



University of Fort Hare
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**EVALUATING REVENUE COLLECTION AND ALLOCATION CHALLENGES
FACED BY NDLAMBE LOCAL MUNICIPALITY (Eastern Cape Province)**

BY

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DECLARATION

I, **N.N. Pieters**, do hereby declare that, this treatise entitled, “**EVALUATING REVENUE COLLECTION AND ALLOCATION CHALLENGES FACED BY NDLAMBE LOCAL MUNICIPALITY**”, submitted to the University of Fort Hare, in partial-fulfilment of the requirements for the degree of Masters in Public Administration, has never been submitted by me or any other person for a degree at this or any other university. This is my original work in design and execution and all material therein has been duly acknowledged by way of appropriate references and citations.

Signature

Date

.....

.....

ACKNOWLEDGEMENTS

Firstly, I would like to acknowledge my Lord and Saviour Jesus Christ for his mercies that are new every morning. This Mini-Dissertation would not have been possible without his unmerited favour upon me. I would also like to acknowledge my supervisor Dr R.T.Mle for being supportive whenever I needed help. Truly, it was indeed an honour working with him. I greatly appreciate.

DEDICATION

This is dedicated to my late sister **Nokwanda Xolisa Pieters** and may her soul rest in peace.

ABSTRACT

In this project, the researcher evaluates revenue collection and allocation challenges faced by South African Municipalities in the case of NDLAMBE Local Municipality and this research project consist of five Chapters. Chapter one introduces and outlines the setting of the study and also provides the problem statement, research questions, research objectives and significance of the study. The chapter further clarifies the key concepts and terms that were used in the study, delimitation and limitations of the study. Chapter two provides a critical discussion of the concept of revenue collection and allocation, focusing on the various perspective of revenue. A source of municipal revenue and revenue collection and allocation model is explained as well as theoretical framework that guides it. Chapter three gives an account of the research design and methodology used in the study and in this study the researcher used the qualitative research approach as a data collection technique and document surveys were used because it is cheap and it saves time. The chapter also highlights the revenue collection and allocation applicable to the study and conclude by discussing the data analysis techniques that were used in the empirical study. Chapter four dealt with the data analysis of data collected presentation and discussion of the results and the researcher analyzed data using the filtering technique and content analysis. Chapter five drew conclusions and made scientific recommendations based on the research findings. The municipality is largely dependent on grants from upper spheres of government and generate less than 20 percent of current expenditures from own resources. As a whole, the revenue collection and allocation challenge of the NDLAMBE Local Municipality, given the current scenario of flows, is a reason for concern. Due to historical and political factors, local governments in South Africa differ substantially in terms of potential revenue base, but it may be that in many cases potential revenue is not exploited and that the high level of dependency on grants, high level of bad debts and lack of political will to be more self-reliant is the result of poor revenue in NDLAMBE Local Municipality.

KEYWORDS; NDLAMBE Local Municipality, Revenue collection and Allocation Challenges, South Africa.

ACCRONYMS

AG GENERAL	AUDITOR
DORA ACT	DIVISION OF REVENUE
GRAP PRACTICE	GENERALLY RECOGNIZED ACCOUNTING
LGMPPRA ACT	LOCAL GOVERNMENT MUNICIPAL PROPERTY RATES
MFMA ACT	MUNICIPAL FINANCE MANAGEMENT
MFPFA ACT	MUNICIPAL FISCAL POWERS AND FUNCTIONS
MTBPS STATEMENT	MEDIUM TERM BUDGET AND POLICY
PFMA ACT	PUBLIC FINANCE MANAGEMENT
SARS ACT	SOUTH AFRICAN REVENUE SERVICES
VATR RECEIVABLES	VALUE ADDED TAX

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CHAPTER ONE: INTRODUCTION AND SETTING OF THE STUDY

1.1 INTRODUCTION AND BACKGROUND

The concept of revenue collection and allocation has attracted considerable attention over recent years and has become an important issue for modern local government, as in most of the countries there is poor service delivery due to inadequate revenue available for municipalities to perform quality services to the community. According to Venter and Van der Waldt, (2007:200) the Constitution of the Republic of South Africa of 1996 establishes three spheres of government namely national, provincial and local government. These spheres of government are distinctive, interdependent and interrelated but the national government is the dominant sphere. Local government is an important sphere of government in that it delivers, according to the Constitution, basic goods and services to members of the society on behalf of the other two government's spheres.

A sound revenue system for local governments is an essential condition for the success of effective service delivery because no public institution or entity can provide goods and services to communities without having money available to cover its operational costs. If an entity such as municipality does not have a sustainable income, it cannot make service commitments or even purchase goods and services. In practice, this means that municipalities have to generate money by raising taxes, levies, rates and service charges from the inhabitants within their municipal borders because local government needs funds in order to provide goods and services that it must deliver to the community.

Various authors define municipal revenue in different ways and municipal revenue is regarded by many as simply the cash that the municipality is paid for selling things or delivering services to the public, for example, user fees and tax. According to Alexander *et al*, (2007:13) revenue is the gross inflow of economic benefits during the period arising in the course of the ordinary activities of an entity when those inflows result in increase in inequity, other than increases relating to contributions from equity participants.

The purpose of this research project is to assess the municipal revenue collection and allocation challenges faced by Ndlambe Local Municipality officials. The emphasis on both local government own revenues and fiscal transfers from the central level are all covered.

1.1.1 Trends of revenue collection and allocation

According to Van Donk, (2008:297) trends in the structure and performance of municipal revenues are closely connected to underlying debates on redistribution, stabilisation and accountability. The inability of most municipalities to collect a significant proportion of revenues that are due to them has been a perennial concern of policy makers seeking to stabilise municipal finances. This problem has been ascribed to many underlying issues including the inability of poor consumers to pay for services, the rent and service boycotts of the 1980s which destroyed the credibility of municipal enforcement capacity, poor financial management practices including weak administration of billing and collection system and inappropriate accounting treatment of consumer debtors, which have dramatically magnified revenue problems.

The Auditor-General reports show that the growth in total debt slowed from 12% to 11% between 2003/04 and 2004/05 (Auditor General 2004/2005 cited in Van Donk, (2008:298). The average debt collection period also fell from 322days in 2003/04 to 136days in 2004/05. Although this provides some (limited) hopes, accumulated consumer debt remains large, at an estimated R28 billion (National treasury 2005) and will place considerable pressure on municipal balance sheets for the foreseeable future. The revenue crisis facing many municipalities has led to concerns that there is a structure imbalance between the revenues and expenditures of municipalities in South Africa and this challenge is still prevailing in Ndlambe Municipality. Clearly, municipalities are always likely to feel that they are not receiving enough from national transfers or they should be given additional resources. This brought the attention of government officials to revenue collected and allocated since they are now being unable to perform their duties effectively with inadequate revenue.

1.2 PROBLEM STATEMENT

The Ndlambe Municipality currently faces profound financial and service delivery challenges and this financial position of the municipality underlines the urgency of developing a coherent, realistic and integrated approach in managing its activities and more specifically actions to improve revenue collection and allocation. According to the Ndlambe Municipality Annual Report (20007/2008: Chapter 4), Ndlambe Municipality is still grant dependant and in the year in question the collection of revenue was not as desired as only R31 284 282 was collected and that has resulted to the bad debts amounting to R52, 083, 928. Many local government tax administrations are often inefficient and not able to properly account for revenues collected, thus, as a result, many South African local governments are facing a governance crisis and poor service delivery capability.

Ndlambe Municipality's Mayor Honourable Tandani in his 2013 Budget speech, alluded to the fact that the municipality is facing a myriad of challenges that require intervention for all involved, these include, thin revenue base that leads to grants dependence which is impacting negatively on speedy service delivery, long outstanding debtors with huge balances remain a daunting challenge and insufficient grants allocated to the municipality to address backlogs in service delivery.

According to Broadway *et al*, (1994:53) local government may find it difficult to change user fees to recover costs effectively thus the low price of user fees charged will cause the municipality to have poor revenue that will be collected from citizens. It is not uncommon for the central government to exercise effective control over revenue sources nominally assigned to the local level. This is because municipalities do not have authority to adjust rates for public utilities without approval from higher levels of government and this is a challenge that causes poor revenue collection by municipalities and an investigation needs to be carried out on how revenue collection can be improved.

According to Devas, (2003:50) in many communities especially in rural areas, access to basic services, such as potable water, electricity and sanitation is quite inadequate and the capacity of local governments to raise revenue is extremely limited because of the

poverty there and the culture of non-payment. For example, most people who leave in Alexandria Town most are poor and they are unemployed people who rely on government old age grants. Furthermore, the refusal of people in Ndlambe to pay water and electrical charges and any rates may consequently result in the municipality having inadequate revenue to perform its responsibilities and revenue allocations from the national government are uncertain and will almost surely be limited in size to a small portion of local needs. The present study seeks to provide a panacea to these ills by emphasizing on revenue collection and allocation challenges faced by officials in Ndlambe Municipality.

1.3 RESEARCH QUESTIONS

The present study is guided by the following research questions:

- .What is the challenges confronted by the Ndlambe Municipality in ensuring effective revenue collection and allocation?
- .What is the causes of poor revenue collection and allocation by public officials in the Ndlambe municipality?
- .To what extent is the Ndlambe municipality making use of its revenue collected and allocated to improve service delivery to the community?

1.4 RESEARCH OBJECTIVES

- . To explore and examine the challenges faced by Ndlambe Municipality in ensuring effective revenue collection and allocation.
- .To examine the causes of poor revenue collection and allocation by officials in Ndlambe Municipality.
- .To comes up with strategies and recommendations that can help in improving on revenue collection and allocation by public officials and therefore enhance effective service delivery in Ndlambe Municipality.

1.5 SIGNIFICANCE OF THE STUDY

This study is important in its attempt to investigate the challenges of poor revenue collection and allocation in Ndlambe Municipality. It is hoped that the findings of the research will assist the National, Provincial and Local government as well as the public

in the development of policies and strategies to ensure the effective revenue collection and allocation by public officials in municipalities. Such a policy could be used as a strategic framework designed to serve as a guide in all municipalities, thereby leading to the improvement of service delivery.

The practical recommendations that will be made at the end of this study will assist leadership and supervisors in Ndlambe Municipality both politically and administratively to effectively deal with challenges they face in ensuring effective revenue collection and allocation. It is also envisaged that the study will provide insight to other researchers interested in revenue collection and allocation in the public sector for effective service delivery to explore further the findings emanating from this study.

The research will contribute to the knowledge production in the sense that it will expose the challenges faced by public officials of Ndlambe Municipality in revenue collection and allocation. This will determine if there is a need to introduce more ways of collecting revenue as well as new formulas in the allocation of revenue. The study will further reflect how public officials in South Africa are coping with the new existing revenue collection and allocation methods.

1.6 RESEARCH DESIGN AND DATA COLLECTION TECHNIQUES

According to Des Vos, Strydom, Fouche and Delport, (2005) a research design is a plan or a blueprint according to which data is collected to investigate the research hypothesis in the most economical manner. Thus, it can be deduced that a research design is a plan of how one intends to conduct the research. In this study the researcher used the qualitative research approach. According to Van Maanen (cited in Welman, Krugar and Mitchell, 2005) qualitative research is an umbrella phrase covering an array of interpretive techniques which seeks to describe, decode, translate and otherwise come to terms with the meaning of naturally occurring phenomena in the social world. According to David and Sutton, (2004), data is what the researcher actually receives from the respondents, be it social or physical. Layder, (1993:54) identifies a number of instruments that can be used to gather data; among these are interviews, intakes forms, questionnaires and surveys, attendance records and documents.

This study used document surveys as a data collection technique and analyzed the information contained thereto. The researcher opted for document surveys because it saves time and it is cheap because data is already available

1.7 CLARIFICATION OF KEY CONCEPTS AND TERMS

1.7.1 PUBLIC ADMINISTRATION

Public administration is defined as a broad spectrum combination of practice and theory which aims to promote public policy making which is sensitive to the needs and aspiration of society, cultivate a greater understanding of the relationship between government and the governed society, and establish managerial practices directed at efficiency, effectiveness and a sensitivity to people's innermost needs. (Du Toit and Van Der Waldt, 1997:61).

1.7.2 MUNICIPALITY

According to Van der Waldt, (2007:166) municipalities such as Ndlambe Local Municipality are a third sphere of government established in terms of the Section 151 of the Constitution of the Republic of South Africa, 1996, (Chapter 2) Section 12 of the Municipal Structures Act 1998, (Act 117 of 1998) and the Eastern Cape Province Government Gazette Extraordinary General Notice 687, 2000. In terms of section 153(a) of the Constitution of the Republic of South Africa, 1996 a municipality must structure and manage its administration and budgeting and planning processes to give priority to the basic needs of the community.

1.7.3 PUBLIC FINANCE

Public finance is that branch of economics that studies how public authorities raise revenue and incur expenditure so that the society may get maximum social benefit (Khan and Hildreth, 2004: 3).

1.7.4 FRAUD

Hansen, *et al* (2005) define fraud as the use of one's occupation for personal enrichment through deliberate misuse or misapplication of the employing organizations resources or assets.

According to Andrew, (2011) fraud is a purposeful deception, misrepresentation, or concealment of facts intended to cause injury or loss to another party, typically for the sake of one's own direct or indirect gain.

1.7.5 SERVICE DELIVERY

This is provision of public activities, benefits or satisfactions. Services relate both to the provision of tangible public goods and to intangible services (Fox and Meyer, 1995).

1.7.6 TRANSPARENCY

This principle is an extension of the accountability principle. Transparency is enhanced when the recipient government and tax payers have access to information about the grant formula and the allocation of funds.

1.7.7 REVENUE ADEQUACY

This simply means that municipal governments should have adequate revenues to discharge their expenditure.

1.7.8 MUNICIPAL FINANCE

Municipal finance is about the revenue and expenditure decisions of municipal governments. It covers the sources of revenue that are used by municipal government's taxes, user fees and intergovernmental transfers (Slack 2009:1).

1.7.9 UNAUTHORISED EXPENDITURE

Unauthorised expenditure is expenditure that has not been budgeted for expenditure that is not in terms of the conditions of an allocation received from another sphere of government, municipality or organ of state and expenditure in the form of a grant that is not permitted in terms of the Municipal Finance Management Act (Act No.56 of 2003). Unauthorised expenditure is accounted for as an expense in the Statement of Financial Performance and where recovered, it is subsequently accounted for as revenue in the Statement of Financial Performance.

1.7.10 IRREGULAR EXPENDITURE

Irregular expenditure is expenditure that is contrary to the Municipal Finance Management Act (Act No.56 of 2003), the Municipal Systems Act (Act No.32 of 2000), and the Public Office Bearers Act (Act No. 20 of 1998) or is in contravention of the Municipality's supply chain management policy. Irregular expenditure excludes unauthorised expenditure. Irregular expenditure is accounted for as expenditure in the Statement of Financial Performance and where recovered, it is subsequently accounted for as revenue in the Statement of Financial Performance.

1.8 DELIMITATION OF THE STUDY

1.8.1 Type of the Organization

Ndlambe Local Municipality is classified as a local government.

1.8.2 Concept of Evaluation

The central concept of evaluation in this study will be revenue collection and allocation challenges in NDLAMBE Municipality with a primary focus on the causes and consequences of poor revenue collection and allocation on service delivery by the municipality.

1.9 ENVISAGED CHAPTER OUTLINE

CHAPTER One: This chapter introduces and outlines the setting of the study and also provides the problem statement, research questions, research objectives and significance of the study. The chapter further clarifies the key concepts and terms that will be used in the study and its delimitation. .

CHAPTER Two: This chapter provides a critical discussion of the concept of revenue collection and allocation, focusing on the various perspective of revenue.

CHAPTER Three: This chapter gives an account of the research design and methodology used in the study. The chapter also highlights the revenue collection and allocation applicable to the study and conclude by discussing the data analysis techniques that were used in the empirical study.

CHAPTER Four: This chapter deals with the data analysis of data collected, presentation and discussion of the results.

CHAPTER Five: This chapter draws conclusions and make scientific recommendations based on the research findings.

1.10 CONCLUSION

This chapter has briefly outlined the introduction, background of the study, statement of the problem, research questions and the research objectives. It has also presented the significance for undertaking the study and clarified the key concepts and terms used. Finally, the chapter highlighted the delimitation of the study and concluded by outlining the preliminary framework for the research. Chapter two deals with literature review.

CHAPTER 2: REVIEW OF RELEVANT LITERATURE

2.1 INTRODUCTION

According to Fink, (1998:3) as cited in McNabb, (2013:411) literature review is a systematic, explicit, and reproducible method for identifying, evaluating, and interpreting the existing body of recorded work produced by researchers, scholars and practitioners. It serves the purpose of familiarizing the researcher with the latest developments in the area of study and thereby attempts to close the existing gaps. Therefore, the purpose of this chapter is to review the existing literature on revenue collection and allocation in the public sector. To achieve this, various sources were explored including books, journals, official reports and Acts.

2.2 REVENUE COLLECTION AND ALLOCATION MODEL

A revenue collection and allocation model defines how the revenues resulting from service delivered by the municipality are being collected and revenue from national and provincial government is being allocated to the municipality. There are various models which show revenue collection and allocation such as municipal revenue business models which focuses on maximizing revenue collection, reducing inefficiency and costs and reducing uncollectible debt. However, in this study the researcher is going to explain the benefit model of local government finance.

FIG 2.1: THE BENEFIT MODEL OF LOCAL GOVERNMENT FINANCE

PRIVATE	PUBLIC	REDISTRIBUTIVE	SPILL OVERS
Water	Police	Social assist	Roads/transit
Sewers	Fire	Social Housing	Culture
Garbage	Local Parks		Social assistance
Transit	Street Light		
USER FEES	PROPERTY TAX	INCOME TAX	TRANSFER

Source: Adapted in Slack, (2009: 18)

The benefit model of local government finance as above shows different financing tools for different services. According to Bird, (1994) given this role of local government to provide goods and services, is the appropriate starting point for municipal finance. As

shown on the benefit model of local government finance above, local government services, wherever possible, should be paid for on the basis of the benefits received from these services (Bird, 2001a). The extent to which municipalities will be able to apply the benefit-received principle, however, depends on the nature and characteristics of the services they provide. The benefit model is further elaborated below.

2.2.1 Services with private goods characteristics

For services with private good characteristics such as water, sewers, garbage collection and disposal, transit and recreation, user fees are appropriate to fund at least some portion of the costs. In general, user fees are appropriate where there is a clear relationship between the fees charged and the benefits received, the tax payer has the choice about the extent to which he or she uses the service, it is possible to collect the charge at a reasonable cost, and equity concerns can be addressed, for example, by lowering or waiving fees for low income users. User fees can play an important role in municipal finance by ensuring that governments do what people want.

2.2.2 Services with public goods

Service with public goods characteristics such as police and fire protection, neighbourhood parks, local streets and street lighting have collective benefits that are enjoyed by local residents but which cannot easily be assigned to individual beneficiaries. These services are more difficult to charge for and require some form of local benefit based on taxation such as the property tax. The property tax allows individuals to express their demand for services where benefits are consumed collectively. In this respect, the property tax can be considered to be generalized or nonspecific user charge (Kneebone and McKenzie, 2003).

2.2.3 Services that redistribute income

Services that redistribute income should be paid for by senior levels of government because they have a wider range of taxes than local governments and they generally have taxes that are more closely related to ability to pay, such as income taxes. Although the primary role of local governments is to provide goods and services and not to redistribute income, however, many local governments do deliver services that are redistributive in nature such as welfare assistance, health and social housing, user fees

and benefit-based taxes such as the property tax are not appropriate to fund these services. User fees defeat the purpose of redistribution and property taxes are more regressive than income taxes and thus are not appropriate for financing redistributive services. For these reasons, services that have a redistributive component should be funded from local income taxes or from central and provincial revenues which include income tax.

2.2.4 Services with spill overs.

There are other services where the benefits or costs spill over municipal boundaries but where local provision is still desirable. Positive spill overs (externalities) occur if residents of neighbouring jurisdictions receive a service for free or at less than the cost of providing the service. For example, a major road constructed in one jurisdiction may be used by residents of another jurisdiction without any charge to them. The result will be an under-allocation of resources to that service because the municipality providing the service would base its expenditure decisions only on the benefits captured within its jurisdiction. It would not take account of the benefits to those outside the jurisdiction. One way to provide an incentive to the municipality to allocate more resources to the services generating the externality is a transfer from the provincial government.

2.3 LEGISLATIVE FRAMEWORK FOR REVENUE

According to Venter and Van der Waldt, (2007:200) legislative framework for revenue collection and allocation includes a large number of laws and public policies that have a direct bearing on who can collect revenue and how, where and when revenue can be collected and allocated to the different spheres and structures of government in order to deliver efficient and effective service. Some of these legislative frameworks are discussed below.

2.3.1 The Constitution of the Republic of South Africa, 1996.

Financial Management is a constitutional requirement for all three spheres of government and by implication, also for the entities created and established by these spheres. The two key sections in the Constitution are sections 215 and 216 in terms of the financial law. Financial management also takes place but in a less structured way. The influx of the new and often inexperienced financial officials requires for greater

structuring of financial management. The Constitution makes provision for the collection and allocation of revenue in the principles of Public financial management and administration which is section 195(1), National Revenue Fund section 213, Equitable Shares and Allocation of Revenue which is on section 24.

2.3.2 Intergovernmental Fiscal Relations Act 97 of 1997

This Act was promulgated to promote cooperation between the national, provincial and local spheres of government on fiscal, budgetary and financial matters and to prescribe a process for determining the equitable sharing and allocation of revenue raised nationally. This Act strengthens the provision of the Financial and Fiscal Relations Act.

2.3.3 Municipal Finance Management Act 56 of 2003

According to Khagram *et al*, (2013:54) in 1999 parliament enacted the Public Finance Management Act which contains a detailed set of procedures compelling government's officials to provide financial information and to account for their actions. The law applies to the nine provinces as well as to the national government. Recognizing that transparency has been far more evident at the national than the sub national level and seeking to ensure that local government complies with the same norms, Parliament enacted the Municipal Finance Management Act in 2003.

According to Tomlinson, (2006:114) the Municipal Finance Management Act 56 of 2003 created a framework for municipalities to borrow money and determine the conditions for short-term and long-term borrowing and Municipal Property Rates Act 6 of 2004 established a uniform property rating system across South Africa. The act applies to all municipalities, all municipal entities and national and provincial organs of the state to the extent of their financial dealings with municipalities. In the event of any inconsistency between a provision of the Act and any other legislation in force when the Act takes effect and which regulate any aspect of the fiscal and financial affairs of municipalities or municipal entities the provisions of the Act prevail.

Craythorne, (2006:249) states that the Municipal Finance Management Act has various objectives which include the ability to secure sound and sustainable management of the fiscal and financial affairs of municipalities and municipal entities by establishing norms

and stands and other requirements for ensuring transparency, accountability and appropriate lines in the fiscal and financial affairs of municipalities and municipal entities. The management of municipal revenues, expenditures, assets and liabilities and the handling of financial dealings and problems in municipalities is another objective of the Municipal Finance Management Act.

According to Pillay *et al*, (2006:306) this act is intended to secure transparency, accountability and sound management of the revenue, expenditure, assets and liabilities of local government institutions. According to Section 64 of the Municipal Finance Management Act, the municipal manager, being the accounting officer of a municipality, is responsible for the management of the municipality's revenue. It is therefore his/her responsibility to ensure that all reasonable steps are taken to collect all revenue due to the municipality (Section 78 of the Municipal Finance Management Act).

2.3.4 Division of Revenue Act 5 of 2012 (DORA).

Division of Revenue Act (Act 5 of 2012) provides a formula for the division of such funds into equitable shares and give effect to section 283 (1) of the Constitution which requires the Act to provide for the equitable distribution of Revenue raised nationally.

Section 214(1) of the Constitution requires that every year a Division of Revenue Act determine the equitable division of nationally raised revenue between national government, the nine provinces and 278 municipalities. According to Moeti *et al*, (2007:73) In terms of s10 of the intergovernmental Fiscal Relations Act 97 of 1997, the Minister of Finance must introduce a Division of Revenue Bill each year, for the next financial year, in the National Assembly when the annual Main Budget is introduced and is to be voted upon. Such Division of Revenue Bill must specify the share of revenue raised nationally that each sphere of government will receive, each provinces equitable share of the provincial share of that revenue, any other allocations to provinces or local government from the national governments share of that revenue as well as any conditions on which those allocations are and must be made.

2.3.5 Medium Term Budget Policy Statement

According to Moeti *et al*, (2007:73) Medium Term Budget Policy Statement (MTBPS) is issued by the National Treasury in October of each year. It outlines the government's fiscal framework, as well as expenditure plans and policies by excluding the proposed division of revenue between the national, provincial and local government over a 3year period. All three spheres of government benefit greatly from this statement of the proposed division of revenue in advance of the new financial year and estimated for a period of two years thereafter. The result of this is increased certainty with regard to medium to long-term planning. Further, the MTBPS not only sets out the equitable division of nationally raised revenue between the three spheres of government, but also explain the rationale behind such division of revenue.

2.3.6 South African Revenue Services Act 34 of 1997

According to Moeti *et al*, (2007:50) this Act was promulgated for the purpose of providing for the efficient and effective administration of the Revenue-collecting system of the Republic of South Africa and for this purpose, to organize the South African Revenue Services and to establish an advisory board.

2.3.7 Municipal Fiscal Powers and Functions Act 12 of 2007

Municipal Fiscal Powers and Functions Act (2007) regulates municipal fiscal powers and functions as provided for in section 229 of the Constitution. The Municipal Fiscal Powers and Functions Act, which came into effect on 7 September 2007, deals with the regulation of all municipal taxes other than property rates. The act aims to promote predictability, certainty and transparency of municipal fiscal powers and functions, and to ensure that these powers and functions are exercised in line with the provisions of section 229 of the Constitution. The act deals with three broad issues: applications for new taxes by municipalities (section 5), national norms and standards for municipal surcharges (section 8) and verification of municipal taxes that existed prior to the act (section 12).

2.3.7.1 Application for a new municipal tax

Section 5 of the Municipal Fiscal Powers and Functions Act provides for a municipality, a group of municipalities or organized local government to apply for a new municipal tax. A municipality cannot impose any new municipal tax if that tax has not been authorized by the Minister of Finance in terms of section 5. Any application for a new tax must include reasons for the proposed tax and the manner in which the revenue from the tax will be used. To date, two applications that comply with the requirements of section 5 of the Municipal Fiscal Powers and Functions Act have been received by National Treasury. The first application is for the introduction of a rural development levy in areas where municipalities struggle to implement the valuation rolls necessary to impose municipal rates. The other application proposes the introduction of a local business tax for businesses operating within the jurisdiction of metropolitan municipalities.

2.3.7.2 Regulation of surcharges

The Municipal Fiscal Powers and Functions Act 12 of 2007 (Section 8) deals with the norms and standards for imposing surcharges on municipal services and becomes effective from the date that the Minister of Finance gazettes these regulations. This section has not been activated. Surcharges currently form part of a tariff (when section 8 regulations are introduced, these will be split). Due to the interrelationship between tariffs and surcharges, the regulations applying to both are aligned. It is important that the National Treasury's regulatory processes regarding surcharges be aligned to the regulatory processes of sector departments regarding municipal tariffs. Although most sectors have some form of regulation in place, municipal regulatory oversight roles have been limited and largely unsuccessful. Most sector departments (the Department of Energy and the Department of Water and Environmental Affairs) have instituted processes to improve their regulatory oversight responsibilities, either directly or through a regulator (for example, the National Energy Regulator of South Africa).

2.3.7.3 Authorisation of municipal taxes that existed prior to the act

According to section 12 of the Municipal Fiscal Powers and Functions Act, a municipality had to apply to the Minister of Finance by 7 September 2009 for the authorization of taxes that existed before the act was enacted. Municipalities provided National Treasury with the potential taxes that were levied prior the commencement of the act. Each application was assessed. Preliminary determinations on how each application should be dealt with were approved by the minister, and published in a government notice for public comment and submitted to Parliament. Written comments on the preliminary determinations by the Minister of Finance, as published in the Government Gazette, were received from various stakeholders. Based on this consultation process, the minister gazetted the final rulings in early 2012. These rulings are subject to review by the Minister of Finance after five years in terms of section 10(2) of the Act.

2.3.8 Municipal Systems Act 32 of 2000

This Act is important for municipal financial management as it confers on the municipalities the powers, to develop policy, plans, programs and strategies providing for and regulating the provisioning of municipal services, and for imposing and recovering rates, taxes, levies and fees. It is intended that these powers be given effect through Integrated Development Plans.

2.3.9 Local Government Municipal Property Rates Act 6 of 2004

The Municipal Property Rates Act (2004) also regulates municipal fiscal powers and functions as provided for in section 229 of the Constitution and the According to Pillay *et al* (2006:305) the national legislation that regulates the power of a municipality to impose rates on property, surcharges on fees for services provided by or on behalf of the municipality or other taxes, levies or duties is a clause in the of Local Government Municipal Property Rates Act of 2004 which states that local government cannot apply taxes at the local level that threaten its own tax-reducing, fiscally conservative strategy. The Minister of provincial and local government may, with the concurrence of the Minister of finance set an upper limit on the percentage by which rates on properties may be increased. Sub urban rate payer associations and the powerful South African

Property Owners Association fought hard for these clauses in the legislation. The Act will shift all municipalities onto a system where the full market value of the property including land and improvements is taxed.

2.3.10 Public Finance Management Act 1 of 1999

The Public Finance Management Act, 1999, is one of the most important pieces of legislation passed by the first democratic government in South Africa. The Act promotes the objective of good financial management in order to maximize service delivery through the effective and efficient use of limited resources.

2.4 FACTORS THAT NECESSITATE REVENUE ALLOCATION SOURCES

According to Gildenhuys, (1993:189) there are two factors that necessitate the allocation of revenue sources to different spheres of government and these factors are the determination of financial needs and financial capacity.

2.4.1 Determination of financial needs

According to Gildenhuys, (1993:189) the three spheres of government have different types of financial needs as a result of the functions performed or services delivered by each sphere. The division of revenue between provinces and municipalities in South Africa takes into account demographic factors, such as the number of school going age and socio economic considerations such as the proportion of people with access to private medical insurance, the number of people with income below the poverty line and the backlog in housing provision. Relative financial needs can be determined by these indicators of demand for public services, taking into account also the costs and affordability of progressive improvements in service delivery.

2.4.2 Determining financial capacity

According to Gildenhuys, (1993:189) the other factor besides financial need which necessitates the allocation of revenue of revenue sources to the different spheres of government is financial capacity. Before sources of revenue can be allocated to the different spheres of government, the financial capacity of such government must be determined.

This means that the capacity of a specific government to generate income, relative to other governments and subjected to the same tax effort and tax base, must be determined. Gildenhuis, (2002:193) puts forward a criteria for determining the financial capacity of the government. These are per capita income of a community, revenue potential of an ideal tax system and the representative revenue system, in which the financial capacity of a government may be regarded as the potential revenue which may be collected within a demarcated area, as compared to the national average per capita rate for each of the various revenue sources applied to similar areas.

2.5 MUNICIPAL SOURCES OF FINANCE

According to Schreiner and Hassan, (2011:37) municipalities obtain their finance from a wide variety of sources but the main categories consist of financial transfers from the central government and locally generated revenue, including debt finance. Central government transfers account for the back of local resources in most countries, particularly for capital investment, and are usually based on a redistribution of certain centrally collected revenues. These transfers bridge the gap between the revenue-raising capacity of municipalities and mandatory local expenditures. Locally generated revenues fall into 3 broad categories that is taxes on property and on economic activities, user fees for the delivery of services and the improvement of infrastructure, and loans borrowed to finance long term investments, generally infrastructure.

Burchell and Listokin, (2012:154) also state that municipal revenue is categorised into two revenue sources. These are municipal own revenue which is raised by the locality itself which consist of taxes and charges and Intergovernmental transfers, contributed by both the state and federal governments. Furthermore, Moshia, (2010:5) states that municipal government derive their revenues mostly from both internal and external sources. Of the internal sources, some are land based in the form of property taxes and land fees and the others are non-land based, like taxes on households and license fees of all sorts, whereas external sources are mostly revenue from intergovernmental transfers, grants, money from borrowing. According to Loots, (2004: 1) since 1998, a share of government revenue collected nationally is distributed equitably to all spheres of government from national, provincial to local government.

According to Bahl and Smoke, (2003:173) the South African Constitution of 1996 and subsequent legislation have given local governments the responsibility for the provision of a substantial number of services, some of which are their exclusive responsibility and others are shared with other spheres of government. Local governments are mandated by the Constitution (section 153a) to give priority to fulfilling the basic needs of their communities. Furthermore, the Bill of Rights explicitly defines access to some municipal services as a basic right of all citizens. To meet these responsibilities, local government is granted a number of sources of revenue by the Constitution and by legislation. According to Moeti *et al*, (2007:76) the municipalities collect revenues in the form of property taxes, municipal levies and service charges and although the South African Constitution does allow the provinces to collect revenue through provincial taxation, this has not happened.

From what has been discussed above, it can be reasonably deduced that municipalities obtain their revenue from two main sources and the researcher will examine these sources, highlight on their value and adequacy to meet the ever rising municipal needs of social and line infrastructure.

2.5.1 Municipal own revenues

Municipalities have the ability to raise their own revenue by means of two major sources i.e. taxes and user charges. The way in which these sources are used differs across municipalities according to their size, location and population base. Section 229 of the Constitution deals with municipal fiscal powers and functions and it provides that municipalities may impose rates on property and surcharges on fees for services provided by the municipality or on behalf of the municipality. It also provides that a municipality may impose other taxes, levies and duties if authorized by national legislation and municipalities may charge for the services they provide, that is, service charges and administration fees.

2.5.1.1 Property rates

The levying of property rates is governed by the Municipal Property Rates Act 2004. Only metros and local municipalities may raise revenue through property rates. In terms of the Act, they are required to adopt property rates policies. Property rates are intended to fund the economic services provided by the municipality, such as municipal roads, storm water systems, street lighting and street cleansing. The consumption of these services is non-exclusive, that is, they cannot be limited to specific consumers so they are funded through a general tax on all potential consumers, namely the owners of property within the municipality's jurisdiction.

2.5.1.2 Service charges and administration fees

According to Bird and Slack, (1993) user fee is a charge per unit of outputs. User fees can take at least three forms which are service fees, public prices and specific charges. Furthermore, Schreiner and Hassan, (2011; 39) state that, user fees form a significant part of municipal revenues, particularly in developed economies. Although widely used, their yield in developing countries has usually been less than the operating and amortization costs of infrastructure system as many governments have set rates below their economic level in order to alleviate hardships on the poor. Pricing of user fees is a matter of public policy, since it plays a central role in determining the financial sustainability of urban services.

A municipality is expected to charge for the services it provides to specific, identifiable customers that derive individual benefit from the consumption of those services. Examples include water, electricity, sanitation, planning and building permissions and the hiring out of municipal facilities. Section 74(2) of the Municipal Systems Act (2000) prescribes that a municipal council must adopt and implement a tariff policy on the levying of fees for municipal services. User Charges are today a much-discussed source of municipal revenue in South Africa and they are designed to generate revenue to cover operating and investment costs.

2.5.1.3 Surcharges, other taxes, levies and duties

The Municipal Fiscal Powers and Function Act (2007) regulate municipal surcharges and municipal taxes, other than property rates. Only the Minister of Finance may authorize a municipal tax by issuing regulations in terms of the Act. The Act also requires municipalities to get authorization for all existing municipal taxes which process still has to be concluded. The Act also empowers the Minister of Finance to prescribe norms and standards for municipal surcharges. The Minister of Finance, acting on his own initiative, may authorize new municipal taxes, or a municipality may apply for a new tax to be authorized.

2.5.2 External sources of revenue

The major sources of external financing for municipalities are various grants from national or provincial government, donor funding, and partnerships with the private sector. Grants include the equitable share allocations which are unconditional and made to all primary municipalities; conditional grants made to those municipalities that apply or are selected to receive funds for achieving specific policy objectives; and grants-in-kind which are made to those municipalities that perform certain services on behalf of national or provincial government are further explained below.

2.5.2.1 Transfers to local government

According to Slack, (2009:35) transfers from senior levels of government are an important source of revenue for municipalities around the world. These transfers from national and provincial government may be direct or indirect in nature. Most transfers entail the funds being directly transferred to municipalities; indirect transfers usually take the form of asset transfers or may be services provided by another sphere of government on behalf of the municipality. Transfers can be broadly

2.5.2.1.1 Unconditional transfers

These have no conditions attached to their use, funds can be spent in any local service or they can be used to reduce local taxes. The vertical division of nationally collected revenues determines the pool of funds to be transferred to local government as unconditional transfers.

2.5.2.1.2 The local government equitable share

This transfer is intended to balance the unequal distribution of fiscal capacity between spheres of government and across municipalities. It redistributes funds from the national fiscus to help fund municipalities.

2.5.2.1.3 Conditional grants

These grants have to be spent on specific expenditures, for example, roads, parks or some other local service. Direct conditional grants are transfers that municipalities may only spend on particular purposes as set out in the conditional grant frameworks. Collectively, these grants are worth almost as much as equitable share transfers. The biggest conditional grant is the municipal infrastructure grant (MIG), which provides funding for municipal infrastructure, principally for extending access to water and sanitation to poor households.

2.5.2.2 *Municipal borrowing*

According to Slack, (2009:43) municipalities may borrow funds from the financial markets to finance part of the economic infrastructure portion of their capital budget. Given that national government does not guarantee municipal borrowing, a municipality's capacity to borrow is a function of sound financial management, sound own revenue management and choice of infrastructure projects. It is envisaged that the metros and the secondary cities should borrow primarily from private capital markets on the strength of their credit ratings, while the Development Bank of Southern Africa (DBSA) will increasingly play its developmental role by lending to the poorer municipalities.

2.6 INDICATORS OF POOR REVENUE COLLECTION AND ALLOCATION

According to The Washington State Office of Financial Management, (2006) municipalities experiencing poor revenue collection and allocation are generally characterized by a number of indicators including (1) low per capita income and tax base condition measured as 50percent below the country's average or median; (2) cash balance of below 5 percent of operating revenue or less than three months of

average operating expenditure; (3) a higher ratio of operating expenditure to debt, higher consumer debt and high proportion of debt to own revenue; (4) a high percentage of earmarked revenue; (5) a high operating deficit; (6) high local services demand measured by high proportions of people without access to municipal services and those eligible for free basic services and (7) low population density levels.

Agyeman and Yung, (1994) further state that municipalities with poor revenue also experience budget crises in terms of balancing the budget, higher tax rates than the population can afford and the inability to maintain a given level of public service. While these characteristics are typical across municipalities with poor revenue, they are neither prescriptive nor exhaustive, given the varying circumstances which prevail across the different categories or types of municipalities in different countries.

2.7 REVENUE COLLECTION AND ALLOCATION CHALLENGES

Kumar, (2013) summarizes some of the other challenges impacting on the ability of municipalities to improve revenue as non-payment by consumers due to unemployment, poverty, declining economic climate and rising electricity costs, little or no growth rate in tax or base rates, absence of credit control policies that are strictly applied and inability of courts to handle the large number of debt collection cases. The factors explained by Kumar, are accompanied by an unacceptable amount of bad debts, thus, a municipality will suffer from poor revenue being collected from citizens.

According to Slack, (2009:10) the challenge of local government is to keep citizens economically viable by delivering high level of services and at the same time, keeping taxes sufficiently low so as not to discourage individuals and business from locating in their jurisdiction. Municipalities are not allowed to increase prices without the approval of the upper sphere; municipalities will suffer from poor revenue since they are collecting very low revenue from services they provide to the citizens.

According to Mosha, (2010:9) municipal government ability to generate revenue through taxation is severely limited because central governments insist on the prerogative of imposing taxes and determining tax rates. Although taxes are the most important source

of revenue accessible to local authorities, the shortcoming is the potential to increase revenues. This shortcoming is exacerbated by the fact that the potential revenue is related to the actual provision of services. In other words, if no services are provided it means there is no revenue that can be collected even if, in terms of household incomes, revenue potential exists. This implies, for example, that the revenue-raising potential is less for rural populations than for urban populations as the former receive fewer services. For example, Nkonkobe Local Municipality is in rural area where some of the poor people are not able to pay for the services rendered.

According to Dirie, (2005) local government in less developed countries like South Africa faces greater challenge when it comes to raising revenue because the municipal revenue base is often weak, especially when compared to the revenue base of the central government. Bird and Slack, (2004) further said that municipalities have few own-source revenues, lack of incentives to generate their own revenues, and do not use the existing revenue potential from these sources. For example, property taxes are difficult to administer and collect.

Slack, (2009:13) state that municipalities have little or no control over the tax rates they can levy and the central there is lack of trust between municipalities and the central government. Furthermore, in many developing countries, including South Africa, the capacity of local government to give effect to its fiscal power is a serious limitation. In South Africa this problem is compounded by the integration of previously disadvantaged communities into municipal boundaries, a culture of non-payment, and poor administrative systems.

2.8 REVENUE COLLECTION AND ALLOCATION MANAGEMENT

According to Venter and Van der Waldt, (2007:199) the accounting officer of a municipality is responsible for the management of the revenue of a municipality. The accounting officer must take all reasonable steps to ensure that among others the municipality has effective revenue collection systems consistent with the municipality's credit control and collection policy, revenue due to the municipality is calculated every month and all revenue received by the municipality, including revenue received by any collection agents on its behalf is reconciled at least every week.

According to Bird, (2001b) increased participation on the part of the public, combined with limited resources at the local level has increased pressure on local government for better municipal financial management. The imbalance between expenditures and revenues at the local level makes it critically important that cities spend the resources they have as efficiently and effectively as possible. Furthermore, the reforms to existing management practices and the introduction of new financial reporting technique have resulted in improving accounting methods and budgeting processes. One example is the use of performance based budgeting to evaluate how well resources are being used and the extent to which the municipality is meeting its objectives.

2.9 Conclusion

This chapter reviewed the literature on revenue collection and allocation in the public sector with a specific reference to the South African municipalities. It alluded to the theoretical framework guiding revenue collection and allocation in this study and the legislative framework governing revenue collection and allocation in South African municipalities. The chapter also highlighted and elaborated on various important aspects of revenue collection and allocation in the municipality including causes of poor revenue collection and allocation and approaches to revenue management. The next chapter outlines the methodology adopted by the researcher in this study.

CHAPTER 3: RESEARCH METHODOLOGY

3.1 INTRODUCTION

This chapter describes the research design and methods that will be used in this study. The research design presents the methodology and methods that will be used in this study. The methodology and method, outlines the research approach and instruments that will be used to collect data respectively. The research design enables the researcher to use data collection techniques that suit the research problem. This chapter will conclude by outlining how the collected data will be analysed and by pointing out what will be covered in the following chapter (chapter 4).

3.2 RESEARCH DESIGN

According to Marczyk, DeMatteo and Festinger, (2010:200) a research design refers to the many ways in which research can be conducted to answer question being asked and it is a plan used to examine the question of interest. The study used the qualitative research approach. According to Van Maanen (cited in Welman, Krugar and Mitchell, 2005) qualitative research is an umbrella phrase covering an array of interpretive techniques which seeks to describe, decode, translate and otherwise come to terms with the meaning of naturally occurring phenomena in the social world. From this assertion, Welman *et al.* (2005) came to the conclusion that the qualitative approach is fundamentally a descriptive form of research. Lewis, Taylor and Gibs, (2005) posit that qualitative data is information gathered in a nonnumeric form. It is a way of collecting information on the knowledge, values, feelings, attitudes, beliefs and behaviours of the target population. Mouton and Marais, (1990) write that qualitative research is characterised by the fact that the researcher is trying to get to multiple meanings and interpretations rather than impose one dominant interpretation.

3.3 DATA COLLECTION TECHNIQUES

According to David and Sutton, (2004), data is what the researcher actually receives from the respondents, be it social or physical. Layder, (1993:54) identifies a number of instruments that can be used to gather data; among these are interviews, intakes forms, questionnaires and surveys, attendance records and documents.

This study uses document surveys as its data collection technique. The researcher opted for document surveys because it saves time and it is cheap because data is already available. Bailey (cited in Devos *et al*, 2005) asserts that official documents or non-personal documents imply documents that are compiled and maintained on a continuous basis by large organizations such as government institutions. Such documents are more formal and structured than personal documents. They include minutes and agendas of meetings, inter-office memos, financial records, statistical reports, annual reports and process records (De Vos et al., 2005).

For the purpose of this study, information will be sought from the following official documentary sources:

- . The Ndlambe Local Municipality Annual Report for the year ended 30 June 2012; and
- .The Auditor General's Report for the Ndlambe Local Municipality for the year ended 30 June 2012.

De Vos *et al.* (2005) posit that when documents are studied, it is of cardinal importance that the researcher evaluates the authenticity, or validity and reliability of documents. The reason for this is that the authors of documents sometimes harbor ulterior motives such as money or prestige. The AG's report and the Annual Departmental report were regarded as reliable and valid for the research mainly because the two are official government documents. These documents were useful because they contained the relevant information needed for the research project.

The choice of document study as the instrument for data collection was informed by the following advantages: *Relatively low cost*- document study is relatively more affordable than, for instance, a comprehensive survey; *Non-reactivity*- unlike surveys or experiments where respondents are aware of the fact that they are being studied, producers of documents do not necessarily anticipate the analysis of their documents at a later stage. The contents of the documents are thus not affected by the activities of the researcher; and *inaccessible subjects*- the researcher does not need to make personal contact with the respondents (De Vos *et al.*, 2005).

However, the researcher was aware of the following disadvantages of document study; *Incompleteness*- reports, statistical records, historical records and historical documents are often incomplete, which means that there are gaps in the data base that cannot be filled in any other way; *Bias*- since documents were not intended for research purposes, there are factors that can influence the objectivity of documents. For example, annual reports of organizations may be formulated to influence consumers positively; and *lack of standard format*- Documents differ quite widely as regards their format. Comparison is then made difficult or impossible, since valuable information contained in a document at a particular point in time may be entirely lacking in an earlier or later document (De Vos et al., 2005).

3.4 ETHICAL CONSIDERATIONS

Bak, (2004) explains that any research that involves people must show an awareness of the ethical considerations and an agreement to conduct the research in accordance with ethical procedures. There are various ethical considerations when conducting a research, but this study considered honesty in reporting of results. The falsification of research results or the misleading reporting of results was avoided (Welman et al., 2005). The information gathered from official documents was used for academic purposes only.

3.5 DATA ANALYSIS

Patton, (2002) writes that qualitative analysis transforms data into findings. This involves reducing the volume of raw information, sifting significance from trivia, identifying significant patterns and constructing a framework for communicating the essence of what the data reveals. Mouton, (1996) describes data analysis as involving 'breaking up' the data into manageable themes, patterns, trends and relationships. According to De Vos et al. (2005) data analysis is the process of bringing order, structure and meaning to the mass of collected data. The purpose of analysis is to reduce data to an intelligible and interpretable form so that the relations of research problems can be studied tested and conclusions drawn. In this study, data will analysed using the filtering technique and content analysis. The filtering method is whereby the researcher filtered out any irrelevant information contained in the voluminous reports.

Welman et al. (2005) describes content analysis as a *quantitative analysis of qualitative data*. They further state that the basic technique involves counting the frequencies and sequencing of particular words, phrases or concepts in order to identify keywords or themes. Jose and Lee, (2007) define content analysis as a technique for making inferences by objectively and systematically identifying specified characteristics of message. Denzin and Lincoln, (2000) explain that content analysis allows for thick description in the analysis of data. This can be facilitated through thematic organization. The themes will then ground the arguments presented in the discussion. The focus considers the frequency with which certain words or particular words or particular phrases occur in the text as a means of identifying its characteristics (May, 2011).

According to Hofstee, (2006) content analysis studies closely examine the content of preserved records. The records are nearly always written documents, although films or videos can also be used. The end goal of content analysis research is to discover the non-obvious meaning contained in the record. Adams, Khan, Raeside and White, (2007) assert that this method may be useful in allowing the researcher to present a picture of what the concepts are but it does not help in understanding why ideas or interpretations arose in the first place. Hofstee (2006) is of the view that these types of studies are invaluable when an in-depth understanding of a text or collection of texts is required.

3.6 CONCLUSION

This chapter has given an exposition of the research methodology applied in this study and the researcher opted for the qualitative approach. In this study, data was collected from official documentary sources the researcher deemed as having the required information. Ethical issues observed in the study were highlighted and justified. The chapter concluded by detailing how the mass of collected data will be analysed using the filtering technique and content analysis. The next chapter will focus on the presentation, analysis and interpretation of the research data which was collected using the methodology described in this chapter.

4 DATA PRESENTATION, ANALYSIS AND INTERPRETATION

4.1 INTRODUCTION

In this chapter the researcher presents the data analyse and interprets it. The data collected from official documents was analysed using the filtering technique and content analysis. The official documents used for this research were the Ndlambe Municipality Annual Report for the year ended 30 June 2012 and the Ndlambe Municipality Auditor General Report for the year ended 30 June 2012. These documents are critically analysed by the researcher in order to identify challenges of revenue collection and allocation

4.1.1 Ndlambe Municipality Annual Report For The Year Ended 30 June 2012

The Annual Financial Statement of Ndlambe Municipality was submitted to the office of the Auditor General as required by section 126(1) of the Municipal Finance Management Act 56 of 2003.

4.1.1.1 *Revenue From Exchange Transactions*

According to Ndlambe Municipality Annual Report, (2012: 17) revenue from exchange transactions refers to revenue that accrued to the municipality directly in return for services rendered or goods sold, the value of which approximates the consideration received or receivable.

4.1.1.2 *Revenue From Non-Exchange Transactions*

According to Ndlambe Municipality Annual Report, (2012: 17) revenue from non-exchange transactions refers to transactions where the municipality received revenue from another entity without directly giving approximately equal value in exchange. Revenue from non-exchange transactions is generally recognized to the extent that the related receipt or receivable qualifies for recognition as an asset and there is no liability to repay the amount. The table below is the financial statement of the Ndlambe Local Municipality where revenue from exchange and non-exchange are shown.

Fig 4.1: Ndlambe Local Municipality Statement of Financial Performance For the year ended 30 June 2013

	Note	2013 R	2012 R
Revenue			
Non-Exchange Revenue.			
Property rates	16	19,069,818	15,632,871
Exchange Revenue			
Service charges	17	24,525,050	15,022,783
Rental of facilities and equipment	18	330,689	215,032
Interest earned - external investments	19	870,954	1,081,540
Interest earned - outstanding receivables	20	1,672,997	5,131,802
Fines		76,910	432,800
Licenses and permits		2,154,470	2,180,958
Government grants and subsidies	21	106,218,163	98,633,372

Other income	22	1,580,837	4,654,122
Total revenue		156,499,888	142,985,278
Expenses			
Employee related costs	23	49,893,071	43,864,502
Remuneration of councilors	24	11,021,955	9,957,032
Bad debts	2,3	11,214,007	18,866,779
Depreciation expense	25	22,937,599	21,546,619
Repairs & maintenance	26	11,103,594	8,891,821
Finance costs		677,391	988,659
Bulk purchases	27	16,730,467	18,163,361
Grants and subsidies paid	28	10,749,961	7,691,014
General expenses	29	32,688,418	25,174,895
Total expenses		167,016,463	155,144,683

Loss on assets	30	69,319	125,458
Deficit for the year		(10,585,894)	(12,284,863)

Source: Adapted In Ndlambe Local Municipality Annual Financial Statement for the year ended 30 June 2013 Page 8

4.2 REVENUE COLLECTION AND ALLOCATION CHALLENGES FACED BY NDLAMBE LOCAL MUNICIPALITY.

The following are some of the major challenges that are confronted the Ndlambe Local Municipality officials (as shown in the Annual Financial Statement above in some of their programs and sub-programmes) which relate to revenue collection and allocation in the department during the year under review.

4.2.1 Dependency on external funding

As indicated in the Ndlambe Local Municipality Annual Report, the most contributor of income in the above schedule is Grant Income being 56, 23% of the total income (2011/2012 financial year) and that is a very serious concern that needs to be addressed with urgent efforts because it is a sign of poor revenue collection and allocation. The Ndlambe Local Municipality is still grant dependent due to lack of income streams and the municipality did not have its own financial reserves to undertake its capital projects hence the daily operations were threatened including the paying of creditors. Revenue scarcity directly influences the extent to which national government augments local revenue through transfers. Transfers are generally pro-poor such that the poorest municipalities like Ndlambe Local Municipality receive the highest grant support. When poorly designed, such transfers tend to ingrain a culture of dependency and minimal revenue raising effort on the part of the recipients. According to Public Services Utilities International (2008), the degree of local government dependency on grants increases their vulnerability to reductions and elimination of grants by national government; as a result of this the municipality suffers from poor revenue collection which will negatively affect service delivery.

4.2.2 Highest amount of bad debts

The increasing and proportionally high level of consumer debt owed to municipalities is a testimony to the existence of revenue collection and allocation challenges. The Ndlambe Local Municipality is suffering from the highest amount of bad debts in the year in question as indicated on the annual report above. The collection of revenue was not as desired and that has resulted to the bad debts amounting to R30, 080,786 as the capacity in collecting and managing the debtor of all customers per category was lacking because both human and physical resources desired could not be obtained. For example, the Ndlambe Local Municipality Revenue Division has only one employed debt collector assisted by other debtor's clerks and this is a challenge that resulted in an increase in amount of bad debts because there is lack of people who can collect all debts and this in turn results in poor revenue collection.

4.2.3 Weak control systems and increased complexity of mismanagement of revenue

The municipality had weak control systems, particularly in the collection and allocation of revenue and this has been exploited by perpetrators of fraud and corruption. In addition, the profile of fraud and corruption perpetrators was diverse as they come from all walks of life, economic circumstances and social classes. Consequently, an increased level of poor revenue collection and allocation has been observed in the municipality. This situation was exacerbated by the fact that the Risk Management unit of the municipality was constrained and limited both in number of staff as well as their level of expertise.

4.3 REPORT OF THE AUDIT COMMITTEE FOR THE YEAR ENDED 30 JUNE 2012

According to the Ndlambe Municipality Annual Report (2012:36) the function of the Audit Committee is primarily to assist the Ndlambe Local Municipality in discharging its duties relating to the safeguarding of assets, the operation of adequate systems, control processes and the preparation of financial reports and statements. The committee operates in terms of section 166 of the Municipal Finance Management Act 2003 (MFMA) (Act 56 of 2003), and has endeavoured to comply with its responsibilities

arising from those requirements. The department of Finance Audit Committee highlighted the following revenue collection and allocation challenges that faced the municipality during the financial year ending 30 June 2012.

4.3.1 Evaluation of Financial Statements

The audit committee noted that lack of appropriate policies, procedures, control mechanism and finance division of the department, makes it difficult for the Municipality to generate a reliable, accurate and complete set of financial statements. For the third time the financial statements were not made available in time for the members to perform the relevant quality reviews on them. At the time of the audit committee meeting arranged to review the annual financial statements, these financial statements were partially complete and the audit committee was not in a position to review and recommend them for approval by the Municipal Manager. The audit committee has reached a conclusion that the department does not have the capacity to produce a set of financial statements within the time frames appropriate to comply with Public Finance Management Act and in the manner prescribed by the applicable accounting framework.

This perpetual failure by the department to meet the deadlines for submission of financial statements will cause poor revenue collection and allocation because they will understate the exact amount of user charges.

4.3.2 Non-implementation of corrective actions

There was poor attendance at Audit Committee Meetings by management which compromised the level of accountability of management performance. The Ndlambe Municipality Department of Finance has for years been failing to implement corrective measures to reduce or to mitigate audit findings and recommendations. In its general reviews conducted during the year under review, the internal audit committee highlighted that there were weak controls and also noted some instances where the control measures set by the Municipality suffered from misinterpretation and noncompliance to policies and procedures or lack thereof. This view is also supported by Du Toit and Van der Walddt, (1999) who assert that the application of complex legislation may sometimes leave room for poor revenue collection and allocation

because regulations and technical points may be difficult to understand; hence, their application sometimes runs counter to their ultimate purpose.

4.3.3 Internal Audit

The internal audit was under-resourced in terms of skills and numbers of personnel because only two employees have since been employed from March 2012 and therefore the department was not in a position to fully discharge its responsibility of collection all revenue due to it. The department also did not operate at full strength for the greater part of the year under review and this impacted on the overall effectiveness of the internal audit during the financial year under review. The audit committee determined that assurance was needed in various areas, such as financial administration which includes revenue collection and allocation. It is imperative for the leadership of the department to take heed of the recommendations of the internal audit committee in order to address the perennial revenue collection and allocation problems confronting the department. The internal audit did not function as required by the Section 162(2) of the MFMA in that it did not report to the audit committee on matters relating to compliance with the Municipal Finance Management Act, the Division of Revenue Act and other applicable legislation.

4.3.4 Poor resourcing

The lack of capacity of the Internal Audit staff and budgetary constraints made it extremely difficult to engage the Internal Audit Activity in either the internal or the external quality assurance reviews. Moreover, the Audit Committee was unable to review and evaluate the accuracy, reliability and credibility of statutory financial reporting in the Annual Financial Statements of the Department. The financial statements were not always readily available to the committee for review and hence the financial statements continued to misrepresent the true financial state of the department.

4.4 REPORT OF THE ACCOUNTING OFFICER FOR THE YEAR ENDED 30 JUNE 2013

In terms of Section 72(1) of the Local Government Municipal Management Act 2003 (Act 56 of 2003) the accounting officer of a municipality must by 25 January of each year assess the performance of the municipality during the first half of the financial year taking into account the past years annual reports, and progress on resolving revenue collection and allocation problems identified in the annual reports. The accounting officer noted the following revenue collection and allocation challenges that were encountered by the department during the financial year.

4.4.1 Poor financial Management

The accounting officer observed that poor revenue management, inefficient utilisation and lack of accountability for financial resources by Ndlambe Local Municipality contributed to poor revenue collection and allocation. This led to poor service delivery and adverse reports. This is a direct contravention of Section 72(1) of the Constitution of the Republic of South Africa which states that the municipality is responsible for improving service delivery for the citizens. According to Pauw *et al.* (2002) weak consequences may lead to perpetrators of fraud and corruption to believe that even if their misdeeds were to be discovered, the repercussions would not be strong.

4.4.2 Corporate governance arrangements

Internal audit functioned for part of the financial year without the necessary capacity and the directorate Risk Management also functioned without the necessary capacity during the year under review. Therefore, it is clear that these two critical units of the department could not execute their mandates effectively due to capacity constraints. This could have paved the way for the reported high bad debts and other forms of poor revenue collection and allocation in the department during the year under review.

4.5 REPORT OF THE AUDITOR-GENERAL (AG) ON THE FINANCIAL STATEMENTS AND OTHER LEGAL AND REGULATORY REQUIREMENTS OF NDLAMBE MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2013.

The above mentioned report of the Auditor-General was submitted in terms of section 21(1) of the Public Audit Act of South Africa read in conjunction with section 188 of the Constitution of the Republic of South Africa and Section 121(3) of the Municipal Finance Management Act of South Africa (MFMA), to express an opinion on the financial statements of the department based on or in accordance with the International Standards on Auditing. The following challenges were confronted by Ndlambe Municipality which resulted in adequate revenue collection and collection.

4.5.1 Reports of the Auditor General

In terms of the Public Audit Act, 2004 (Act No. 25 of 2004) the Auditor General must submit an audit report on the audit of an auditee in terms of the relevant legislation applicable to the auditee. The audit report must be submitted to the relevant legislature in terms of legislation and within a reasonable time. In terms of Section 40 (2) of the PFMA, 1999 the Auditor General is required to audit the financial statements submitted by the accounting officers of a government department, trading entity, or constitutional institution as per the provisions of this Act. It is, however, important that the Auditor General submits an audit report on these statements to the accounting officer within two months after the statements are received. As far as the consolidated financial statements of the National Treasury and the provincial treasuries are concerned Sections 8 and 19 of the PFMA, 1999 state that the Auditor General must submit an audit report on consolidated statements to the National Treasury and provincial treasuries within three months after they have received them.

In the case of the local sphere of government, Section 4 (1) of the Auditor General Act, 1995 (Act No. 12 of 1995) requires the Auditor General to submit a report on the auditing of the accounts of an accounting officer on provincial government level, to the relevant provincial legislature. The Auditor General must transmit a copy of such a report to the Member of the Executive Council (MEC) of a province who is entrusted with the financial matters of such province, the chairperson of the council, and the

accounting officer seven days before he or she submits it to the provincial legislature in terms of Section 4 (2) of the Auditor General Act, 1995 (Act No. 12 of 1995). Section 4 (4) of this Act states that the Auditor General can see to it that a report on the auditing of the accounts and financial statements which he or she has to audit and which was signed by him or her is included in the annual report of the institution. In terms of Section 21 of the Public Audit Act, 2004 (Act No. 25 of 2004) the Auditor General may in the public interest submit an audit report to any legislature, whether or not it be the relevant legislature, or to any organ of state.

4.5.2 Strategies of the AGSA in improving financial accountability

As the SAI of the Republic of South Africa the Auditor General is the only institution mandated to audit and report independently on the spending of South African taxpayer's money. This is crucial in adding credibility to information reported by government, thereby promoting accountability. The Auditor General exists to strengthen democracy by enhancing oversight, accountability and governance in the public sector. This is a constitutional mandate. In an effort to improve and strengthen financial accountability the AGSA employs various strategies and some of these will be discussed below.

4.5.3 Increasing the relevance of audit reports

The AG operates in a constantly transforming and developing country. In order to remain relevant in such a dynamic environment, the AG is constantly redefining itself to meet the challenges posed by the changes. The AG (2007a: 3) states that, "in an effort to enhance governance in the public sector, we continue to explore ways to simplify our reports and make them more relevant to enable the stakeholders to understand the key messages". This helps in enhancing and deepening stakeholders' understanding of the AG reports. This is a very important strategy for it is in the understanding of the audit reports that financial accountability can be improved. As an important strategic initiative towards increasing the relevance of audit reports, the AG introduced a number of changes to their content and format.

Relevance of reporting was introduced as a strategic theme in 2007-08 to drive audit product development and focus the outcomes of the annual audit processes (AG, 2008: 29). This concept implies striking a balance between assuring the quality of auditing,

and enhancing the value of each report to the stakeholders (AG, 2008: 29). Aligning these two requirements reflects the AG's commitment to be responsive to stakeholder's needs and to advance the transformation of public finance management within the parameters of the auditing standards. The office of the AG has implemented effective strategies to improve the quality of audits significantly. These include: the quality control strategy and the incorporation of the new auditing standards into electronic working papers, ongoing training in auditing and quality management, annual pre-issuance prior to finalization of identified audit reports and consistency reviews to ensure consistent reporting (AG, 2008: 30). The annual quality control process is one of the key measures that the office of the AG utilizes to establish whether audits are conducted in terms of International Standards on Auditing (AG, 2007a: 5). The credibility of this review process is enhanced by the reviews of an external entity, the Independent Regulatory Board for Auditors (IRBA) (AG, 2007a: 5). To this end, the AG continues to implement strategies to improve the quality of audits which is an effort to improve financial accountability.

4.5.4 The AG's phased-in approach

In the annual report of 2012- 2013 financial year the AG states that "our audits in the past focused mainly on financial management and fair representation of financial statements, since 2004 we have phased in the audit of reporting against predetermined objectives" (AG, 2011b: 32). In terms of Sections 20 (2) (c) and 28 (1) (c) of the Public Audit Act, 2004 (Act No. 25 of 2004) the AG is required to provide an opinion or conclusion on the performance of the auditee against predetermined objectives. Additionally, Section 13 of the same Act requires that the AG determine the standards to be applied in performing such audits. The Auditor General has adopted a phased-in approach in complying with the relevant sections of the Public Audit Act, 2004 (Act No. 25 of 2004) with regard to the auditing of performance information. As part of the phased in-approach the AGSA adopted various audit procedures in the AGSA annual reports and individual management reports to the departments for them to consider as part of the process to improve performance information being reported (AG, 2007a: 4).

“This approach recognizes the need for the establishment of a framework for performance information and the formalizing of systems and processes within public sector entities to facilitate the definition, collection, reporting and use of performance information” (AG, 2007a: 4). The AG continues to report on the review of auditing of performance information in line with the phased in approach in the auditing of performance information. This approach takes auditing to the next level thereby establishing parameters for enhancing financial accountability.

4.6 Conclusion

From the above analysis, it is clear that the Ndlambe Local Municipality is experiencing challenges in improving revenue collection and allocation at both individual and organisational level. This unfortunate state of affairs is attributed to many factors as highlighted in the Municipality's Annual Report and the Auditor General's Report. This include among others, the highest amount of bad debts, the municipality is grant dependent, poor document management system and the deliberate disregard of the laws, rules and regulations governing the way in which officials in the department should execute their mandates. In such an environment abuse of power and resources is inevitable. Hence the Auditor General's findings for the Municipality were reflective of fraud, poor revenue management and other irregularities including over spending, irregular, fruitless and wasteful expenditure. Unless the Ndlambe Municipality and the upper sphere of Government act seriously without reservations on this impasse, the municipality is likely to continue receiving disclaimers of opinion from the Auditor General. The next Chapter will focus on the conclusion, recommendations, of the study and future research directions.

CHAPTER 5: CONCLUSION AND RECOMMENDATIONS

5.1 INTRODUCTION

This chapter presents the conclusions and makes recommendations based on the research findings. The primary objectives of the study were:

- To explore and examine the challenges faced by Ndlambe Local Municipality in ensuring the effective revenue collection and allocation.
- To examine the causes of poor revenue collection and allocation by public officials in Ndlambe Local Municipality.
- To come up with strategies and recommendations that can help in improving revenue collection and allocation by public officials and therefore enhance effective service delivery in Ndlambe Local Municipality.

5.2 CONCLUSION

The following conclusion and recommendations can be drawn based on the study's major findings emanating from the analysis of the 2011/2012 Ndlambe Local Municipality Annual Report and Ndlambe Local Municipality Auditor General's Report.

- Ndlambe Local Municipality received a disclaimer of opinion from AG due to the lack of direction and accountability within the municipality.
- The Ndlambe Local Municipality is grant dependent because it has a limited revenue base and there is the highest amount of bad debts.
- There were poor standards of reporting in the department and information contained in some reports was far from being accurate. Long lines of communication were also evident which resulted in unnecessary delays in getting information for either internal or external use by the department.
- There was a total breakdown of internal control systems and the Risk Management unit of the municipality was constrained and limited in personnel and expertise. The material areas that were affected include financial administration, planning and reporting. The root causes for these weaknesses are lack of appropriate capacity and expertise at correct levels, lack of will at senior levels to enforce best practices, non-compliance with management

policies, and lack of proper document management system. The researcher concluded that the municipality has poor revenue collection and allocation strategies or practices.

- There is poor attendance at Audit Committee Meetings by management which compromises the level of accountability of management performance. The control measures set by the municipality suffered from misinterpretation of and noncompliance to policies and procedures or lack thereof. The Ndlambe Local Municipality Management has for years been failing to implement corrective measures to reduce or to mitigate audit findings and recommendations. The Audit Committee was unable to review and evaluate the accuracy, reliability and credibility of statutory financial reporting in the Annual Financial Statements of the Municipality.
- The municipality did not have the capacity to produce a set of financial statements within the time frames appropriate to comply with the Public Finance Management Act and in the manner prescribed by the applicable accounting framework.
- The municipality had poor record keeping and record management of documentation.

5.3 RECOMMENDATIONS

The last objective of this research is to come up with strategies and recommendations that can help in improving on revenue collection and allocation by public officials and therefore enhance effective service delivery in Ndlambe Municipality. Based on the above research findings, the Ndlambe Local Municipality should implement the following administrative reforms to improve revenue collection and allocation and these reforms are also applicable to all municipalities in the Republic of South Africa and other public sectors.

- The municipality should take seriously the recommendations of the Auditor General and the Audit Committee and implement them without reservations.
- Excessive levels of municipal debt from residential customers, businesses and government, which undermine the long-term financial viability of the sphere, must be reduced through constant taxpayer education and incentives by way of general improvement in provision of good quality services.
- Government must provide for or enable local government through the Municipal Systems Act of 2000 to issue garnishee orders on defaulting customers and the judicial system should have dedicated courts to deal with outstanding municipal accounts until the debt is reduced to acceptable levels.
- The Revenue Raising Component of the Local Government equitable share should be reformed in such a way that it rewards good performance in revenue collection as opposed to the current Robin Hood system or stepped tax bands which allocate more funding on the basis of low revenue collection.

- The municipality must abide with legislative requirements on financial management so as to ensure effective revenue collection and allocation. For example, Section 96 of the Municipal Systems Act states that a municipality must collect all money that is due and payable to it and for this purpose, must adopt, maintain and implement a credit control and debt collection policy that is consistent with its rates and tariff policies.
- The Municipality should also legislate through section 43 of the Local Government Municipal Systems Act of 2000, revenue collection as one of the key performance areas against which to assess overall municipal performance.
- The municipality also needs to develop measures to convince residents to pay their taxes such as strong public awareness and proactive revenue collection departments would help in revenue collection.
- The municipality should work with private companies and appoint a firm of professional debt collectors who should be registered members of the Council for Debt Collectors to undertake all debt collection. This public- private partnership will enable municipalities to improve revenue since all debts are collected by a private company on their behalf.
- The municipality should endeavour to develop income generating initiatives through introducing programmes that aim to expand the revenue base of the Ndlambe Local Municipality through supporting revenue enhancement activities. This will ensure the transparent management of the revenue function to ensure customer awareness and support and this will further ensure that business and residential customers pay a fair share of the cost of municipal services taking reasonable account of ability to pay. This proposal will expand the municipality's revenue base through eliminating weaknesses in the billing system and improving intergovernmental relationship management.

- The computerization of all the municipal functions will ensure proper record keeping and record management of documentation. It will also facilitate easy retrieval of documentation for internal or external use. The municipality should try to use appropriate but also cutting edge information and communication technologies when feasible in administering local revenue programs. Among the technologies that have proven to be effective are various computerized systems and valuation and electronic and banking systems for payments and accounting.
- The leadership of the municipality should capacitate all the relevant units of the municipality with skilled and experienced personnel to ensure timely, accurate and quality production of reports and financial statement within the time frames appropriate to comply with the Public Finance Management Act and in the manner prescribed by the applicable accounting framework.
- To improve revenue collection, the municipality must implement strictly the established laws, regulations and procedures, and ensure that the taxes and fees are being administered in a transparent, accountable and fair manner. Management and operational staff need to ensure that the property tax and business registers are complete and kept up to date, assessments are calculated properly, tax demand notices are distributed, taxpayers are made aware of their obligations and the procedures to pay, and taxes and fees are collected systematically and fairly from all rate payers and businesses.
- The municipality should mobilise the community through enhanced participatory budgeting and civic participation because this will engage the citizens and also facilitate enhanced revenue collection. Taxpayers and business owners must be convinced to pay their tax obligations and this can be facilitated if they observe improved local services provision and perceive that the taxes and fees are being administered fairly and efficiently.

- The municipality should have close supervision and improved management of revenue collection because this can improve the revenue yield and equity of the rating and business licensing system. Transparency in the whole process is essential. In La Paz, Bolivia for example, then Mayor Ronald MacLean Abaroa supported collection through established banks, and adopted external auditing mechanisms to minimize possibilities of corruption (Klitgaard et al. 2000).

This chapter has briefly outlined the conclusion of the research and the recommendations that the municipality should take in order to overcome revenue collection and allocation challenges. It is clearly explained that the municipality is still grant dependent and there is an unacceptable amount of bad debts the municipality should follow the recommendations given above in order to improve service delivery in the future. For example, the municipality should implement strictly the established laws, regulations and procedures to in order to reduce the amount of bad debts.

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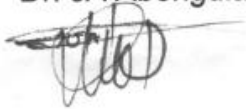
21 August 2015

CONFIRMATION OF EDITING

This is to confirm that I Dr. J. A. Abongdia edited for language use, the thesis entitled Evaluating Revenue collection and Allocation challenges faced by Ndlambe Local Municipality by N.N.Pieters student number 201214461 this editing involved issues such as spelling, punctuation, sentence and paragraph structure as well as language usage. I hold a doctoral degree in Linguistics and work as the language Specialist in the Faculty of education at the university of Fort Hare in East London.

Regards.

Dr. JA Abongdia.

A handwritten signature in black ink, appearing to be 'JA Abongdia', written over a horizontal line.