

THE **Municipal Fiscal Powers & Functions Act**

TOWARDS THE COORDINATION OF MACRO-ECONOMIC TAX POLICY

The Municipal Fiscal Powers and Functions Act (Act 12 of 2007) gives effect to sections 229(1)(b) and 229(2) of the Constitution and is one of the final building blocks in the creation of a regulatory framework to coordinate macro-economic tax policy objectives across all three spheres of government. The Act took effect on 7 September 2007. In 2003, the Provincial Tax Regulation Process Act was enacted, setting out the framework for provincial taxes; the Municipal Fiscal Powers and Functions Act sets out a similar framework for local government.

Purpose of the Act

The Municipal Fiscal Powers and Functions Act (the Act) aims to promote predictability, certainty and transparency in respect of municipal fiscal powers and functions and to ensure that these powers and functions are exercised in a manner that will not materially and unreasonably prejudice national economic policies, economic activities across municipal boundaries, or the national mobility of goods, services, capital or labour.

The Act regulates municipal taxes and surcharges referred to in section 229 of the Constitution, other than property rates (which are regulated by the Municipal Property Rates Act). The Act does not list or identify specific taxes which municipalities may enact. Responsibility for initiating a tax proposal rests with municipalities and organised local government (SALGA); they may propose any tax not prohibited by the Constitution. The Act further provides for the process and procedure necessary for the authorisation of taxes, levies and duties that municipalities may impose under section 229(1)(b) of the

Constitution in a way that allows for the evaluation of applications for consistency with national economic policy and other constitutional requirements. It also regulates the exercise by municipalities of their power to impose surcharges on fees for services under section 229(1)(a) by empowering the Minister of Finance to prescribe norms and standards.

Although the importance of surcharges as a funding source to assist municipalities in meeting their expenditure obligations, especially for poverty alleviation and social and economic development, is acknowledged, these surcharges do increase the tax burden on consumers. It is therefore important to regulate the imposition of surcharges to ensure:

- the reasonableness of the overall tax burden on consumers (who are also subject to provincial and national taxes); and
- that surcharges on fees for services do not materially and unreasonably prejudice national economic policies, economic activities across municipal boundaries, or the national mobility of goods, services, capital or labour.

Who is affected by the Act?

The Act has a direct impact and places various responsibilities on all municipalities. It also has indirect or ad hoc implications for other local government stakeholders, such as SALGA, the Financial and Fiscal Commission and sector departments regulating municipal services, such as the Department of Minerals and Energy, the Department of Water Affairs and Forestry, and the Department of Environmental Affairs and Tourism. For example, the National Electricity Regulator will need to review its current regulatory processes to exclude the surcharge component which currently forms part of the electricity reticulation tariff – that is, the tariff should only regulate the ‘base tariff’, as soon as regulations are issued to prescribe norms and surcharges on electricity reticulation services.

What are the immediate implications for municipalities?

If municipalities are considering the introduction of any new municipal tax, they must comply with the process prescribed in section 5 of the Act. In respect of existing municipal taxes, they must put in place a process to identify all taxes currently levied or imposed, after which they must apply for the continued imposition of the tax in terms of section 12 of the Act. In respect of surcharges, municipalities must ensure that surcharges on municipal services are affordable and reasonable, are set through a transparent process and are disclosed in accordance with section 75A of the Municipal Systems Act. Once the norms and standards for surcharges have been prescribed, municipalities must also comply with them.

When can a new municipal tax be introduced?

A municipality, group of municipalities, SALGA and/or the Minister of Finance (on his/her own accord) may apply for the introduction of a new municipal tax in terms of section 5 of the Act. A municipality may introduce a new municipal tax only after the Minister of Finance has:

- notified the municipality, group of municipalities or SALGA and the minister responsible for local government, in writing, of his/her approval of the proposed municipal tax; and
- prescribed regulations regarding the imposition and administration of a municipal tax or taxes. The regulations will, among other things, determine the date from which the municipal tax may be imposed (the commencement date must coincide with the start of a

KEY POINTS

- The Municipal Fiscal Powers and Functions Act is one of the final building blocks in the creation of a regulatory framework to coordinate the macro-economic tax policy objectives across all three spheres of government.
- The Act aims to promote predictability, certainty and transparency in respect of municipal fiscal powers and functions.
- It seeks to ensure that these powers and functions are exercised in a manner that will not materially and unreasonably prejudice national economic policies and economic activities across municipal boundaries.
- Municipalities must ensure that any existing taxes and surcharges comply with the requirements of the Act within two years.
- The Minister of Finance will announce a long-term replacement for the RSC and JSB levies in the 2008 or 2009 budget.

municipal financial year), the collecting agent of the tax and any limitations placed on it.

What about existing municipal taxes?

All existing municipal taxes will be subjected to a verification process to determine whether they may be continued or should lapse. Municipalities must, by no later than 7 September 2009, apply to the Minister of Finance for the authorisation of any taxes imposed by them prior to the commencement of the Act on 7 September 2007, except for a regional establishment levy or regional services levy imposed under the Regional Services Council Act (Act 109 of 1985) or the KwaZulu and Natal Joint Services Act (Act 84 of 1990). An existing tax will lapse on 6 September 2009 if a municipality fails to apply for its authorisation or six months after the Minister of Finance has notified the municipality that an application is not approved.

What about surcharges?

With regard to surcharges, although municipalities can continue to levy current surcharges on municipal services as

What is a municipal tax?

In general a tax ('levy' and 'duty' have the same meaning) is a government charge which is not in return for a specific benefit. There is not necessarily a direct relationship between the tax payable and the benefits provided by government. Taxes are taken into general revenue and used for general purposes. The taxpayer receives no specific service in return for the payment of tax, but rather a set of general services such as municipal roads, street lighting and the like. Taxes may be contrasted with fees or user charges. For fees and user charges there is a direct link between the amount paid and the benefit provided.

What is a municipal surcharge?

A surcharge on a municipal service is a charge levied by a municipality in addition to the fee or tariff charged for the provision of the service. A surcharge is thus an indirect tax, as it is a payment in addition to the normal charge. Surcharges generated from trading services, such as water and electricity reticulation, are usually used by municipalities for the funding or subsidising of other essential municipal activities where limited or no charges are levied.

budgeted for, municipalities will have to reassess current practices as and when the regulations are made. In the interim, municipalities have been urged by the Treasury to ensure that surcharges on fees are affordable to all categories of users of all municipal services.

The Minister of Finance may prescribe compulsory national norms and standards for imposing municipal surcharges. The norms and standards may differentiate between different kinds of municipalities, types and levels of municipal services, categories of users, debtors and customers, consumption levels and geographic areas. The norms and standards may also determine:

- maximum municipal surcharges that may be imposed;
- the basis and intervals for increasing municipal surcharges; and
- matters that must be assessed and considered by municipalities in imposing municipal surcharges on fees.

Municipalities must comply with any norms and standards prescribed by the Minister of Finance when imposing a surcharge on fees for services. Municipalities must, as part of their budget preparation process, annually review any municipal surcharges and comply with the Municipal Systems Act relating to the manner in which fees, charges or tariffs are levied and how a resolution in that respect must be made known. The Minister of Finance may, where practicalities impede strict compliance with norms and standards, or on

application by a municipality, group of municipalities or SALGA, or of his/her own accord, exempt a municipality from complying with any norms and standards for a period and on the conditions determined in that notice.

Replacement of the RSC and JSB levies

Any permanent replacement(s) for the regional services council (RSC) and joint services board (JSB) levies will be dealt with in terms of the Act. Various medium- to long-term options to replace these levies were proposed in a discussion document by the National Treasury in December 2005. Replacement options, as listed in the discussion document and identified through the consultation process, are currently being evaluated in terms of the intergovernmental fiscal and taxation framework as well as the fiscal framework for local government so as to ensure that any replacement option will have limited negative economic impact, provide adequate revenue at acceptable rates and be easy to administer. The intention is for the Minister of Finance to announce long-term replacement options for the RSC and JSB levies as part of the 2008, or possibly 2009, budget.

This is an adapted version of *MFPFA Circular No. 1: Introduction to the Municipal Fiscal Powers and Functions Act No. 12 of 2007*, issued by the National Treasury. Many thanks to Ms Wendy Fanoë (wendy.fanoë@treasury.gov.za) for her kind assistance in this regard.