or experience in working with the PEFA methodology and assessment of PEFA indicators and reporting will be advantageous.

The cumulated experience of the experts should ensure that the team is able to cover the analysis of the different areas of the PFM-Performance Report.

The working language for this assignment will be English.

9 Logistics, timing and budget

The assignment will commence no later than 19 June 2008 and end no later than 22 September 2008 with the submission of the final report. During the overall period, the experts will deliver a maximum of 50 person/days of service (the assignment will be 69 calendar days per expert) – also refer to Section 8 of the Terms of Reference.

A tentative table indicating the dates and key steps in preparing the PFM-PR, as well as the experts involved is included in Annexure A to this Terms of Reference. For the purpose of this contract, experts have the permission to work during weekends and public holidays, as required for delivering the requested services.

The analyses phase of the assignment will be carried out in Pretoria, Republic of South Africa. The European Commission and National Treasury will provide support to the experts with the arrangements of any stakeholder workshops.

The contractor will cover the travel costs and subsistence allowance of the consultants from the overall budget value. The budget should make provision for:
- International travel depending on the home base of the experts proposed;
- Local travel costs;
- Per diems, and
- Other costs related to research and the arrangement of the indicated workshops.

10 Reporting

Reporting requirements are set out below:
- The experts will provide within 6 working days after the start of the mission submit an Inception Report (inclusive of a detailed workplan) that will guide the remainder of the assignment and the allocation of resources;
- In view of the final session of debriefing at the end of the mission, the experts will provide the European Commission with an *Aide Mémoire* (10 pages maximum, excluding annexes), in 5 hard copies and one electronic copy, indicating the main findings and reflections which will be developed in the draft report. This Aide Mémoire will be complemented by the detailed analysis of the 31 indicators of the PFM-PMF;
- By the end of the mission on the spot, the experts will provide to the European Commission a draft PFM-Performance Report, in 5 hard copies and one electronic copy, based on Annexes 1 and 2 of the above-mentioned PEFA document;
- Within 15 days following the reception of the draft report, the stakeholders (donors, government) will send their comments to the experts. Comments will be sent to the European Commission, who will be responsible to consolidate the comments and forward it to the team leader;
- Within 11 working days after the reception of the comments, the experts will write the final report. The latter will be sent in 5 copies to the European Commission. It will contain, in an annex, the observations of the government on the points where the latter disagrees with the findings of the experts;
- All reporting will be done in English.

Please note the following information for the final reporting:

FINAL REPORT	
Title	PEFA Public Financial Management Performance Assessment Report for the Republic of South Africa, 2008 Specific Contract N° AFS / 2008 / 159-145
Language	English
Date of delivery	22 September 2008
Recipient	EC Delegation in Pretoria
Responsible	Mr Hubert Perr, Counsellor Development
Copies to submit	5 hard copies + electronic copy

Annex A: Indicative Road Map for the preparation and execution of the mission

Tasks	Responsible	Calendar
Preparations & recruitment of the experts	Donors	
Recruitment of consultants according to the specific recruitment procedures of each contracting donor.	European Commission Delegation to South Africa	28 May
Works of the experts and finalisation of the report	Experts	
1. Mission inception – PEFA Training Workshop	FWC Team (all experts), European Commission and National Treasury	19/20 June
2. Inception meetings & report 3. Collection of documentation and request for additional information	3 x Experts	30 June
4. Mission on the spot: analysis of documentation and interviews with administration	3 x Experts	30 June to 15 August
5. Submission of Aide Mémoire and workshop	3 x Experts	By 25 July
6. Submission of draft report and debriefing meeting	3 x Experts	15 August
7. Comments from stakeholders, consolidation of comments	European Commission	5 September
8. Compilation and submission of final report	FWC Team (do not have to be on-the-spot, can be home-based)	22 September
Validation of the reports	Donors, Government, Secretariat of PEFA**	
- Check the quality of the draft report - Draft and send comments to the experts. - Approval of the final report	The comments of the donors and of the PEFA Secretariat will be consolidated by the lead donor.	15 August to 26 September

** On request of the donors the Secretariat of PEFA may be asked to check the quality of the draft report and/or of the final report. It is desirable that its opinion be asked at the stage of the draft report.

Annex 2 PFM Performance Measurement Framework Indicators Summary

No.	Indicator	Scoring	Brief Explanation and Cardinal Data used
A.	**PFM-OUT-TURNS: Credibility of the budget**		
PI-1	Aggregate expenditure out-turn compared to original approved budget	A	Actual primary expenditure deviated from expenditure estimates below 5% for three of the years considered. Deviations were 0.3%, -0.6% and 1.4% respectively.
PI-2	Composition of expenditure out-turn compared to original approved budget	A	Variance in primary expenditure composition exceeded overall expenditure deviation by no more than 5% in any of the years considered. Variance in expenditure composition exceeded overall deviation primary expenditure by 5%, 2% and 2% respectively.
PI-3	Aggregate revenue out-turn compared to original approved budget	A	Domestic revenue collection exceeded 97% in all three of the last three budget years. The ratio of aggregate revenue out-turn to original approved budget were 111%, 108% and 101% respectively.
PI-4	Stock and monitoring of expenditure payment arrears	A	
(i)	Stock of expenditure payment arrears (as a percentage of actual total expenditure for the corresponding fiscal year) and a recent change in the stock	A	The ratio of expenditure arrears to total expenditure for all three years considered was lower than 2%.
(ii)	Availability of data for monitoring the stock payment arrears	A	Reliable complete consolidated expenditure arrears data is provided as part of the Consolidated Financial Information. The reported expenditure arrears include an aging profile presented graphically.
B.	**KEY CROSS-CUTTING ISSUES: Comprehensiveness and Transparency**		
PI-5	Classification of the budget	A	The budget formulation and execution is based on economic, administrative, programme and sub-programme classification that can produce consistent documentation according to GFS/COFOG standards at the functional as well as sub-functional level. The chart of accounts is derived from and is an extension to the GFS 2001 standard.
PI-6	Comprehensiveness of information included in budget documentation	A	Budget documentation fulfils all 9 benchmarks. The Budget documents are comprehensive.
PI-7	Extent of unreported government operations	A	

No.	Indicator	Scoring	Brief Explanation and Cardinal Data used
(i)	Level of unreported extra-budgetary expenditure	A	All revenues generated directly by the Departments are transferred to the National Revenue Fund. Intelligence and security agency budgets are reported on, if not in detail. There is no evidence of off balance sheet debt instruments being used to finance subsidies and deferred financing arrangements such as incorporated into public private partnership transactions are reported on within the budget. The consolidation process of the Departmental final accounts includes an aggregate reconciliation process that would reveal any gaps in the sources and uses of funds. The level of unreported extra-budgetary expenditure remains insubstantial.
(ii)	Income/expenditure information on donor-funded projects	A	Complete income/expenditure data of donor funded grant projects are not included in budgetary information. However, reasonable extrapolations of how much donor grant funded expenditure occurs beyond expenditure channelled through the RDP account still suggests the total amount to be less than 1% of total expenditure.
PI-8	Transparency of inter-governmental fiscal relations	A	
(i)	Transparent and objectivity in the horizontal allocation among SN government	A	The transfers to Provincial and Local Governments are classified as unconditional equitable share transferred directly to the Provinces, and the conditional share transferred through the Departments. Both components are transparent and rule based and embodied into the annual Division of Revenue Act.
(ii)	Timeliness of reliable information to SN government on their allocations	A	All SNGs are provided reliable guidelines on the budget ceilings through the MTEF process prior to the start of their detailed budget procedures even though, minor adjustments may be made after the budget hearings. While the capital transfers are not made available to Local Authorities at the start of the budget preparation process, their later fiscal years (July 1st to June 30th) allow them ample time to prepare their detailed budgets after their individual allocations have been agreed in the National Budget
(iii)	Extent of consolidation of fiscal data for government according to sectoral categories	B	58% of SNG fiscal information (ex-ante and ex-post) is consolidated into annual reports within 10 months of the close of the fiscal year and 100% within 18 months (see table below)
PI-9	Oversight of aggregate fiscal risk from other public sector entities.	B+	
(i)	Extent of central government monitoring of AGAs/PEs	B	All Public Enterprises submit audited financial statements to the central government. All Major Public

No.	Indicator	Scoring	Brief Explanation and Cardinal Data used
			Entities are consolidated into the Consolidated Financial Information. While there is a requirement for the submission of quarterly fiscal reports, this is not yet being adhered to by all Major Public Entities.
(ii)	Extent of central government monitoring of SN governments' fiscal position	A	SNGs cannot on their own authority generate fiscal liabilities for the central government. Any loan that binds the National Revenue Fund requires the written approval of the Minister of Finance. The fiscal position including the level of outstanding debt is consolidated into the Local Governments Budgets and Expenditure Review, and the Provincial Budgets Expenditure Review.
PI-10	Public access to key fiscal information	A	All of the six listed elements of information are made available to the public access via the web and other means. The exception is the information on resources available to primary service units.
C.	**BUDGET CYCLE**		
C(i)	**Policy-Based Budgeting**		
PI-11	Orderliness and participation in the annual budget process	B	
(i)	Existence of and adherence to a fixed budget calendar	A	A clear annual budget calendar exists that is generally adhered to and the calendar allows six to eight weeks for Departments to meaningfully complete their detailed estimates of revenue and expenditure. There is also sufficient time for Departments to re-programme approved bids (up and above the base line) after the approval by cabinet of the bid allocations.
(ii)	Guidance on the Preparation of budget submissions.	A	The National Treasury issues comprehensive and clear budget circulars for an integrated recurrent and capital budget process. The previous MTEF allocations serve as firm budget allocation guidelines but may be subject to usually relatively minor adjustments through a bid process up and above these allocation guidelines. The bid allocations are approved by Cabinet. Such approval of finalised ceilings allows Departments about a further 4 weeks to incorporate any amendments.
(iii)	Timely budget approval by the legislature	D	In the three years reviewed under this assessment, the budget was signed into law after two months after the start of the fiscal year.
PI-12	Multi-year perspective in fiscal planning, expenditure policy and budgeting	B	
(i)	Multi-year fiscal forecast and functional allocations	A	Forecasts of fiscal aggregates are prepared for three years, including the budget year. The forecasts are directly linked to subsequent budget ceilings and include functional/sector classifications.

No.	Indicator	Scoring	Brief Explanation and Cardinal Data used
(ii)	Scope and frequency of debt sustainability Analysis	A	DSA for external and domestic debt is carried out every year by both the National Treasury as well as the South Africa Reserve Bank.
(iii)	Existence of costed sector strategies	D	Sector strategies exist for all Departments. These though are not developed within a broad fiscal frame and even where costed never include forward linked recurrent cost implications.
(iv)	Linkages between investment budgets and forward expenditure estimates	A	The selected investments have links to the National strategy framework through the linked sector strategies even though such links are qualitative. The selection of investment is based upon sector and program priorities; however they may also be influenced by the political objectives expressed for example through the Apex priorities included in the State of the Nation address as was done for the 2008/09 FY.
C(ii)	**Predictability and Control in Budget Execution**		
PI-13	Transparency of taxpayer obligations and liabilities	A	
(i)	Clarity and comprehensiveness of tax liabilities	A	For all major taxes the obligations are well specified in the Acts and in regulations. The SARS issues specific public information that ranges from general guidance to detailed sector, entity and tax specific documents. Waiving of tax, penalties and interest is subject to policy notes and rules detailed in manuals and any waiving has to be reported to the Auditor-General, the Minister of Finance and the National Assembly.
(ii)	Taxpayer access to information on tax liabilities and administrative procedures	A	For all major taxes SARS provides education and support to taxpayers and has made it a priority to provide information that is as accessible and clear as possible. The website contains a set of useful regulations, documentations, guides and tools. A help desk and call centres during the filing period are also in place to respond to public demand for information. SARS also makes use of all available mass communication means such as print media, radio and television, text messaging and mobile offices. All new legislations and regulations are subject to a wide consultative process.

No.	Indicator	Scoring	Brief Explanation and Cardinal Data used
(iii)	Existence and functioning of a tax appeals mechanism	A	For all major taxes SARS applies an administrative appeal mechanism referred to as the Alternative Dispute Resolution process. Clear policies and rules have been developed. A guide on the appeal system has been published by SARS and data available demonstrates that the system is operational and that appeals receive due attention.
PI-14	Effectiveness of measures for taxpayer registration and tax assessment	A	
(i)	Controls in taxpayer registration system	A	Taxpayers are registered in databases for income tax, VAT that have direct links with each other and with the Registrar of Companies and through the inclusion of bank accounts with the Financial Sector. The Customs database is linked to the Income Tax through VAT.
(ii)	(ii) Effectiveness of penalties for non-compliance with registration and declaration obligations	A	Penalties for all major taxes are set high enough to deter against non compliance with registration and filing. In addition SARS is empowered to bond the businesses revenues and bank accounts to cover any unpaid tax liabilities.
(iii)	(iii) Planning and monitoring of tax audit and fraud investigation programs	A	Tax audit and fraud investigation are based upon clear risks assessment criteria undertaken independently by the Business Intelligence. Audits are carried by the Audit Unit on the basis of cases prepared by the Business Intelligence. Reports are used to provide feedback from audits to risks assessment and for fraud investigation. The Customs post clearance inspections and audits are also selected independently by the Business Intelligence.
PI-15	Effectiveness in collection of tax payments	D+	
(i)	Collection ratio for gross tax arrears, being percentage of tax arrears at the beginning of a fiscal year, which was collected during that fiscal year	D	Although the collection of current debt is strong and well managed, historical debt is significant and not reduced. The total debt stock stands at 13% of revenue collection in 2006/07 and the collection ration is less than 30% in the last two years.
(ii)	Effectiveness of transfer of tax collections to the Treasury by the revenue administration	A	SARS operates a very efficient collection system that enables an effective transfer of tax collection to the Treasury Single Account daily.

No.	Indicator	Scoring	Brief Explanation and Cardinal Data used
(iii)	Frequency of complete accounts reconciliation between tax assessments, collections, arrears records and receipts by the Treasury	A	Reconciliations between tax assessment and collections and between collections and receipts by the Treasury are done daily. Reporting is done monthly in Section 32 within 30 days of the close of the month.
PI-16	Predictability in the availability of funds for commitment of expenditures	A	
(i)	Extent to which cash flows are forecast and monitored	A	Draw down schedules (cash flow forecasts) are prepared annually by the Departments. The Treasury informed by the pro forma cash flows and cash availability projections allocates funds on an annual basis by entering Draw Down Schedules at the vote, and programme level. These are updated monthly based upon updated cash flow projections. It is not clear that across all Departments the pro forma cash flows are prepared on the basis of detailed procurement plans.
(ii)	Reliability and horizon of periodic in-year information to MDAs on ceilings for expenditure commitment.	A	Departments are provided with an annual Draw-down schedules that reflect the annual Budget Forward Plans. These allocations are updated on a monthly rolling basis.
(iii)	Frequency and transparency of adjustment to budget allocations, which are decided above the management of Line Ministries	A	Due to effective budgetary allocation controls, all programme virements must be made subject to the approval of the National Treasury not exceeding 8% of programme estimate. Any re-allocations above this requires the approval of parliament .Typically an Adjustment Budget is submitted once a year in October.
PI-17	Recording and management of cash balances, debt and guarantees	A	
(i)	Quality of debt data recording and reporting	A	Comprehensive records on domestic and external debt are compiled and are updated and reconciled on a monthly basis. Comprehensive statistical reports providing information on debt stocks, debt service and debt management operations are prepared on a monthly basis.

No.	Indicator	Scoring	Brief Explanation and Cardinal Data used
(ii)	Extent of consolidation of the Government's cash balances	B	The payments system utilises the National Revenue Fund for all payments on Government expenditure (except for a number of grant funded project accounts). This facilitates a monitoring mechanism that reports and reconciles the account on a daily basis. All other outside of the RDP Fund account do not appear to be reported on even though progress reports and financial statements are submitted to the IDC on the implementation grant funded projects.
(iii)	Systems for contracting loans and issuance of guarantees	A	The contracting of loans and the issuing of guarantees are bound by transparent criteria. Targets are set within the Budget Review. Debt Management Strategy sets clear benchmarks. Debt is monitored and reported on against the strategy targets.
PI-18	Effectiveness of payroll controls	A	
(i)	Degree of integration and reconciliation between personnel records and payroll data	A	The application used in South Africa, PERSAL, allows for a direct link between the establishment and personnel and the payroll databases. Salary, promotions and allowances are criteria attached to a post, not to a person thus ensuring effective control.
(ii)	Timeliness of changes to personnel records and the payroll	A	Payrolls are controlled monthly and changes are effected within the next month pay period. Retroactive changes are rare and almost never extend beyond two pay periods.
(iii)	Internal controls of changes to personnel records and the payroll	A	The types of changes that can be made are restricted. Only authorised persons are granted access through passwords to PERSAL. All entries create an audit trail. All payrolls have to be verified monthly by the employee's supervisor.
(iv)	Existence of payroll audits to identify control weaknesses and /or ghost workers	A	Payroll audits are conducted routinely by the Internal Audit Unit and specific audits are performed by the Auditor-General. PERSAL has features that support physical audits.
PI-19	Competition, value for money and controls in procurement	D+	
(i)	Evidence of the use of open competition for award of contracts that exceed the nationally established threshold for small purchases	D	There is no central registry for procurement requirements and awards but the data generated by LOGIS, the procurement proprietary software, is stored in the Business Intelligence Platform of Treasury. Data was not retrieved during the assignment. Evidence submitted by the Department of Health suggests high level of compliance but this is insufficient to draw a conclusion on the national statistic.
(ii)	Extent of justification for use of less competitive procurement methods	D	The Act or Regulations do not clearly establish open competition as the default procurement method, with a requirement to justify less competitive methods when used. There is some indication that there is

No.	Indicator	Scoring	Brief Explanation and Cardinal Data used
			occasional abuse of emergency as a reason for circumventing competitive methods without adequate justification at year end when expenditure is rushed in a bid to prevent unspent funds being returned to the National Treasury.
(iii)	Existence and operation of a procurement complaints mechanism	B	A complaints mechanism exits and is functional. The Supply Chain Management Unit keeps a record of complaints and resolutions. Complaints are systematically responded to in order to settle matters or refer the case to a higher authority. Resolutions are not accessible to public scrutiny.
PI-20	Effectiveness of internal controls for non-salary expenditure	C+	
(i)	Effectiveness of expenditure commitment controls	A	Commitment control is a requirement of the PFMA and specific procedures have to be developed by Departments for all internal controls. The accounting software (BAS) provides a sound basis for ensuring an effective commitment control.
(ii)	Comprehensiveness, relevance and understanding of other internal control rules/ procedures	A	Other internal controls are well covered in the PFMA and the Treasury Regulations and manuals. Integration between the accounting and procurement management software support the application of rules. Departments have developed policies and procedures which are widely understood.
(iii)	Degree of compliance with rules for processing and recording transactions	C	Although compliance to rules is generally considered high according to the Internal Audit Units there are important concerns about the abuse of procurement rules to circumvent the use of competitive methods during what is referred as the March spike.
PI-21	Effectiveness of internal audit	A	
(i)	Coverage and quality of the internal audit function	A	The Internal Audit Function and its supervision by Audit Committees cover all Departments. The Internal Audit Units apply the IIA standards. The Internal audit unit prepare annual works plans that include process/full expenditure chain and procurement audits, payroll, compliance and financial audits, forensic, systems including IT audits and performance audits. At least 50% of the audit time is deemed spent on system audits.
(ii)	Frequency and distribution of reports	A	The audit reports carried out against a work plan are prepared and presented quarterly to the Departments through Audit Committees, the National Treasury and the Auditor-General.
(iii)	Extent of management response to internal audit findings	A	The Department management response to internal audit findings is complete and timely.
C(iii)	**Accounting, Recording and Reporting**		
PI-22	Timeliness and regularity of accounts reconciliation	B+	

No.	Indicator	Scoring	Brief Explanation and Cardinal Data used
(i)	Regularity of Bank reconciliations	B	All treasury managed bank accounts are reconciled to the cash book on a monthly basis within 10 days of the close of the month. There are other government accounts specifically donor funded project accounts which are not reconciled on a regular basis.
(ii)	Regularity of reconciliation and clearance of suspense accounts and advances	A	The reconciliation and clearance of suspense accounts is carried out monthly within 30 days of the end of each month. As part of the year end closing procedures all suspense accounts are force closed at the end of each year to facilitate the issuance of the annual financial statements.
PI-23	Availability of information on resources received by service delivery units	A	The front line service delivery units are managed by the nine provinces and five metropolitan authorities and their expenditure reported upon annually. The National Treasury compiles this data and presents it in a consolidated report: the Provincial Budgets and Expenditure Review.
PI-24	Quality and timeliness of in-year budget reports	C+	
(i)	Scope of reports in terms of coverage and compatibility with budget estimates	C	Comparison to the main budget is available at the vote and main economic classifications reported for both the current period and accumulated to date. Information includes all items of expenditure at the payment level but not at the commitment level.
(ii)	Timeliness of the issue of reports	A	Reports are prepared monthly by Departments and submitted to the National Treasury within 15 days of the close of the month. The National Treasury consolidates the submittals and publishes the consolidated report on its website monthly, within 30 days of the close of the month.
(iii)	Quality of information	A	Comparison to the main budget is available at the vote and main economic classifications reported for both the current period and accumulated to date. Information includes all items of expenditure at the payment level but not at the commitment level.
PI-25	Quality and timeliness of annual financial statements	A	
(i)	Completeness of the financial statements	A	A consolidated government statement, termed consolidated financial information is prepared annually. It includes all revenues and expenditures, liabilities and financial assets.
(ii)	Timeliness of submission of the financial statements	A	While the Departmental financial statements are submitted to the Auditor-General within two months of the end of the fiscal year, the consolidated financial information was submitted within 5 months of the close of the fiscal year to the Auditor-General for each of the three years reviewed during this assessment.

No.	Indicator	Scoring	Brief Explanation and Cardinal Data used
(iii)	Accounting standards used	A	The Accounting Standards Board of South Africa has been constituted to set and promulgate accounting standards. All financial statements disclose the accounting policies that have been employed.
C(iv)	**External Scrutiny and Audit**		
PI-26	Scope, nature and follow-up of external audit	B+	
(i)	Scope/nature of audit performed (incl. adherence to auditing standards)	A	The Auditor-General audits all Departments and public and constitutional entities every year within the specified period by law. He performs a full range of audits including systems, financial, compliance, procurement, IT and some performance related audits (without formal opinion). The Auditor-General adheres to the ISA and INTOSAI Standards.
(ii)	Timeliness of submission of audit reports to the legislature	B	The Auditor-General combines its audit of the institutions with the audit of their financial statements. As a result, audited financial statements are submitted to the legislature within three months from the receipt of the financial statements by the Auditor-General. The Auditor-General's Reports are submitted to the legislature within five months from the fiscal year-end.
(iii)	Evidence of follow-up on audit recommendations	B	Although a formal response is made in timely manner, there is no systematic evidence of corrective measures taken by the Executive.
PI-27	Legislative scrutiny of the annual budget law	A	
(i)	Scope of the legislature's scrutiny	A	The legislative review covers the details of revenue and expenditure estimates, a medium term expenditure framework, a medium term sector and fiscal policies including the impact of the changes in the new tax policy proposals.
(ii)	Extent to which the legislature's procedures are well-established and respected	A	The legislature's powers are enshrined in the Constitution and in the PFMA. The House rules govern a number of Budget Committees whose requirements are adhered to. Rules are generally clear and accessible.
(iii)	Adequacy of time for the legislature to provide a response to budget proposals (time allowed in practice for all stages combined)	A	The Legislature is involved both at the beginning and at the end of the budget cycle. The combined time that the legislature has to review the budget documentation is five months.
(iv)	Rules for in-year amendments to the budget without ex-ante	A	Clear rules exist for in-year amendments without ex-ante approval. Excessive virements and

No.	Indicator	Scoring	Brief Explanation and Cardinal Data used
	approval by the legislature		expenditure over budget ceiling require the approval of the National Assembly of an Adjustment Budget.
PI-28	Legislative scrutiny of external audit reports	B+	
(i)	Timeliness of examination of audit reports by legislature (for reports received within the last three years)	A	A review of all departments' Annual Reports is done within two months from submission prior to the start of the formal in depth hearings.
(ii)	Extent of hearings on key findings undertaken by legislature	A	Public Hearings are conducted for the departments where serious concerns are identified e.g. adverse or qualified opinion. The hearings are thorough and are publicly accessible. In addition to this process, SCOPA has rules to ensure that each department is summoned at least once every three years.
(iii)	Issuance of recommended actions by the legislature and implementation by the executive	B	Actions emanating out of the SCOPA hearings are always recommended to the Departments, but these are not systematically implemented which leads to some implementation delays and omissions.
D.	**DONOR PRACTICES**		
D-1	Predictability of Direct Budget Support	D	
(i)	Annual deviation of actual BS from the forecasts provided by the donor agencies at least 6 weeks prior to the government submitting its budget proposals to the legislature	D	In at least two of the three years considered the actual budget support outturn fell well below 15% of the forecast amounts. The forecasts are provided only at the time of signing the FA which does not necessarily occur at least 6 weeks prior to the submittal of the budget to the legislature.
(ii)	In-year timeliness of donor disbursements (compliance with aggregate quarterly estimates)	D	The actual "weighted disbursement delays" are well in excess of 50% for each of the years reviewed.
D-2	Financial information provided by donors for budgeting and reporting on project and program aid	D	
(i)	Completeness and timeliness of budget estimates by donors for project support	D	The Government of SA does not have comprehensive and reliable information on the value and composition of all donor assistance provided to the Government. While all major donors channelling funds through the RDP Fund (which represent less than 25% of all donor funds) provide data on pledges, commitments or available funding, they do not provide actual budget estimates informed by fully developed procurement plans and absorptive capacities pertaining to realistic schedules of project implementation. These budget estimates are not aligned to the SA budget cycle.
(ii)	Frequency and coverage of reporting by donors on actual donor	D	A few donors provide data on actual disbursements to national departments and/or National Treasury

No.	Indicator	Scoring	Brief Explanation and Cardinal Data used
	flows for project support		(IDC). Most donors however do not provide any financial quarterly reports. In some cases annual financial reports are provided.
D-3	Overall proportion of aid funds to central government that are managed through national procedures	D	Donor funds channelled through the RDP Fund amounted to approximately 1 billion Rand in 2007/08 which according to verified estimates represent about 25% of the total estimated donor funds. So, 75% of the funds did not use national systems.

Annex 3 List of Stakeholders Interviewed

Name	Organisation	Position
National Treasury		
Kuben Naidoo	NT, Budget Office	Head: Budget Office
Dr. Kay Brown	NT, Budget Office	Chief Director: Budget Planning
Raquel Ferreira	NT, Budget Office	Director: National Budgets Budget Planning: Budget Office
Rathipe Nthite	NT, Budget Office	Chief: Expenditure Planning Unit
Matthew Simmonds	NT, Budget Office	Chief Director: Fiscal Policy Unit
Hennie Swanepoel	NT, Budget Office	Chief: Public Finance Statistics Unit
Chad Chaponda	NT, Budget Office	Chief: PPP unit
Kogan PIllay	NT, Budget Office	Director: Business Development, PPP Unit
Robin Toli	NT, Budget Office, IDC Unit	Chief: IDC Unit
Thulani Mabaso-Mahlangu	NT, Budget Office, IDC Unit	Senior Policy Analyst, Portfolio Manager for EC funds
Luyanda Yaso	NT, Budget Office, IDC Unit	Senior Policy Analyst, Portfolio Manager for EU Member States funds
Andrew Donaldson	NT, Public Finance Division	Head: Public Finance Division
Robert Clifton	NT, Public Finance Division	Budget Advisor
Umesh Natha	NT, Public Finance Division	Director
Liesel Smith - Eksteen	NT, Public Finance Division	Acting Chief: Governance & Administration Unit
George Tembo	NT, Public Finance Division	Governance and Administration Unit; Director: DPLG, DPW & SAMDI
Julia de Bruyn	NT, Public Finance Division	Chief: Social Services Unit
Lungisa Fuzile	NT, Intergovernmental Relations Division	Head: Intergovernmental Relations Branch
Kenneth Brown	NT, Intergovernmental Relations Division	Intergovernmental Policy and Planning
Phakamani Hadebe	NT, Assets and Liability Management Division	Deputy Director-General Head: Assets and Liability Management
Johan Redelinghuys	NT, Assets and Liability Management Division	Chief Director: Financial Operations Unit
Ravesh Rajlal	NT, Assets and Liability Management Division	Director: Transport and Defence (financial oversight of SOE)
Anthony Julies	NT, Assets and Liability Management Division	Strategy and Risk Management Unit
Henry Malinga	NT, Special Functions Division	Chief Director: Supply Chain Policy Unit
Bobby Maake	NT, Special Functions Division	Chief: Financial Systems Unit

Name	Organisation	Position
Beerson Baboojee	NT, Office of the Accountant - General	Chief Director: Risk Management
Johan Wagener	NT, Office of the Accountant - General	Director: Accounting Services
Kobus van Wijk	NT, Office of the Accountant - General	Office of the Accountant - General
Nols Du Plessis	NT, PFMA Implementation Unit	Chief Director
South African Revenue Service (SARS)		
Edward Chr. Kieswetter	SARS	Chief Operations Officer
Franz Tomasek	SARS	General manager: Legal and Policy
Randall Carolissen	SARS	General Manager: Operations, Standards and Policies
Mamiky Leolo	SARS	Revenue Analysis
Deon Breytenbach	SARS	Revenue Analysis
Andrew Fisher	SARS	Revenue Analysis
Marius Potgeiter	SARS	Revenue Analysis
Mvusi Mguyane	SARS	Business Intelligence Unit
Clifford Cadlings	SARS	Anti-corruption and Security
Jonas Makwakwa	SARS	General Manager Enforcement Unit
Desrae Laurence	SARS	Enforcement Unit
Leornard Radebe	SARS	Customs
Rudolf Matatenkrock	SARS	Criminal Investigations
Etienne Pillay	SARS	Compliance Risk, Business Intelligence Unit
Annie Naidoo	SARS	Operations Support (legal)
Rae Cnukshank	SARS	Customs Trader Management and Trader Compliance
Fabian Murray	SARS	General Manager Performance Management
Mike Kingon	SARS	General Manager Operations Support
Thinus Marx	SARS	General Manager National Operations
Department of Education (DOE)		
Theuns Tredoux	Financial Support Services	Chief Director
Lizette Wook	Staffing Services	Director
Anton Schoeman	Personnel Administration and Development	Director
Ntsetsa Molalekoa	Financial Services	Senior Officer
Patel Firoz	System Planning and Monitoring	Deputy Director General
F.C. Mavuso	Supply Chain Management	Chief Director
P. Du Toit	Internal Audit	Senior Auditor
G. B. Modise	Provincial Budget Monitoring and Support	Senior Officer
J. Wakefield	Financial Services	Senior Officer
A. Poolman	Financial Services	Senior Officer
G. Maaka-Tlokana	Development Support Coordination of grants and donors	Director
Department of Health (DOH)		

Name	Organisation	Position
Gerrit Muller	DOH	Chief Financial Officer
Martin Komape	DOH	Deputy Chief Internal Audit
Edu Combrinck	DOH	Procurement Unit
Abel Masemola	DOH	Chief Internal Audit
Department of Public Works (DOPW)		
James Radebe	DOPW	Internal Audit
Ntumisheng Mokgoatjane	DOPW	Payroll
Ronel Mostert	DOPW	Payroll, Human Resource Management
Thapeco Motsoeneng	DOPW	Acting Chief Financial Officer
Jerry Shaga	DOPW	Strategic Management Unit
Department of Provincial and Local Government (DPLG)		
Mbulelo Sigaba	Finance and Supply Chain Management	Deputy Chief Financial Officer
William Ramphewe	Municipal Finance Monitoring	Senior manager
Chaka Moloto	Demand and Management	Acting Senior Manager
Masilo Mathura	Financial Accounting Service	Senior Manager
Department of Public Enterprises		
Hanlie Bedford	Department of Public Enterprises	Director: Financial Management
Department of Public Service Administration		
Kenny Govender	Management of Compensation Branch	Branch Head
Edward Harris	Remuneration Policy Directorate	Senior Officer
Auditor-General Office		
Jan van Schalkwyk	Auditor-General Office	Business Executive: Audit Research and Development
National Assembly		
Themba Godi	Standing Committee on Public Accounts	Member of Parliament, Chairman
Louisa Lerato Mabe	Joint Budget Committee	Member of Parliament, Chairperson
South African Reserve Bank		
Dr. Johan Van Den Heever	South African Reserve Bank	Head Research Department
Gerrie Terblanche	South African Reserve Bank	Head: Financial Services Department
Philip Franken	South African Reserve Bank, Financial Services Department	Assistant General Manager
Donors		
Gerard McGovern	EC Delegation to South Africa	Head of EC Delegation
Hubert Perr	EC Delegation to South Africa	Counsellor (Development)
Gerhard Plenaar	EC Delegation to South Africa	Project Officer
Cas van der Horst	Embassy of the Kingdom of the Netherlands	Counsellor / Co-ordinator Development Aid Head Socio-Economic Co-operation
Cornelius Hacking	Embassy of the Kingdom of the Netherlands	First Secretary, Education Expert, Socio-Economic Co-operation
Nick Amin	DfID	Senior Economic Advisor
Gillian Oroni	DfID	Programme Officer: Livelihood and Health
Rokia Banda	DfID	Assistant Programme Officer

Name	Organisation	Position
Pinky Pheeloane	DfID	Programme Officer: Growth, Trade and Investment
Karen Terblanche	DfID	Deputy Programme Manager: Growth, Trade and Investment
Lelanie Swart	DfID	Programme Manager
Steve Burton	DfID	Deputy Programme Manager: Resilient Livelihoods
Rejean Hamel	Government of Canada, High Commission	Counsellor (Development)
Jean-Didier Oth	Government of Canada, High Commission	Second Secretary (Development)
Ernst Hustadt	GTZ	Public Sector Reform Sector Coordination Good Governance: Programme Manager
Gert van der Linde	The World Bank	Senior Financial Management Specialist
Sean Nolan	IMF	Senior Resident Representative
Monica Moore	USAID	Regional Program and Project Development, Project Development Officer
Pitsi Semenya	USAID	Budget Specialist
Naoyuki Nemoto	JICA	Assistant Resident Representative
Iwao George Sakurai	JICA	Project Formulation Advisor
Civil Society Institutions		
Etienne Yemek	Institute for Democracy in South Africa (IDASA)	Senior Policy Analyst
Russel Wildeman	Institute for Democracy in South Africa (IDASA)	Programme Manager
Bill Lacey	South African Chamber of Commerce and Industry (SACCI)	Consultant - Economic Affairs
Michael McDonald	Steel and Engineering Industries Federation of South Africa (SEIFSA)	Manager: Economic and Commercial

Annex 4 List of Documents Consulted

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- National Treasury, Statement of the National Revenue, Expenditure and Borrowing, May 31 2008
- National Treasury, Schedule of Domestic Government Bonds, June 30 2008
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- National Treasury, The Risk Analysis of Government Explicit Contingent Liabilities of Selected SoEs as at 31 March 2007, Assets and Liabilities Division, 2008
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- National Treasury, Consolidated Financial Information 2005/2006, 2006/2007 and Draft Consolidated Financial Information 2007/2008
- National Treasury, Local Government Budgets and Expenditure Review 2008 (2003/04 – 2009/10)
- Free State Province, Budget Statement 2008/2009

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- Department of Education, Risk Analysis
- Department of Education, Audit Plan for 2007/08
- List of Procurements 2008/09, Department of Health
- Three-Year Strategic Plan, Internal Audit, Department of Health
- Annual Operational Plan 2006/2007, Internal Audit, Department of Health
- National Annual Health Plan 2008, Department of Health
- Department of Health Annual Report 2006/2007
- Department of Public Enterprises, Annual Report, 2006-2007
- Strategic Plan 2008/09 – 2010/11 Department of Health
- Report of the Auditor-General 2007/2008 Department of Provincial and Local Government
- Cash Flow Statement 30 June 2008 (shows commitments) Department of Education
- Strategic Plan 2007-2012, Department of Provincial and Local Government
- Business Plan 2008-09, Department of Provincial and Local Government

- Strategic Plan 2008 – 2012 and Operational Plans 2008-2009, Department of Education

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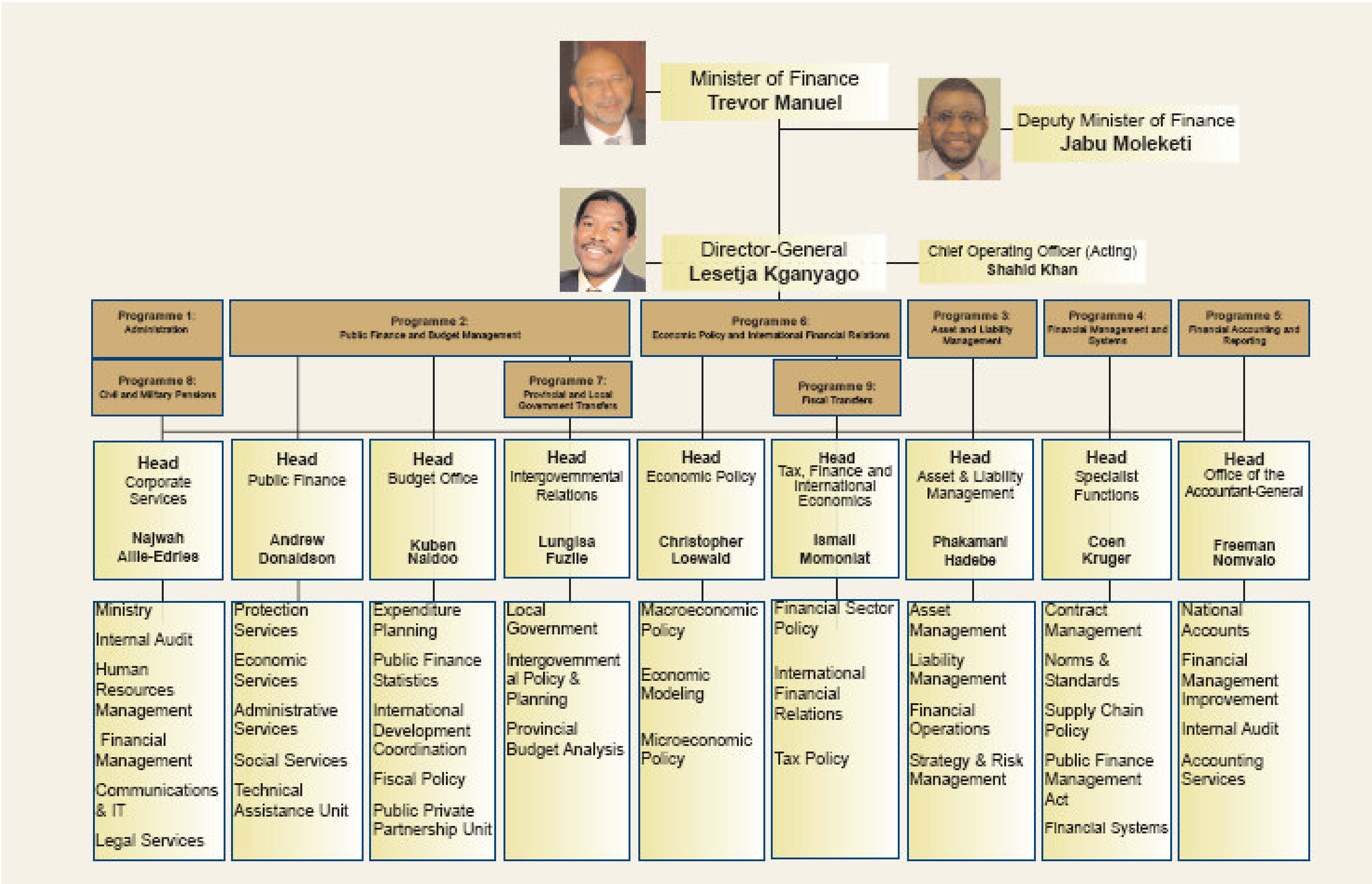
Annex 5 Organisational Chart of the MOF



Annex 6 Comments and Responses on the Draft Report on the PEFA Assessment

Overall impression

PEFA Secretariat

Comment 1.1

The overall quality of the report is very good. The structure of the Performance Measurement Framework is closely followed. The scoring of the performance indicators under Section 3 is generally well-supported by evidence, the sources of which are generally well-identified. The Summary Assessment is well prepared, though, at 17 pages, it is considerably longer than the 3-4 pages recommended in the Framework document.

Response 1.1

A number of factors in the case of South Africa are unique and limit the conclusions that can be drawn of a PEFA Assessment. Addressing these unique factors contribute to the length of the report. Further, the EC has emphasised that the PEFA provides an opportunity for insight and should not be restricted to a tick box exercise. The objective of providing insight to the operation of a rather sophisticated PFM system has resulted in a rather long Summary Assessment. That said, every opportunity to clarify the text has been taken to provide a fully readable final version.

Government of South Africa

Comment 1.2

There is general agreement with the findings of the Public Expenditure and Financial Accountability (PEFA) assessment. However, in respect of the draft report certain issues need to be expanded upon and certain points noted.

Response 1.2

The consultants through follow up meetings have worked with Government officials to further clarify issues in the draft pointed to in the Government's comments. Further, all of the points to be noted have been incorporated into the final report.

Comment 1.3

While acknowledging that the PEFA performance measurement framework is a standardised assessment tool, the point needs to be made that one could criticise the methodology in many respects. However, the standardised methodology is taken as given. There are however, a few instances in which it should be noted that South Africa scores badly and it could be argued that these scores appear to be worse than they are given SA's PFM history, policy choices and planned reforms.

Response 1.3

Indeed for a standardised PFM assessment framework that is based upon high level indicators such as the PEFA assessment tool, there may be instances where the tool does not fully and appropriately capture performance. However, the tool's robustness and consistency would still permit comparisons of progress over time, even if each specific scoring was considered biased. Of course the narrative can and should seek to clarify the particular circumstances that can lead to such bias. Indeed this has been the case in a number of instances such as in the narrative for PI-4 on expenditure arrears, PI-15 (i) that addresses tax arrears, PI-19(i) that addresses open competition in procurement.

Comment 1.4

There are also instances in which the report notes areas for PFM improvement, which are not strictly the subject of PEFA assessments. While the assessment stays at a high level, as it uses high level indicators, the narrative alludes to some practices that are at lower level, which may make the PEFA assessment appear to be more subjective. It is not argued that any of these is excluded from the report, it is however requested that these are captured in the narrative report in a way that accurately reflects the policy and other developments in SA PFM.

Response 1.4

It is absolutely correct that there should be no areas alluded to for PFM improvement since the PEFA methodology in keeping with the "Strengthened Approach" intentionally does not include recommendations. All such allusions are inappropriate and every effort has been made to remove all of them. Two instances were found in the draft that could have been interpreted as suggesting an area for improvement and the narrative has been rephrased to point to the weakness rather than suggest it to be an area for improvement. Any such allusions that might remain in the final version are in error and are the responsibility of the authors.

The narrative provides an opportunity to take the PEFA Assessment beyond a tick box exercise and provide some insight to the underlying causes for the observed strengths and weaknesses. It does not pretend to be a full blown diagnostic tool, but there are some aspects of lower level practices that illuminate what is observed at the higher level and these are important. If however, and such observations or analysis presented in the narrative are inaccurate or purely speculative then of course these have no place in the final report. The authors have been very careful to only include lower level information that is backed by evidence. At the very minimum only information and analysis that could be corroborated by a number of reports and audit findings as well as comments provided through interviews with civil society organisations were included. Given that, *Comment 1.4* does not argue these to be excluded from the report, it is presumed that there is agreement that this standard of evidence backed observation and analysis has been maintained.

Comment 1.5

A general point that can be made is that the introduction of the MTEF was more to provide departments with certainty and continuity in respect of funding, so as not to hamper their planning ability, rather than being to allowing the reallocation of resources to new programmes.

Response 1.5

One of the rationales for introducing MTEF is the opportunity it provides in allowing the reallocation of resources to new programmes. If this was not explicitly one of the reasons for the adoption of MTEF in South Africa it should not preclude it, as the narrative suggests, from benefiting from increased opportunity for more efficient reprogramming.

Summary Assessment

PEFA Secretariat

Comment 2.1

The summary assessment is of good quality, though it would benefit from being shortened. Some apparent anomalies could be explained: (i) why the March spike occurs, despite the detailed monthly cash flow forecast that must be made at the beginning of the new fiscal year and the emphasis given by the Supply Chain Management Unit on the need to prepare procurement plans in line with the approved budget: (ii) why arrears are increasing each year, despite the commitment controls under BAS; and (iii) why expenditure commitments are not reported on under the in-year reporting system. A concluding paragraph containing a “story line” that succinctly sums up PFM performance and the key challenges that lie ahead would be useful.

Response 2.1

Without procurement plans to properly address a reasonable time horizon on cash flow requirements, cash flow projections remain effective only in the short term. When the end of year arrives, Departments without having carefully focussed on payment commitment profiles and procurement plans find themselves under pressure to spend, otherwise risk losing budgeted funding. This probably contributes to the bypassing of procurement controls in some cases and delayed issuances of general purchase orders which may not accommodate the full time required to effect a complete procurement expenditure cycle, which can then contribute to expenditure arrears.

One of the contributing factors to National Departments not adhering closely to sound procurement practice may be the very small proportion (approximately 7%) of expenditure that employs the procurement vehicle. Indeed at an aggregate level the observance of a March Spike is more a characteristic of late transfers to provinces and Local Authorities rather than the contributions made to a March spike (at an aggregate level) due to procurement practice anomalies.

It would appear that expenditure commitments have not been reported upon across all National Departments because the monthly expenditure reporting requirements are supposed to be made in accordance with the format of Section 32 which does not at the present time include commitment expenditure reporting. However, the information is available and indeed some Departments, such as the Department of Education, incorporate it in internal management reports.

Government of South Africa

Comment 2.2

The report notes that a PEFA assessment of SA is anticipated every 3 to 4 years, no such undertaking exists. Further it should be noted that SA PFM progress is being monitored by various means, including by a number of domestic and international studies. It would probably be more appropriate to note that the PEFA assessment will be a good basis for measuring PFM progress **in respect of donor funding**. The point has been made that a PEFA assessment of provinces would provide a more complete picture and should be considered, not necessarily that the PEFA assessment will be extended.

Response 2.2

The narrative has been improved to clarify the point that it is the PEFA methodology that anticipates that assessments be carried out every three to four years, rather than implying that the South African government has given any undertaking to carry out any future PEFA Assessments. It also makes clearer that the methodology could be extended to the Provinces, but does not comment upon whether or not the government desires to do so.

The European Commission

Comment 2.3

Page 13. top paragraph. The consultants clearly see *lack of predictability* of donor funds as a problem – this will be discussed in the comments on the donor practices section. The weaknesses in procurement and expenditure management are clearly a problem that the donors should look into and provide support for - it seems that this should be part of all of our programmes.

Response 2.3

This is clearly an area that if improved upon would impact positively donor practices and consequently PFM practice in South Arica.

Comment 2.4

Page 14, 2nd paragraph. The issue of procurement planning is important and again we should be providing support in this area in future.

Response 2.4

This would support an area of PFM weakness.

Comment 2.5

Page 15, 2nd paragraph. With so many donors and so many systems it would be difficult to have a standard. We think most donors would have the information required. Maybe what we should be looking at is some standard presentation to government over and above the donor systems - this should then provide government with the information they require for budget planning.

Response 2.5

Whatever the standard different donors might adopt for defining pledges, they could all respond to a standard definition of what is expected of a budget estimate as defined by the host country. This would lead to more consistent budget estimate submittals.

Comment 2.6

Page 21, 2nd paragraph. What is said here is of great concern and is confirmed later in a table (Table 3.11, Page 86). It appears that government are not following their own procurement procedures especially when it comes to open competition. This is clearly against EC rules and in our view could potentially cause problems with giving SBS.

Response 2.6

It would be inaccurate to conclude that government are not following their own procurement procedures especially when it comes to open competition. Table 3.11 is in error and reflects the exact opposite that was intended. It has been corrected to show that the Department of Health comply very closely with open competition requirements.

However, as the report states; there is concern that there appear to be some weaknesses in the procurement legal and regulatory framework and there is indication of some abuse pertaining to open competition, but that does not mean that for the most part government is not following open competition. Indeed interviews with two civil society organisations suggest that there is a perception that public procurement is perceives as accessible and competitive.

Comment 2.7
Page 21, 4th paragraph. What is said here about release of donor funds is very unbalanced. What is said may well be true but the experts should explain the reasons, which are usually because government do not meet the payment conditions on time.
Response 2.7
While there are of course important issues of governance that might be tied to budget releases, PEFA focuses on the net result. There is a combination of reasons for delays that was cited including the government not having met some conditionalities. However it should also be noted that should there be governance issues that preclude a given country from meeting the disbursement conditionalities, then budget support is not the appropriate aid delivery method to adopt because the net result is to introduce unpredictability to budget releases which undermines sound PFM.

Comment 2.8
Page 24, 1st paragraph. This again stresses the problems with *implementation* of the budget which have not been looked at and also the procurement problems.
Response 2.8
This might be an area for dialogue with the government.

Comment 2.9
Page 24, Point 1. The concurrent roles of all three spheres of government and not just central and provincial should be mentioned. This is further complicated by there being two pieces of legislation - the PFMA and the MFMA.
Response 2.9
The Provincial Budgets and Expenditure Review describes concurrent functions strictly for central government and provincial government and does not extend such concurrency to local government. The interpretation adopted in this PEFA Assessment is consistent with the National Treasury interpretation as expressed in the Provincial Budgets and Expenditure Review. It should be noted that there are institutional arrangements that manage such concurrency between the national and provincial budgets.

While there are some minor discrepancies between the PFMA and MFMA, the authors are of the general opinion that the two acts strengthen rather than undermine PFM practice in South Africa.

Comment 2.10
Page 25. Strategic allocation of resources. The second sentence is highly relevant and an area where donors should be providing support especially in our SBS programmes.
Response 2.10
This might be an area for dialogue with the government.

Section 1 – Introduction

PEFA Secretariat

Comment 3.1

The introduction is well-prepared. In indicating the purpose of the mission (to prepare a PFM-PR on the national government) it could be emphasised why the assessment report is relevant, even though the national government covers only 30 percent of the public sector. The first page of the Summary Assessment appears to indicate that the usefulness of the assessment is somewhat limited due to the limitation in scope. Perhaps the justification for the study could be put in a more positive light. For example, the common use of the BAS across national and provincial governments might suggest that PFM in provincial governments is related to PFM in the national government, so that the assessment of national government alone provides some indication also of PFM performance in provincial governments.

Response 3.1

The limitation in proportion of expenditure as well as PFM function is a crucial and important qualification to be made in concluding on PFM practice in South Africa on the basis of this PEFA Assessment applied at the central government level. It is not to cast this PEFA assessment or PFM systems, practices and procedures in a negative or positive light; but rather to make the reader aware to the fact that for the reasons outlined this PEFA assessment is a partial assessment of Public Finance Management. Without a clear appreciation of such limits, the reader might make conclusions about PFM in South Africa that would be wrong. Should, PEFA Assessments be carried out in the Provinces, the picture provided would be more complete and permit conclusions more reflective of PFM and practice in South Africa. Further, an appreciation of this point goes a long way to explaining how credibility of the budget is achieved as predicted by the PEFA methodology, in spite of exposed weaknesses in such areas as expenditure payment arrears, procurement planning or regular commitment expenditure reporting.

It should be emphasised, that the mere fact that provincial governments utilise PERSAL and BAS is not sufficient to make any conclusions (based upon evidence) about the performance of PFM at the provincial level. To do so would be highly speculative.

Section 2 – Country Background Information

PEFA Secretariat

Comment 4.1

This is well-prepared. Some specific points:

- Table 2 does not provide information on 2007/08, though the scope of the review is supposed to include it. Table 2 also seems inconsistent as the financing does not equal the budget balance. It would be useful to include debt/GDP statistics;
- Could mention that BAS only covers national and provincial governments.

Response 4.1

At the time of the field mission in a number of instances only revised estimates rather than actuals were available. The tables have been modified to include revised estimates where actuals were not yet available.

A line that reports on debt/GDP statistics has been added to the table.

A sentence in the description of the Financial Systems has been introduced to note that the BAS financial management system covers national and provincial governments.

Section 3 – Performance of systems, processes and institutions

PEFA Secretariat

Comment 5.1

This section closely follows the structure contained in the Framework document and is generally well-prepared. We have specific observations on the need for additional evidence to support the scoring as well as on the correspondence between evidence provided and score given for some of the individual indicators, as highlighted in the table below.

Response 5.1

Each of the specific comments are addressed in the table following.

Government of South Africa

Comment 5.2

A general point that can be made is that the introduction of the MTEF was more to provide departments with certainty and continuity in respect of funding, so as not to hamper their planning ability, rather than being to allowing the reallocation of resources to new programmes.

Response 5.2

One of the rationales for introducing MTEF is the opportunity it provides in allowing the reallocation of resources to new programmes. If this was not explicitly one of the reasons for the adoption of MTEF in South Africa it should not preclude it, as the narrative suggests, from benefiting from increased opportunity for more efficient reprogramming.

	Comments on the rating	Response
PI-1	**PEFA Secretariat:** The A rating appears correct, based on the evidence. The decision to include the small amount of donor aid in primary expenditure justified.	The out turn for 2007/2008 has been corrected which eliminates the inconsistency observed in the Table under PI-2.
	Changes made to the narrative and / or scoring: No changes made to the scoring. Correction made to data in table and changes made to the narrative.	
PI-2	**PEFA Secretariat:** The ‘A’ rating appears correct, based on the evidence. There is an inconsistency between actual expenditure for 2007/08 and the figure in the table under PI-1, but this should not affect the rating. It seems odd that procurement planning is weak, given the Supply Change Management Unit in National Treasury which encourages procurement planning.	The correction in the outturn for 2007/2008 eliminates the inconsistency. Interviews were carried out with four different National Departments during the field mission. The picture portrayed was that there was only very limited procurement planning carried out.
	Changes made to the narrative and / or scoring: No changes made to the scoring or to the narrative.	
PI-3	**PEFA Secretariat:** A rating appears correct, based on the evidence, but the actual revenue figure for 2007/08 is missing in the table.	No changes made.
	Changes made to the narrative and / or scoring: No changes made to the score or to the narrative	
PI-4	**PEFA Secretariat:** The A, A and overall A ratings appear correct, based on the evidence. What is the reason for the increase in arrears each year? It is not clear from the narrative how arrears can accumulate, given that purchase orders can only be issued through BAS. As mentioned under PI-2, it is also not clear why procurement planning is weak, given the long time horizon allowed to make commitments, the procurement legislation and the Supply Chain Management Unit. Also not clear why there is no information on	No change in the scorings. Arrears can accumulate (and do accumulate) if and when there is a rush to spend at the close of the year. Commitments are made too close to the end of the year to complete payments before the close of the year. These get carried over to the next year and are booked as outstanding payments. Should these outstanding payments remain for more than 30 days into the new year, then they are accounted for as arrears. The narrative has been changed to make the point clearer.

	Comments on the rating	Response
	commitments entered to, when purchase orders can only be issued through BAS.	At this stage Section 32 reporting does not include commitment reporting. As stated in the narrative some Departments such as Education prepare monthly expenditure reports for their own requirements that do include commitment reporting; however this is not the case across all Departments.
	An interesting point is made about the stock of arrears relative to total Department spending (i.e. excluding transfers to SNGs) instead of total govt. expenditure. But the impact on budget credibility has to be looked at in terms of the magnitude of arrears relative to total expenditure, as arrears payments are financed out of the overall resource envelope representing the total expenditure ceiling.	Yes this is true in strict accordance with the PEFA methodology. It is however possible to get caught in the trap of limiting credibility of the budget considerations solely to aggregate dimensions. However, given the concurrent roles it is critically important that all the corresponding roles and responsibilities be met. For the central government such responsibilities include expenditure beyond transfers and debt service. Surely there would be little budget credibility if for example only half the staff were paid in a timely manner (or paid at all) even though given the small ratio of personnel emoluments in the central budget this budget credibility undermining feature would not be significantly exposed in the aggregate numbers.
	Government of South Africa: EXPENDITURE ARREARS: As noted the report mentions expenditure arrears, its impact on PFM and that this might be a response to the March Spike phenomenon. However, in investigating these arrears, where the data used for calculating the arrears to expenditure ratios is extracted from the consolidated financial information, it is clear that most of the arrears, about 90%, are older than 3 years. This relates to old arrears dating back to pre 1994 which have never been written off and has no bearing on the current PFM system.	The expenditure arrears data shows an almost tripling over the three years considered (see Table 3.6) This however is not consistent with 90% being more than three years old. There it ought to be considered relevant to the current PFM system.
	The report also concludes that there is growth in arrears over the period. This growth in arrears over the 3 year period is mainly due to the introduction of reporting on such arrears in the financial statements of departments. It is only since 2005/06 that arrears have been included in the financial statements and most of the growth in arrears up to 2007/08 can be attributed to the disclosure of arrear accounts, which were previously not reported on, and should therefore not be viewed as an increase in arrear accounts, but rather as improved	While arrears have only been included since the start of the period considered for the PEFA Assessment and so may reflect a spurious effect in terms of merely reflecting the improved disclosure of arrears and hence the apparent the rate of growth of expenditure arrears, given the source to be audited financial statements, whose noted do not mention the figures to portray a partial picture, it would be surprising if these figures were not reasonably representative. If not it would raise some question as to the reliability of the audited financial statements.

	Comments on the rating	Response
	disclosure of arrears in the financial statements.	
	Changes made to the narrative and / or scoring: No change made to the overall scoring. Changes made to the narrative to improve clarity.	
PI-5	**PEFA Secretariat:** The A rating appears correct, based on the evidence.	No changes made.
	Changes made to the narrative and / or scoring: The indicator's scoring is left unchanged. Minor changes made to the narrative.	
PI-6	**PEFA Secretariat:** The A rating appears correct, based on the evidence. It is not clear whether elements 4 and 5 are met in terms of details being provided for the beginning of the current year, but 7 of out 9 benchmarks met still justifies an A rating	The narrative has been made clearer to support 9 bench marks being met.
	Changes made to the narrative and / or scoring: The indicator rating is not changed. The narrative has been changed.	
PI-7	**PEFA Secretariat:** The A, A and overall A ratings appear correct, based on the evidence. **Government of South Africa:** EXISTANCE OF EXTRABUDGETARY ACTIVITIES: It is acknowledged that generally this is a contentious area. The PEFA indicator measures evidence of unreported extra-budgetary activities. There is no evidence of any such activities in South Africa. However in terms of the PEFA measurement framework, lack of evidence of possible extra-budgetary activities is not taken by the assessment to automatically denote non existence of such activities. In relation to this particular matter, it has been noted that donor funding is not properly reported on. To clarify it should be said that donor funding is reported upon, although the reporting is not fully consolidated within the budgetary processes, as the largest proportion of donor funding is in the form of "in-kind" support. The PEFA assessment does not reflect this nuance. Technically, the	It ought to be clarified that the PEFA Assessment methodology makes no comment upon whether "lack of evidence of possible extra-budgetary activities is not taken by the assessment to automatically denote non existence of such activities". However, there is some difficulty posed by an approach that is evidenced based to make the case for an A by arguing that there is no evidence of extra-budgetary activities that remain unreported. A distinction should be made between the donor activities tracked and managed through the RDP fund. These are properly budgeted for and reported on. However, what this assessment also reveals is that there is substantial donor activity representing approximately about 75% of donor funds that are managed outside of the RDP that are for the most part not reported on.

	Comments on the rating	Response
	2008 Budget should not form part of the review as the review focuses on the 2005/06 to 2007/08 financial years, while the 2008 Budget focuses on 2008/09. Therefore as in the 2007 Budget Review, and ENE donor funding was presented as part of the consolidated budget framework including “in-cash” and “in-kind” allocations. It is only in respect of the subsequent financial year that donor funding was not reported on.	
	Given the small quantum of donor funding in SA, this does not merit disproportional mention in the report – especially given that the report contains a section on assessing donor support. For example, the impact of poor donor funding reporting is also captured in PI-17(ii), where PEFA draws upon this (weakness) to assess consolidation of the Government‘s cash balance.	While it is true that donor funding in South Africa represents a small quantum of total expenditure, it is important to appreciate that donor activity does have an important impact on PFM in a given country with respect to PFM systems and procedures. Our best estimates suggest that donor activity is just barely below the 1% threshold that automatically scores this sub indicator (PI-7(ii)) an A. We note that even small increases in donor funding could take it above the threshold and if this were done, without significant improvements in tracking there would result an automatic decrement in the overall rating of PI-7 from A to C+.
	Changes made to the narrative and / or scoring: The indicator rating is not changed.	
PI-8	**PEFA Secretariat:** A, A, D ratings and overall B rating appears correct, based on the evidence.	The D has been changed to B with an overall rating change to B. Evidence on consolidated financial reporting for local authorities was provided and this has resulted in a review of the assessment of the transparency of intergovernmental relations.
	Table 3.7 could be clarified to explain that the figures for provincial government and local governments represent transfers from national government. It would be useful to indicate how totals relate to total national govt. revenue shown in PI 3.	The title to table 3.7 refers to the “Division of national revenue between central government and sub national government”. Table 3.8 refers to revenues including own revenues as allocated between levels of SNG.
	The meaning of reference to Regional Councils in first paragraph is unclear. The meaning of footnote 24 is unclear. It is unclear why own revenue of local government is referred to, but not own revenue of provincial governments.	This sentence is in error and has been deleted. Footnote 24 is no longer relevant since actual data for Local Authorities has been provided. Provincial government revenue is derived solely form central government transfers.

	Comments on the rating	Response
	Changes made to the narrative and / or scoring: The overall indicator rating has been changed from B to A. Changes to the narrative have been made.	
PI-9	**PEFA Secretariat:** The B, A and overall B+ ratings appear correct, based on the evidence, assuming that central government cannot guarantee loans to provincial governments (the narrative only specifically mentions that central government cannot guarantee loans to local authorities).	The central government cannot guarantee loans to the provincial government. Further, the Local Government Budgets and Expenditure Review, and the Provincial Budget Review provides fiscal and debt information and provides an overall fiscal risk assessment.
	Changes made to the narrative and / or scoring: The indicator rating is not changed. The narrative has been changed to reflect additional evidence provided on local authority financial reporting.	
PI-10	**PEFA Secretariat:** The A rating appears correct, based on the evidence, provided that tender awards are published soon after the awards are made.	No changes have been made to the scoring or the narrative.
	Changes made to the narrative and / or scoring: The indicator rating is not changed. No changes have been made to the narrative.	
PI-11	**PEFA Secretariat:** The A, A, D and overall B ratings appear correct, based on the evidence.	No changes have been made to the scoring or the narrative.
	Changes made to the narrative and / or scoring: The scoring remains unchanged. No changes have been made to the scoring or the narrative.	
PI-12	**PEFA Secretariat:** The A and A ratings for dimensions (i) and (ii) appear correct, based on the evidence. It is not clear what is meant by “cluster classifications”. D rating for (iii) appears incorrect, as it appears inconsistent with the A rating for (iv), under which investments are consistently selected on the basis of relevant sector strategies. Or else, the A rating for (iv) appears wrong if the D rating for (iii) is correct. **Government of South Africa:** COSTING AND BUDGETING OF POLICY PRIORITIES: In relation to this,	No changes made to the scoring. Sector strategies exist for all sectors; however they are not costed and are not developed within a forecasted fiscal frame. That results in a D. That said, the projects included in the MTEF are derived from the sector strategies and consider recurrent cost implications that are included in forward budget estimates for the sector. That results in an A. There is nothing inconsistent about these two scores.

	Comments on the rating	Response
	PEFA assesses in terms of a near zero-based strategy costing, linked to sector budget projections. In this regard it should be noted that in SA, sector allocations for the new MTEF are not provided, it is not our budgeting practice. There is one available funding envelope and besides the vertical division thereof, there is no further division. All departmental bids may therefore compete equally with each other. [Cluster bids may be submitted, but each department's commitments in terms of finance and performance should be clearly indicated. All requirements are the same as for submissions of individual departments, which are the overwhelming majority of submissions.] It should also be noted that the statement of "Apex priorities" is not a standing practice in SA, it was merely a statement for this financial year, which is the closing year of the current government..	It has been noted that the statement of "Apex priorities" is not a standing practice in SA, it was merely a statement for this financial year, which is the closing year of the current government and the narrative adjusted accordingly.
	Also it is noted in the report that the link between planning and budgeting (costed strategies) is weak. South Africa is currently engaged in a major budget reform around performance. A framework for managing performance has been developed and at the moment work is being done to improve the Strategic Planning Framework, amongst others. This comes out of the awareness that often strategy and budgets are not effectively linked but we are developing national guidelines to improve processes to ensure that when plans are developed, there is an explicit requirement to link this to the budget. It should be noted though that in SA there is a belief that while planning should be linked to the budget, some plans may need to be made even if there is no budget link at the present time. There should be no maximum time limit to departmental plans. [While one does not want blue skies planning, one does not want to confine planning only to what is affordable currently.] To some extent, proper implementation of SA's performance management guidelines will provide a greater link between planning and budgeting.	This has been noted and has been incorporated into Chapter 4 on Government Reform Processes.
	<u>Changes made to the narrative and / or scoring:</u> The scoring remains unchanged. The narrative has been amended to include the initiatives on better linking planning and budgeting.	

	Comments on the rating	Response
PI-13	**PEFA Secretariat:** The A, A, A and overall A ratings appear correct, based on the evidence.	No changes have been made to the scoring or the narrative.
	Changes made to the narrative and / or scoring: The scoring remains unchanged. Changes have been made to the narrative.	
PI-14	**PEFA Secretariat:** The A. A, A and overall A ratings appear correct, based on the evidence.	No changes have been made to the scoring or the narrative.
	Changes made to the narrative and / or scoring: The scoring remains unchanged. The narrative has been clarified further.	
PI-15	**PEFA Secretariat:** The D, A, A and overall D+ scores appear correct, based on the evidence (the D+ score is missing from the text box).	No changes have been made to the scoring.
	Government of South Africa: TAX ARREARS: Relating to the tax arrears, the report scores South Africa poorly due to the fact that our tax arrears are not a true reflection of what is likely to be recovered and paid back. This is not necessarily an indication of bad tax recovery practices but more specifically owing to SARS' policy in respect of writing off tax arrears, which has resulted in a large proportion of arrears relating to history periods. SARS is not entirely content with the narrative describing this situation.	Changes in the narrative have been made to further clarify the unique circumstance that contribute to high recording of tax arrears and that contribute to a particularly low measure of collection ratio for gross arrears.
	Changes made to the narrative and / or scoring: The scoring remains unchanged. The narrative has been amended.	
PI-16	**PEFA Secretariat:** The A, A, A and overall A ratings appear correct, based on the evidence.	No changes have been made to the scoring or the narrative.
	Changes made to the narrative and / or scoring: The scoring and text remain unchanged.	
PI-17	**PEFA Secretariat:** The A, B, A and overall A ratings appear correct, based on the evidence. The last two sentences in the text box for dim (iii) appear to have been inadvertently	The repetition in the text box has been deleted.

	Comments on the rating	Response
	copied from the text box for dim (ii).	
	Changes made to the narrative and / or scoring: The scoring remains unchanged. The repetition in the text box has been deleted.	
PI-18	**PEFA Secretariat:** The A, A, A, A and overall A ratings appear correct, based on the evidence.	No changes have been made to the scoring or the narrative.
	Changes made to the narrative and / or scoring: The scoring and the text remain unchanged.	
PI-19	**PEFA Secretariat:** The D and B ratings for dims (i) and (iii) appear correct, based on the evidence. The D rating for dim (ii) appears incorrect, based on the evidence. If regulations permit use of less competitive methods in certain circumstances (e.g. March Spike), then a B or C score may be justified. A C score may be appropriate if MDA justification is weak as evidenced by deliberate leaving of procurement until the last minute (as indicated under PI 20). But leaving procurement to the last minute seems inconsistent with the detailed cash flow forecast that must be provided at the beginning of the new fiscal year, as it seems unlikely that the National Treasury would accept a detailed cash flow forecast that shows procurement mainly happening at the end of the fiscal year. Although the procurement act does not explicitly state open competition as the default method of procurement, the monetary threshold effectively establishes open competition as the default procurement method for planned procurement above the threshold. **South African Government:** PROCUREMENT DATA: The relevant act does not compel government agencies and institutions to make use of open procurement procedures; therefore the PEFA score is automatically determined. Lack of existence of	The Blue Book clearly and unambiguously states that a D be assigned when "Regulatory requirements do not clearly establish open competition as the preferred method of procurement". Evidence is provided from the regulations referred to in the narrative that such preference is obscured by subjecting it to a standard of pragmatism (see 3.4.7 paragraph 2 of the PEFA report). If cash flows are not based upon procurement plans, and there is not an emphasis placed upon expenditure commitment reporting then pro forma cash flow adjustments may not suffice the management of addressing end of year expenditure rushes where it is understood that funds remained unspent will be lost. Whether, unlikely or not, there is substantial evidence that points to this occurrence. Note that the SEIFSA, also corroborates this practice of end of year expenditure. The March Spike is not solely a consequence of the practice of rushed expenditure and the by pass of open competition observed at the end of the year. However, though small in aggregate terms, this procurement practice does contribute to it.

	Comments on the rating	Response
	consolidated procurement data, makes the practice in this regard hard to determine in aggregate, and therefore no conclusion can be reached regarding the extent of competitive procurement practices. (Conclusions can only be made in terms of evidence provided in respect of one national department, and therefore can in no way be considered to be representative of government practice.) Procurement practices should not necessarily be linked to fiscal dumping.	
	Changes made to the narrative and / or scoring: The scoring and narrative were changed to reflect the analysis of additional evidence.	
PI-20	**PEFA Secretariat:** The A rating for dim (i) is not sufficiently evidenced. The statement that “commitment control is effective and limits expenditure to available cash” should be expanded to indicate if the described commitment control processes actually function as they should. The evidence presented under PI-4 indicates that perhaps this is not the case. The A and C ratings for dims (ii) and (iii) appear correct, based on the evidence.	The A is considered appropriate because comprehensive commitment controls are in place and limit spending in accordance with approved budgets. There are no exceptions with respect to types of expenditure so there is no basis for a B rating. How then does that tally with the incidence of arrears? In a rush to spend at the end of the year a number of commitments (for which supplies and services are provided) remain unpaid. These appear as outstanding payments in the new year and when they remain so more than 30 days they are recorded as arrears.
	Changes made to the narrative and / or scoring: The scoring and text remain unchanged.	
PI-21	**PEFA Secretariat:** The A, A, A and overall A ratings appear correct, based on the evidence.	No changes have been made to the scoring or the narrative.
	Changes made to the narrative and / or scoring: No change in scoring. The narrative was amended to introduce additional evidence.	
PI-22	**PEFA Secretariat:** The B and A ratings appear correct, based on the evidence. The overall score, however, is B+, not A.	Changes have been made to the overall scoring from A to B+.
	Changes made to the narrative and / or scoring: The overall scoring has been changed from A to B+. The narrative remains unchanged.	
PI-23	**PEFA Secretariat:** The D rating appears insufficiently evidenced. How to score this indicator	Additional evidence has been provided and the scoring has been changed from a D to an A.

	Comments on the rating	Response
	depends on the extent to which the funding for these public services mainly comes from conditional grants from national government or from own revenues plus unconditional grants from the national government. PI-23 applies here if much of the funding is through conditional grants. *Queries* - Local governments also deliver services; does the information received by provincial governments on resources received by service delivery units (SDUs) include information on resources received by SDUs at local government level? - If provincial governments have the information on resources received by SDUs, why have they not been giving this to the national government? - The narrative could mention plans (outlined in Section 4) to strengthen the flow of information on resources received by SDUs.	The narrative has been modified to take into account the additional evidence provided.
	Government of South Africa The report (for example on PI-23) mentions that no information is available on primary schools and health care facilities, however, due to the fact that the report only focuses on the national level, such information will not be available as it is provided for in provincial and municipal budget publications and financial statements.	The requisite information is available in the Provincial Budgets and Expenditure Review 2003/04 – 2009/10.
	Changes made to the narrative and / or scoring: Changes made to the scoring from D to A. Corresponding changes have been made to the narrative.	
PI-24	**PEFA Secretariat:** The C, A, A and overall C+ ratings appear correct, based on the evidence. It would be interesting to know why commitments do not appear in the monthly reports, when BAS presumably has the capacity to include commitments, as purchase orders are processed through BAS.	The standard reporting format referred to in the PFMA (Section 32) does not include commitment reporting and so for those Departments which seek to meet the minimum requirements such reporting is absent. But as noted there are some Departments such as Education that for internal reporting and monitoring purposes do include commitment reporting.

	Comments on the rating	Response
	Changes made to the narrative and / or scoring: No changes made to scoring or narrative.	
PI-25	**PEFA Secretariat:** The A rating for dimension (i) appears incorrect, based on the evidence as complete consolidation is not achieved. The A and A ratings for (ii) and (iii) appear correct, based on the evidence.	If one assumes a strictly technical interpretation of consolidated as per accounting use, as opposed to a general interpretation to mean an aggregation of results then South Africa has not achieved complete consolidation. Indeed that is why it reports its aggregated financials as Consolidated Financial Information. However, there is substantial consolidation that has been achieved and to ignore that would, according to PEFA, lead to a score of D. This would seem to be a far more egregious mischaracterisation or rating of the quality of South African financial statements, than the slight overstatement of referring to the aggregated financial statements with partial elements of consolidation, as consolidated. This especially so where the narrative has been careful to explain the precise status of consolidation in South Africa. For this reason we maintain the A rating.
	Changes made to the narrative and / or scoring: No changes made to scoring or narrative.	
PI-26	**PEFA Secretariat:** The A, B, B and overall B+ ratings appear correct, based on the evidence.	No changes have been made to the scoring or the narrative.
	Changes made to the narrative and / or scoring: No changes have been made to the scoring or the narrative.	
PI-27	**PEFA Secretariat:** The A, A, A, A and overall A ratings appear correct, based on the evidence.	No changes have been made to the scoring or the narrative.
	Changes made to the narrative and / or scoring: No changes have been made to the scoring or the narrative.	
PI-28	**PEFA Secretariat:** The A, A, B and overall B+ ratings appear correct, based on the evidence.	No changes have been made to the scoring or the narrative.
	Changes made to the narrative and / or scoring: The scoring has been completed and the narrative has been amended.	
D-1	**PEFA Secretariat:** The D, D and overall D ratings appear correct, based on the evidence.	

	Comments on the rating	Response
	<u>European Commission:</u>	
	1. <u>Page 100, Section 3.7.1.</u> A large portion of the information presented is not correct and should be verified.	It should be made clear that the data shown was taken from IDC within the National Treasury and verified by data received form donors.
	2. *<u>1st paragraph</u>*. In the water sector the Irish are also giving SBS.	The data has been updated to include the Irish sector budget support.
	3. *<u>3rd paragraph</u>*. Presentation of the basic principles of SBS is not correct. Disbursement is based on the *conditions* in the financing agreement. These are agreed between the donor and the government and can relate to many things - macro-economic, PFM, planning, reporting, performance etc. Disbursement forecasts are available for the life of the donor SBS programme since they are included in the financing agreement.	While the PEFA methodology expects that the narrative shall include the explanation of possible reasons for the observed deviation between forecasts and actual disbursements, the inclusion of such conditionalities in the financing agreement do not serve as a mechanism for predicting disbursement. Of course governance considerations place such reasons within a high priority criterion, however irrespective of the reason for delayed or partial disbursement the impact on PFM of such predictability of disbursements is negative.
	4. *<u>4th paragraph</u>*. Again what is presented here may be true but an explanation needs to be given. The reason is because the government do not submit the documents to show the disbursement conditions have been met on time. Of course donors are slow to pay but the process starts late because of government.	There was no clear evidence reviewed to ascertain the reasons for delayed payments but the point is well taken and will serve to inform the dialogue efforts anticipated between donors and the government to improve upon cooperation modalities.
	5. *<u>Table 3.12</u>*. The water figures are wrong. Assuming this relates to the central government financial year the figures should be: Masibambane II - 2005/06. Forecast Q3. 19M. Paid Q3 18.34M 2006/07. Forecast Q3. 15M. Paid Q3. 14.43M (Paid 2007/08 Q3 1.188551M - this was a catch-up tranche because they did not meet the payment conditions before) Masibambane III - 2007/08. Forecast Q4. 31M. Paid 2008/09 Q1 31M - this was because they only send us the signed FA in May 2008 and we then paid in the same quarter.	The figures in table 3.12 have been verified with the EC and IDC and discrepancies corrected. Please note that there are discrepancies in the disbursement figures because they were derived from IDC figures (kept in Rand) using the Info Euro exchange rates. This rather than the actual disbursements in Euro.
	<u>Page 101. Paragraph after Table 3.13</u>. The figures presented here would be	Even after correction the ratings remain unchanged.

	Comments on the rating	Response
	different if the true water figures had been used.	
	Changes made to the narrative and / or scoring: The scoring remains the same. Corrections have been made to the tables. And some changes made to the narrative.	
D-2	**PEFA Secretariat:** The D, D and overall D ratings appear correct, based on the evidence.	No changes have been made to the scoring or the narrative.
	Changes made to the narrative and / or scoring: The scoring is unchanged.	
D-3	**PEFA Secretariat:** The D rating appears correct, based on the evidence.	No changes have been made to the scoring or the narrative.
	Changes made to the narrative and / or scoring: The scoring remains unchanged.	

Section 4 – Reform Efforts

PEFA Secretariat

Comment 6.1

This section is generally well-done, as far as it goes, but it appears that some of section 4.2 is missing.

Response 6.1

There is a confusing sentence that refers to the next section that was left after reorganisation of the text. This has been removed to take away the suggestion that there is a missing section.

PFM Performance Indicator		Draft Report	Final Report
A. PFM-OUT-TURNS: Credibility of the budget			
PI-1	Aggregate expenditure out-turn compared to original approved budget	A	A
PI-2	Composition of expenditure out-turn compared to original approved budget	A	A
PI-3	Aggregate revenue out-turn compared to original approved budget	A	A
PI-4	Stock and monitoring of expenditure payment arrears	A	A
B. KEY CROSS-CUTTING ISSUES: Comprehensiveness and Transparency			
PI-5	Classification of the budget	A	A
PI-6	Comprehensiveness of information included in budget documentation	A	A
PI-7	Extent of unreported government operations	A	A
PI-8	Transparency of inter-governmental fiscal relations	B	A
PI-9	Oversight of aggregate fiscal risk from other public sector entities	B+	B+
PI-10	Public access to key fiscal information	A	A
C. BUDGET CYCLE			
C(i) Policy-Based Budgeting			
PI-11	Orderliness and participation in the annual budget process	B	B
PI-12	Multi-year perspective in fiscal planning, expenditure policy and budgeting	B	B
C(ii) Predictability and Control in Budget Execution			
PI-13	Transparency of taxpayer obligations and liabilities	A	A
PI-14	Effectiveness of measures for taxpayer registration and tax assessment	A	A
PI-15	Effectiveness in collection of tax payments	D+	D+
PI-16	Predictability in the availability of funds for commitment of expenditures	A	A
PI-17	Recording and management of cash balances, debt and guarantees	A	A
PI-18	Effectiveness of payroll controls	A	A
PI-19	Competition, value for money and controls in procurement	D+	D+
PI-20	Effectiveness of internal controls for non-salary expenditure	C+	C+
PI-21	Effectiveness of internal audit	A	A
C(iii) Accounting, Recording and Reporting			
PI-22	Timeliness and regularity of accounts reconciliation	A	B+
PI-23	Availability of information on resources received by service delivery units	D	A
PI-24	Quality and timeliness of in-year budget reports	C+	C+
PI-25	Quality and timeliness of annual financial statements	A	A
C(iv) External Scrutiny and Audit			
PI-26	Scope, nature and follow-up of external audit	B+	B+
PI-27	Legislative scrutiny of the annual budget law	A	A
PI-28	Legislative scrutiny of external audit reports	B+	B+
D. DONOR PRACTICES			
D-1	Predictability of Direct Budget Support	D	D
D-2	Financial info provided by donors for budgeting/reporting on project/program aid	D	D
D-3	Proportion of aid that is managed by use of national procedures	D	D