REPUBLIC OF SOUTH AFRICA

Medium-Term Expenditure Framework

Treasury Guidelines

2008 MTEF

National Treasury

June 2007

The document is available on the Internet at: www.treasury.gov.za

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Introduction

Government's Medium-Term Strategic Framework (MTSF) continues to focus on growing the economy, improving the organisation and capacity of the state, aligning the spatial planning across the three spheres of government and increasing efforts towards poverty alleviation programmes. In addition, the acceleration of infrastructure delivery programmes is a priority for the coming period. Government spending levels have experienced sustained growth since 2001 to give effect to the strategic priorities. This trend is expected to continue over the 2008 Medium-Term Expenditure Framework (MTEF) and should enable the pace of service delivery to be accelerated. Budget priorities for the 2008 MTEF should give expression to the January 2007 Cabinet Lekgotla, the 2007 State of the Nation address by the President and the 2007 State of the Province address in the case of provinces.

The Ministerial submissions received in response to the request for policy proposals from the Minister of Finance will form the basis of the Ministers' Committee on the Budget (MinComBud) discussion on policy priorities for the 2008 MTEF. It is expected that these priorities will be in line with the MTSF and give effect to departmental strategic plans. Further guidance on strategic planning and budgeting is included in chapter 2 of the guidelines. This chapter highlights the importance of comprehensive budget submissions to include the priorities of state owned enterprises and in order to eliminate the need for additional budget bids through the adjustments budget process.

Although economic performance has shown consistent and sustained improvement, the pace of service delivery in key sectors remains a challenge. Departments are expected to pay particular attention to the causes of service delivery blockages and to institute corrective measures in their planning and budgeting processes to meet specified service delivery targets.

The National Treasury will increasingly complement its role of assessing the quality and credibility of budget bids with an assessment of past performance of departments and assess quantifiable outputs related to departmental programmes. Further information is provided in chapter 2 of the guidelines. Practical guidance is provided in the accompanying *Framework for Managing Programme Performance Information.* It is important that departments familiarise themselves with the content of this guideline in order to continue the drive towards improving non-financial information reported in budget documents, annual reports and other relevant publications.

Chapter 3 provides specific instructions on growth assumptions and inflation projections, guidance on changing of programme structures and budgeting for 2010 FIFA World Cup ™. The National Treasury has established a rigorous process for funding of conditional grants. All applications will be assessed by a conditional grants committee and applications should be submitted in the format and templates required by this chapter and the conditional grants annexure.Chapter 4 on budgeting for infrastructure and capital projects includes revised definitions of classification of capital projects and provides guidance on the funding motivation for new and existing projects. Due to the volume of submissions and the need for intensive scrutiny, all infrastructure funding requests should be submitted by 27 **July 2007**. The Capital Budgets Committee (CBC), a sub-committee of the Medium-Term Expenditure Committee (MTEC), will undertake a detailed review of requests across departments and entities.

Although the budget reforms are applicable to both national and provincial government, certain budget process requirements are unique to provinces. Chapter 5 amplifies the specific processes applicable to provinces and should be read together with the other chapters in the guideline.

The Annexes for completing the budget submission to the National Treasury are attached to the guidelines. All departmental budget bids must reach the National Treasury by Friday, 10 August 2007.

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Budget Process

In addition to observing normal practices related to planning, budget implementation and reporting activities, the following key dates in the 2008 Budget Process should be noted.

2008 Budget Process Critical Dates

Milestone	Date
2008 MTEF Guidelines issued	**June 2007**
Letters to Departments / Ministers	**25 June 2007**
CFO Letters	**25 June 2007**
Submission of Infrastructure Funding Requests	**27 July 2007**
Information Sessions - with national departments	2 July 2007
Education 10X10	11 July
Health 10X10	12 July
Social Development 10X10	13 July
MinComBud: Discussion of spending and policy priorities	18 July 2007
Cabinet Lekgotla: Considers policy priorities and MTSF	23 July 2007
MinComBud: Fiscal Framework and Sector Policy Issues	8 August 2007
Budget Submissions	**10 August 2007**
Budget Council Lekgotla: Revised Fiscal Framework, Division of Revenue (DoR), and Policy Issues	August 2007
MinComBud & Finance MECs: DoR Discussion	4 September 2007
MTEC Discussions	**Late Aug–Mid Sept 2007**
MinComBud: Consideration of MTEC recommendations & MTBPS themes	Beginning of October 2007
Extended Cabinet: Approval of Division of Revenue	October 2007
National Assembly: Tabling of the MTBPS	30 October 2007
Cabinet: Approval of 2008 MTEF	November 2007
National Assembly: Tabling of the Budget	**27 February 2008**

Departmental budget submissions for the 2008 MTEF must reach the National Treasury by **Friday 10 August 2007**.

Medium-Term Expenditure Committee (MTEC) discussions

The Medium-Term Expenditure Committee (MTEC) will focus on the spending priorities outlined in the Medium-Term Strategic Framework and the recommendations from MinComBud on accelerating further spending priorities. The MTEC discussions will focus on particular sector

priorities and examine spending priorities of relevant clusters. It is important that departmental cluster chairs continue to co-ordinate the activities of their clusters to assist in aligning priorities and budgeting. The MTEC will continue to focus its engagements on delivery over the past three years and examine the key service delivery outputs expected over the MTEF period.

MTEC meetings are expected to be hosted between late August and mid September 2007. Further guidance on the MTEC schedule and format will be provided separately.

An information session on the content of the 2008 Budget guidelines will be scheduled for Monday 2 July 2007. Smaller practical technical training sessions will be scheduled to explain the database requirements.

Strategic Planning and budgeting

The link between strategic planning, budgeting and spending plans is important in compiling a credible budget, as inadequate planning could lead to budgets which do not give effect to strategic priorities. In recognition of the different planning needs of policy departments, as opposed to service delivery departments, the National Treasury is developing further guidance on simplifying and improving planning and budgeting processes. These reforms will be updated in the amendments to the Public Finance Management Act (PFMA).

Government's revised MTSF continues to emphasise existing policy priorities of economic growth, focusing on targeted poverty reduction, reducing vulnerability of low-income households, strengthening the capacity of the state and aligning spatial planning across the three spheres[1] Departmental planning and budgeting should be premised on these strategic areas within the available resource envelope. In addition to identifying new policy proposals, strategic plans should address measures to scale up and implement existing programmes and priorities. When developing budget bids for the 2008 MTEF, a re-examination of departmental strategic priorities within the context of the MTSF is important.

In determining priorities for the 2008 MTEF, the implementation of existing programmes, personnel capacity, procurement processes and the achievement of service delivery targets should be considered. Programmes that have not performed as expected should receive particular attention over the Medium-Term.

Despite the buoyancy of the South African economy and the average growth in departmental baselines by 12,1 percent between 2003/04 and 2010/11, the pace of service delivery has been less than adequate. Important targets, which include the reduction of classroom shortages, the eradication of the bucket system in informal settlements, the number of houses being built and the roll-out of HIV/Aids treatment have not been fully achieved over the past few years. Budget submissions for the 2008 MTEF should prioritise areas of slow delivery over the temptation to develop new policy proposals, which are not ready for immediate implementation.

In order to measure the success of government programmes and to accelerate the implementation of these programmes, the National Treasury will continue to assess the efficacy of public spending, or whether value for money has been obtained on past spending. Further guidance is provided in the section relating to performance information.

In order to finalise budget bids for the 2008 MTEF, departments should assess the following criteria:

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[1] Medium-Term Strategic Framework (2004-2009)

Examination of the Baseline

Departments should closely examine their current baselines to ensure that programme funding is adequate to address priorities identified. This may necessitate reallocation of funds within a vote to slow-performing programmes in order to meet service delivery targets. This exercise should include an assessment of capacity and identification of skills shortages. The examination of baseline exercise may, in certain instances, necessitate a change in programme structure. Further guidance on the criteria for changing programme structures is provided in Annexure 6 to the guidelines.

Non-recurrent expenditure

Many departmental programmes include projects that are once-off in nature or involve spending that takes place over a defined period, such as two to three years of the MTEF. These associated costs will not recur once the project is concluded. In order to prepare credible MTEF budgets, these amounts should be excluded when the baseline is re-examined in order to avoid distortions and possible underspending of departmental budgets. Non-recurrent expenditure should be identified by sub-programme in the attached annexures.

Identification of savings

The baseline examination and assessment of performance against actual outcomes should also identify savings to be reallocated to other priorities.

Official Development Assistance (ODA)

Many development partners and donors provide funding or in-kind support for research and development initiatives, in line with departmental strategic priorities.

It is important that this funding be aligned to Government's development agenda, sectoral strategic plan and budgetary priorities, including its sub-regional and African development commitments. The overall donor funded programme should be output and outcome-based such that it contributes to addressing the development challenges stipulated within the sector. The programming and operational plans of donor funded programmes/projects should, therefore, be reflected and captured into the national and provincial budgetary planning process and be clearly linked to performance indicators. This will help ensure replicability and sustainability of the interventions beyond the ODA funding.

ODA should be applied largely as a resource tool for leveraging innovation, best practices, risk-taking and piloting. Modelling of system development ultimately contributes to knowledge sharing, skills and capacity building. It should serve as a knowledge-based instrument to enhance and strengthen the implementation of its own budgetary resources.

The individual ODA programme reporting process should follow the same budgetary reporting systems of the department unless the agreements stipulate additional specific reporting requirements.

All stakeholders are encouraged to identify innovative approaches on how and where donor resource applications could add value. The operational plans for implementation should incorporate actual deliverables including a breakdown of committed and disbursed resources covering direct donor expenditure, including technical co-operation and grants in addition to funds

disbursed to governments. Special consideration should be given to strategic priorities and spending plans over the MTEF.

Disclosure of donor funding will enhance the comprehensiveness of budget bids and assist in resource allocation. Where possible, donor funding should be identified per programme rather than per project, in order to improve presentation and harmonisation with current reporting formats. This will improve the transparency and comprehensiveness of departmental budgets. Stakeholders should declare potential and existing donor support when presenting at the MTEC meetings. This reform should be carefully observed as it will be extended to other financial and non-financial reporting requirements

Relevant information should be captured on the programme sheets and will be summarised in a separate summary sheet..

State-Owned Enterprises/Public Entities

Sections 52 and 53 of the PFMA require public entities, government business enterprises and non-business enterprises to submit their budget bids to executive authorities before the start of the department's financial year. These requirements are intended to ensure that departmental bids are comprehensive and allow certainty and predictability of funds to state-owned enterprises (SOEs). It is important that the budget process is observed by all SOEs and public entities to provide credibility to the allocation process and to avoid the temptation of making additional budget bids through the adjustments budget. The National Treasury will continue to strengthen its monitoring of accountability of SOEs and public entities for public funds.

Performance information

Performance information indicates how well a department is performing against its aim and objectives and could assist in determining budget allocations. This requires moving from input-based budgeting to an output-based results-oriented system linking the use of resources (inputs) to objectives and performance (outputs and outcomes). Credible performance indicators and targets will assist in measuring progress in achieving government's aims and objectives. Over time, this information will increasingly be used to inform decisions on allocations of resources. It is important to set realistic targets, linked to resources allocated to a spending programme and to measure performance against targets on a regular basis. Where necessary, non achievement of targets should be examined and corrective measures instituted through plans and budgets.

National Treasury has issued the Framework for Managing Programme Performance Information providing a detailed guide on using performance information to manage towards results. The framework also provides guidance on developing performance indicators and systems. It applies to all three spheres of government and its entities. It is important that the guidance in the performance information framework is closely observed as the information related to the performance against predetermined objectives, is subject to audit in terms of section 20(2)(c) or section 28(1)(c) of the Public Audit Act, 2004. The Auditor-General has adopted a phased-in approach to compliance with these sections and envisages expressing an opinion on the performance information published by organs of state from 2009/10 onwards. Further guidance is provided in the directive on performance information, published in Government Gazette No. 29919 on 25 May 2007.

The National Treasury is also increasing its focus on monitoring performance. In recognition of the unique nature of different government programmes both trendable quantitative indicators and more qualitative indicators will be monitored. The latter should be presented in the programme and subprogramme sheets, while the trendable quantitative performance indicators should be identified in line with Annexures 5.1 and5.2. .

The National Treasury will consult directly with departments to verify and validate the quality and usefulness of all performance information included in the MTEF submissions. In addition, the National Treasury will work specifically with five departments, who have already been approached, to pilot the use of trendable quantitative performance indicators to be used for tracking programmatic results. This approach to performance monitoring may be expanded to additional departments, as appropriate, over the MTEF period. However, other departments may also opt to submit this information. All the performance information submitted must aid decisions regarding the efficient allocation of resources and for tracking progress in service delivery.

Capital Budgeting

Capital budgeting remains a challenge for many government departments. Good budgeting practice requires an integrated approach to capital and recurrent budgeting to ensure adequate maintenance for capital projects. Chapter 4 provides further guidance on capital budgeting and Annexures 1.1 and 1.2 provide the templates for submitting new and existing capital budget bids.

Budget proposals for 2008

Once the practices outlined in this chapter have been followed, departments should complete 2008 budget submissions in terms of Annexure 2. The submission should be in the form of a letter signed off by the Accounting Officer and include:

- Detailed costing of policy proposals, limited to four (4) bids per department;
- Departmental spending plans over the MTEF;
- Legislative plans;
- Administrative plans;
- Implementation plans; and
- Identified outputs (at sub-programme level) and outcomes (at programme level) in line with the strategic plan and programme objectives over the MTEF
- Additional information requested by relevant budget analysts

In order to assist in preparing comprehensive summaries for the MTEC meetings, it is important that detailed, relevant, narrative information is provided with budget submissions at programme and sub-programme level. The narrative submission should provide further relevant clarification on the submission of annexes and explain how new policies relate to existing departmental aims and programme objectives. Evidence of feasibility studies and implementation readiness should be provided where relevant. An explanation should also be provided on why the new policy proposals could not be accommodated into the reprioritisation exercise. Where business plans of projects have been changed or amended, the deviations from the original financial approval, must be disclosed. Ideally, the written submission should be limited to a maximum of three pages per programme.

3

Instructions to Departments

Growth assumptions and inflation projections

The MTEF allocations provide for average growth of approximately 10 percent in 2008/09 and 2009/10 and an average of 6 percent for 2010/11. The programme baseline for the third-year is an indicative allocation and may change, depending on more rigorous examination of programme baselines.

Wage negotiations and personnel cost

The previous wage agreement will expire on 30 June 2007 and the wage agreement for public servants is currently being negotiated to become effective 1 July 2007. In the interim, departments are advised to budget for the following salary increases over the MTEF. This projection is based on projected CPIX plus 1 per cent.

2007/08	2008/09	2009/10	2010/11
7.5 per cent	6.5 per cent	5.5 per cent	5 per cent

Budget structures

Despite previous guidance on the importance of designing programme structures and the process for amending them, many departments still do not adhere to the guidelines. It is important that budget structures are designed to give effect to departmental strategic plans and that approval is sought from the National Treasury for amending budget structures. This will assist in aligning past expenditure at programme and sub-programme level, in line with revised structures. It should be emphasised that departmental budget structures are not necessarily linked to a department's human resources structure. This implies that budget structures need not always be amended to cater for staff reorganisations. The budget submission must be provided in the proposed new budget structure. Annexure 6 provides further clarification on the design and amendment of programme structures. Additional information may be requested by relevant budget analysts.

Budgeting for 2010 FIFA World Cup™

Guarantees

Certain national departments (Home Affairs, National Treasury, Safety and Security, Communications, Transport, Environmental Affairs and Tourism, Trade and Industry, Justice and Constitutional Development, Foreign Affairs, Health, Sport and Recreation South Africa) provided guarantees to FIFA for the 2010 FIFA World Cup. These guarantees must be reflected in budget submissions per programme under non-recurrent expenditure.

Budget submissions

The 2007 MTEF has prioritised R7,8 billion towards construction and rehabilitation of stadia and R8,3 billion for transportation and related costs of hosting the 2010 FIFA Wold Cup™. This planned expenditure has been classified into two categories:

1. Capital expenditure: Sport (Stadia), Transport (Infrastructure–road upgrades, etc), Communications (appropriate broadcast technology), Safety and Security (additional human resources and surveillance technology).

2. Support services, mainly additional human resources in departments to deal with 2010 requirements. These include allocations to Government Communication and Information Systems, Arts and Culture and Environmental Affairs and Tourism.

In order to determine the progress with capital projects, relevant departments are required to provide regular progress reports on implementation and estimated escalation of costs for those major projects that were funded through the 2007/08 budget. The submission should include:

- The name of the department and the 2010 FIFA World Cup™ project.
- A progress report on the implementation of those 2010 FIFA World Cup™ projects that commenced in the 2007/08 financial year.
- A description of the project, including a clear indication of the readiness of the department to implement the project within the 2008 MTEF and the procurement schedules.
- Planned outputs and links to other 2010 FIFA World Cup™ projects (e.g. connecting stadia to roads/rail links etc).
- Estimated budget implications especially "operational spikes" in the outer years (e.g. Safety and Security will "spike" as the event approaches).
- Estimated escalation of costs for those capital projects that have already commenced in the 2007/08 financial year. The department should use the cost escalations provided by the Bureau of Economic Research at Stellenbosch University as a basis to estimate the cost escalations and the determination of the funding required.
- A monitoring plan for expenditure relating to the 2010 FIFA World Cup™.

Departments responsible for support services should include relevant information in their budget submissions on the status of implementation and reallocation of funds for the event. MTEC will consider issues relating to adjustment of priorities to cater for 2010 FIFA World Cup™ activities and programme allocations. The MTEC discussion will particularly focus on joint inter-departmental meetings to deal with 2010 FIFA World Cup activities to assess the degree of inter-departmental co-ordination. The Medium-Term Budget Policy Statement (MTBPS) will provide detailed information on programmes funded by government and a progress report on those projects that commenced implementation during the 2007/08 financial year.

Requests for approval of conditional grant funding

Policy initiatives or priorities can be initiated in a sector department or may be developed in response to a priority identified by Cabinet or the President's State of the Nation Address. When requesting that a policy initiative or priority be funded as as conditional grant the national department must provide a clear indication of the purpose of the intended grant programme and why it should not be funded as a normal line function programme. The applying department must indicate the, costing and performace indicators of the programme over the MTEF and outcomes (long term and medium term) the grant programme is intended to achieve.

A business plan should be submitted to the National Treasury for consideration and or approval in terms of the conditional grants Excel file attached to the guidelines. Two separate templates have been provided for provincial and national departments. The submission must be signed by the appropriate accounting officer and must address all the information requirements called for in the spreadsheet. Supplementary information can be appended to the submission to provide additional insight as to the merits of the proposal.

The deadline for all conditional grant submissions is Friday, 10 August 2007.

4

Budgeting Framework for Infrastructure and Capital Projects

Overview

This chapter provides guidance on proposals for new and up-scaling of existing infrastructure/capital projects. In respect of funding requests relating to infrastructure and capital acquisitions, they are to be motivated separately from other budget proposals, as infrastructure/capital projects will be reviewed and appraised by a separate sub-committee of MTEC, called the Capital Budgets Committee (CBC)

All infrastructure/capital funding requests and associated explanatory and supporting documentation, motivations and feasibility studies are required before the start of the MTEC process by **27 July 2007**, in order to allow the CBC to undertake a proper review of such requests across all departments and associated entities. A Project Concept Note is also required for all projects or programmes to be appraised and is to be attached to the front cover of supporting documentation.

The type and depth of information required for appraisal will depend on the size and nature of the infrastructure or capital project being considered. Project bids should be suitably motivated through detailed supporting documents, keeping in mind the nature and complexity of the project. All infrastructure projects, programmes and major capital acquisitions must be classified according to three broadly pre-defined categories. These categories will require different levels of analysis and information as they have different budgetary implications and will thus be appraised accordingly. These categories are outlined below.

Classification of Infrastructure/Capital Projects and Programmes

Funding requests for infrastructure and capital projects and programmes must be classified according to the category into which they fall. There are three broad categories of projects/programmes:

- “Mega” projects or programmes: estimated to cost more than R300 million per year for a minimum of three years, or R900 million total project cost;
- “Large” projects or programmes: estimated to cost between R50 million and R300 million per year within a given MTEF; and
- “Small” projects or programmes: estimated to cost less than R50 million per annum.

Within these broad categories, projects can be either *existing projects* or *new projects*. These are discussed in more detail in the paragraphs below, and will be further clarified by the relevant budget analysts.

Mega projects and programmes

Mega projects consist of all new or existing infrastructure projects, programmes and capital acquisitions that require *more than R300 million*, either from the fiscus, from departmental

virements and savings, inter-departmental or inter-sphere funding, or through borrowings (from private or public institutions). All projects that extend beyond the MTEF period also fall within the "mega" category. Being the largest capital commitments on the fiscus, mega projects and programmes will require the most detailed information and preparation and will follow a more rigorous review by the CBC in order to lower risks associated with project failure, as well as limiting the chances of inefficient expenditure. A detailed feasibility study is thus required for all mega projects and programmes.

Large projects and programmes

Large projects consist of all new or existing infrastructure projects, programmes and capital acquisitions that require between *R50 million and R300 million per year*, either from the fiscus, from departmental virements and savings, inter-departmental or inter-sphere funding, or through borrowings (from private or public institutions). Large projects and programmes will also require detailed information and preparation and will follow a rigorous review by the CBC in order to lower various risks of project failure as well as the chances of under-expenditure. A detailed feasibility study is thus required for all large projects and programmes.

Funding motivation for existing and new projects or programmes

Extension of Existing projects or programmes (Small, Large, Mega)

Funding for "existing" projects or programmes is either based on the need to complete or the need to extend, based on new needs, within an existing project or programme. Where many small projects (under R50 million) exist, these may be grouped together and motivated as an infrastructure programme requiring extension. Within this category, it is important to give an accurate and detailed account of the history of the existing project or programme, an assessment of its output performance, the change in needs if applicable, and sound reasoning motivating the extension in respect of timing and expenditure as applicable. Ongoing infrastructure transfers to public agencies, entities and other spheres, which require further support, may also be motivated under this category.

New projects and programmes (Small, Large, Mega)

These are infrastructure projects and programmes, which have not been previously funded. New small projects (under R50 million), which are not part of an existing programme, but which are of similar nature, may be grouped together and motivated as a new infrastructure programme. All new projects or programmes require an appraisal which may vary in complexity depending on the size of the project or programme.

Appraisal process for infrastructure and capital projects

Departments and entities are responsible for the appraisal of projects and programmes that require funding. The CBC will undertake a review of appraisal submissions and make recommendations within an environment of 'competing' requests and scarce resources. Therefore, the onus is on departments to provide suitable detail and ensure that motivations, feasibility studies and other supporting documents are comprehensive, realistic and fully motivated.

The appraisal guideline for infrastructure and capital acquisitions is intended to provide government institutions with procedural framework for the appraisal, approval and budget allocation of new projects. This guidance is designed to promote efficient project development and the efficient allocation of resources across government. This is achieved by informing decision-makers and by improving the alignment of departmental and public entity policies, programmes and projects with government priorities.

Why a project appraisal? A project appraisal is performed for the following reasons:

- To develop and formulate potential projects precisely and concisely;
- To stop badly planned projects (“white elephants”);
- To prevent good projects from being destroyed (promote value for money projects);
- To identify sources of risks and how to reduce and effectively mitigate these; and
- To promote transparency.

The sections below set out some questions/requirements that departments need to look at within their motivating documents to demonstrate advanced planning and/or implementation readiness in their capital budget requests. In general, a submission should be laid out as a discussion, with supporting graphs and tables where statistical information requires illustration. Large and mega projects each require separate submissions.

Mega and Large projects appraisal guideline

The following must be addressed by departments and entities when making funding requests for mega or large projects:

Needs Analysis

A needs analysis must demonstrate why a particular project is required and how the project or programme is aligned to the strategic objectives of an institution. The following aspects need to be considered:

- What are the statistical trends and key indicators in the relevant area of service delivery that point to the need or increased demand at this time?
- What is the extent and urgency of the need and the consequences if the need is not met, by what systems are people/users currently coping and what is the impact on them?
- What proportion of the need is the request intended to fulfil, and how far into the future will it be operational?
- What are the proposed outputs and outcomes, that is, what will be built/procured and how many will it serve, and for how long?
- Does the project/programme fit in with your overall departmental strategic plan or infrastructure delivery plan?

Options Analysis

Alternative ways of meeting a need should be identified and examined when considering project options. A discussion is required on different options considered. These should comprise a range of viable solution options available for providing the specified outputs (for example. the service to be provided as a result of a capital project). The department should explain why the proposal under consideration was selected as the preferred option and why other options were rejected.

Cost-Benefit Analysis

Cost-Benefit Analysis (CBA) estimates and totals up the equivalent money value of the benefits and costs of projects or programmes to society to establish whether they are worthwhile. The following should be considered:

- Show the build-up of all costs, present and future, and all assumptions made to determine these (including escalations due to inflation, exchange rates, tender estimation etc.)2;
- Show the estimates of all revenues (if relevant);
- Identify the proposed or perceived economic and social benefits (to the country and individuals with respect to cost and time saving, positive externalities, etc.) of the project or programme, present and future, and all assumptions made;
- Quantify the social and economic benefits as far as possible over time;
- Perform a financial (and economic) *Net Present V*alue (NPV) analysis on costs and revenues outlining all assumptions made, including financial and social discount rates.

Lifecycle Costs and Affordability

- What are the operational implications of the infrastructure or capital acquisition on the budget of the department/entity in future years (for example, more staff, maintenance, etc) and is this affordable and sustainable?
- What are the operational impacts and responsibility implications on other spheres of government and demonstrate their agreement in this regard?
- If funding is required for a public entity, demonstrate why this should be funded by taxpayers and not the users.

Implementation Readiness

- Indicate the project stage (identification, feasibility, design, tender, construction, etc).
- What is the proposed start target date for construction and what is the estimated construction duration for the project? Outline the implementation schedule of the project or programme. Does it extend beyond the MTEF period?
- Who are the intended implementation agents, such as public works, own department, private sector, etc, for the various stages, from design to construction to project management and monitoring?
- Discuss the level of planning already undertaken/achieved on the project or programme, and what still needs to be done.
- Are there other stakeholders that are required to make this project or programme succeed?
- What are the risks and constraints faced in the delivery of the project/programme?

Funding and Approvals

- Does this type of infrastructure generate ongoing user revenue? Does a trading account exist for this purpose?
- What are the funding sources that have been considered?
- Outline the proportional contributions from each funding source.
- If relevant, why was a PPP option not considered?
- List all approvals and permissions obtained for the project/programme, including environmental impact assessments (EIAs), etc.
- In general, CBC will seek to verify the following:
- Whether the funding bid is consistent with the prescribed guidelines
- If the proposal is consistent with the departmental strategic plan
- The likely financial impact of the project (and project cash flows)
- Assumptions with respect to the social, economic and environmental impacts
- Risks involved and their mitigation
- The appropriateness of proposed funding arrangements
- The template below provides guidance for completing the project concept note and identifying costs.

Project concept note for proposed infrastructure or capital project/programme

1. Project name and location:
2. Type of project:
3. Brief description of the project:
4. Project stage:
5. Estimation of construction duration (months):
6. Estimation of project cost:
7. Outline of needs analysis:
8. Outline of various options considered:
9. Outline of economic and social benefits:
10. Outline of funding sources that have been considered:

The above submission should include programme and sub-programme information.

Identifying costs

Departments must take account of the extent to which projects incur costs over a period of years. Costs should reflect the value of resources displaced, namely, opportunity cost to society, as a

result of the project. Departments must identify and calculate all costs associated with the planned investment; these should include but should not be limited to:

- Capital or construction costs (for example, land, buildings, equipment, labour costs, consultancy fees, contractors and/or any other pre-production expenses)

- Annual operating costs (for example. purchases of additional equipment, personnel costs, loan repayments and associated interest and/or any other operational costs)

- Annual maintenance costs

- In addition, all *non-quantifiable* costs should be listed and described as a matter of public reference.

5

Provincial budgeting process

In addition to the information provided in the previous chapters, provinces are also expected to meet the requirements of their own provincial budget processes. This chapter highlights some of these additional requirements and acknowledges that these may vary across provinces.

The Constitution and Budget Process

One of the major successes of the intergovernmental fiscal relations system was the implementation of a co-operative and participatory budget process, as well as significant improvements in transparency and quality of budgetary information.

The budget process starts early in the year when Provincial Executive Councils review policy priorities against the overall budget framework which includes fiscal policy considerations, overall spending growth and inflation assumptions. This review may give rise to new priorities requiring funding and for which additional resources may have to be identified.

Provinces have embarked on processes to improve or revise current budgetary processes, documents and the capacity of both government and legislatures to use the information provided through the budget process, and to fully exploit the benefits of the forward-looking three-year budgeting system.

In respect of a way forward, the provincial budget process is poised to further improve the performance accountability system, through the institutionalisation of non-financial performance indicators. Thus far, many departments have not succeeded in developing effective non-financial performance indicators, nor have they reported on their in-year performance on a quarterly basis or post-financial year through annual reports. Provincial executives will further need to prioritise the development of meaningful performance indicators and also for each sector or cluster.

Provincial departments are also encouraged to improve the quality of their annual performance plans (APPs) and annual reports, to cover their non-financial performance and service delivery activities. The role of legislatures in this respect is also critical and is dealt with below.

Priority setting

The priorities expressed in the budget must reflect the outcomes of the various political engagements, including meetings of the extended Cabinet and President's Co-ordinating Council, Budget Council, Budget Forum, the National Health Council (formerly MINMECs) and various other technical meetings.

The national and provincial budget processes are interrelated and to a large extent run on parallel lines. National priorities set the context for provincial and local government priorities, which find expression in provincial and local budgets and, in broad terms, are encapsulated in the following priorities:

- Accelerating the pace of economic growth and the rate of investment in productive capacity;

- Advancing participation of the marginalised in economic activity through expanded job creation and the promotion of sustainable livelihoods. Investing in people and ensuring that skills development complements employment creation are critical platforms on which to build future prosperity;

- Maintaining and expanding a progressive social security net, alongside investment in community services and human development;

- Improving the capacity and effectiveness of the state, including combating crime and creating a service- orientated public administration; and

- Building regional and international partnership for growth and development.

Provinces should, within their resources, aim to address all or most of these priorities of government. There should also be an attempt to link these priorities with the Provincial Growth and Development Strategies (PGDS) and the Integrated Development Plans (IDPs) at municipal level. During the deliberations with provincial departments, provincial treasuries should ensure that these linkages are clearly visible between the various departmental programmes, PGDS and the IDPs.

Where critical spending pressures and major policy considerations exist, the Provincial Treasury initiates bilateral discussions with the relevant departments. The policy review component of the provincial budget process or Medium-Term Expenditure Committee meetings are designed to inform departmental planning, budgeting and guides the Provincial Government in evaluating budget proposals.

Interactions further aim to more rigorously examine the economic and fiscal implications of policy development over the medium-term to long-term period.

The timeline for critical budget decisions in the policy review stage of the process is outlined in Table 1

Table 1: Policy review and budget timeline

Date	**Critical budget decisions**
May – September 2007	Propose spending priorities
May 2007	EXCO considers spending priorities
July – September 2007	Revise macroeconomic framework
June – July 2007	Provincial technical committees consider key spending pressures Policy discussions with line departments
September 2007	EXCO considers in year pressures and new policy priorities for the upcoming MTEF
October/November 2007	Adjusted Estimates tabled in Legislature
December 2007-January 2008	Provinces prepare budget documentation
February 2008	Provincial budgets tabled

Revision of five-year strategic plans and annual performance plans per province

The process of strategic planning allows the respective MECs to set the policy direction for the department.

Only one *Five-year Strategic and Performance Plan (SPP)* per provincial department is produced per election cycle and lays the foundation for the development of the *Annual Performance Plans (APP).*

The purpose of the APP is to set out what the provincial department intends to do in the upcoming financial year towards progressively achieving the full implementation of the *SPP*. This means specifying performance measures and performance targets that will ensure that the provincial department realises its strategic goals and objectives set out in the *Five-year Strategic and Performance Plan.*

A secondary focus area of the APP is to provide annual updates on any changes made to the strategic planning framework set out in the *Five-year Strategic and Performance Plan*, for instance, changes resulting from new policy developments or changes in environmental circumstances.

The APP covers the upcoming financial year and the following two years in line with the MTEF. It should inform and be informed by the *Budget* and the MTEF and should show how the provincial department's future service delivery plans link to its MTEF.

The in-year implementation of the *APP* is monitored through the *Quarterly Performance Reports,* while the end-year reporting is done in the departmental performance section of the *Annual Report.*

Preparation of Annual Financial Statements and Annual Reports

The last stage of the accountability cycle starts with the publication of the annual report, which serves to inform the legislature and the public how a department has performed in achieving its stated objectives. The annual report and financial statement provide crucial information of departmental performance for the previous period.

Departmental planning and budgeting

Planning and budgeting are closely related processes. Planning guides the preparation of the MTEF budget proposals that are submitted to the relevant treasury. These proposals are evaluated in line with Government's priorities and recommendations on medium-term allocations made to provincial executive councils.

Before engaging in the planning exercises, provincial departments are expected to review performance or service delivery results of the previous period. These results provide feedback when planning for the new medium-term expenditure period.

Provincial departments are expected to prepare their new MTEF budget proposals by **August 2007** and, where possible, indicate five year spending projections. The 4th and 5th years need not be in as much detail as the MTEF budget figures. In addition to their budget proposals, provincial departments are also expected to also provide the Provincial Treasury with copies of their Annual Financial Statements and Annual Report. These documents are used by the National Treasury

budget analysts when preparing for the Provincial and National Medium-Term Expenditure Committee (MTEC) hearings in September, which focus on the following aspects of the department's MTEF budget proposals:

- The proposed revisions to the department's medium-term plans and the link to Government's broad policy priorities and key challenges identified for each of the sectors;
- The credibility of the costing and affordability of the new proposals;
- The department's ability to implement their new proposals over the MTEF period based on past performance and expenditure trends; and
- The outputs to be achieved in support of departmental objectives.

The following text box illustrates a typical planning process:

Planning process

When assessing service delivery performance against targets and examining provincial departmental strategic objectives against broader government policy and spending priorities, frame the following queries:

- Are provincial departmental strategic objectives and planned outputs aligned with the core functions and mandates of the department?
- Are planned outputs and deliverables still relevant?
- Have service delivery commitments and targets been met?
- ***If*** there is a high degree of alignment between:
  - Government priorities and provincial departmental objectives and outputs?
  - Service delivery performance against targets?

Then the department or institution should revise those aspects of their strategic plan and objectives that will improve service delivery and better achieve the desired results over the next five years.

On the other hand, *if* there is a low degree of alignment, *then* the department or institution will have to take a much more extensive review of its delivery plans in relation to Government's medium-term policy and spending priorities. The available budget affects what may be achieved and helps set priorities for resource allocation and service delivery objectives and targets.

The final stage in the process is to assess the costs and resource implications of the revised strategic plan in terms of the departmental medium-term budget allocation. This may lead to significant reprioritisation of the medium-term budget to reflect changing priorities and fiscal realities, which depend on the broader economic environment.

The MTEC discusses each of the above areas with the relevant department, and finalises a recommendation to The Provincial Executive Committee (EXCO) that details changes to a department's programme structure, objectives and changes to programme MTEF allocations.

The Provincial Treasury allocation letters circulated to departments in mid-November set out the Provincial Executive Committee's decisions on changes to the MTEF programme allocations. The letters give detail, rationale and conditions of the final allocations to provincial departments for the new MTEF period. Once final allocation letters have been received, provincial departments are required to revise their plans for the 2008 - 2011 periods and to pay particular attention to priority policies and strategies and to ensure affordability of their planned outputs.

Infrastructure

Submission of infrastructure project proposals should include infrastructure programme implementation plans by the client department, infrastructure programme implementation plans by the implementation agent and an organisational support plan and in the prescribed Construction Industry Development Board toolkit format, including the Expanded Public Works Programme requirements.

Infrastructure projects and plans should be linked to the strategic and annual performance plans.

Managerial role of legislatures

On Budget Day the MEC for Finance presents the outcome of the Executive's budget process to the legislature, in the form of a three-year expenditure framework and seeks legislative appropriation for the first year.

The provincial budget process is presented as follows:

- The *Appropriation Bill*, once enacted, gives provincial departments the legal authority to spend money allocated to them. A brief summary of the Appropriation Act is provided in Text Box 2:

The Provincial Appropriation Act is explained in the following text box:

Provincial Appropriation Act

Section 213(2) of the Constitution determines, *inter alia,* that money may only be withdrawn from the National Revenue Fund in terms of an appropriation by an Act of Parliament. The Appropriation Act is also a money bill in terms of Section 77 of the Constitution for national departments and section 120 for provinces. The Appropriation Act is therefore the legal mechanism by which departments obtain funds from the National Revenue Fund to finance their activities.

The Appropriation Act contains the expenditure information of all national departments at programme level as well as short descriptions of the aims, outputs and targets of the departments and their programmes. In addition to the allocations per department and programme, the expenditure is also divided between current and capital expenditure, as well as transfers.

The Appropriation Bill must be debated and approved by the National Assembly before it is referred to the National Council of Provinces for concurrence and approval. Once Parliament has approved the Bill, it is referred to the President for assent and enacted.

Alongside, the budget legislation, the MEC also tables *Budget Statement I and 2.* Budget Statement 1 provides an overview of the province and discusses anticipated budget trends and developments over the current and forthcoming MTEF periods. It also provides a snapshot of the

socio-economic and demographic profile of the province, while taking care to isolate salient features. It gives a more detailed analysis of receipts and expenditure performance, covering infrastructure expenditure and transfers to local government and public entities. In addition, Budget Statement 1 dedicates an entire section to analysing the province's fiscal performance in recent years, drawing attention to the fiscal challenges confronting the province. The challenges, for the most part, arise from endeavours to raise receipts and contain expenditure pressures on a wide variety of fronts.

The Budget Statements are endorsed by the MEC for Finance in the Province, which reinforces the notion that the development of the Budget is a political inclusive process. It affords the MEC of Finance with an opportunity to present the political priorities on which the budget is premised, together with general information on economic and financial developments within the province. It should clearly state that the budget is more than just about numbers, but rather about limited resources and hard trade-off—often between competing priorities. It should further explain how the budget gives effect to government's policies and priorities, and how it will be translated into the service delivery to citizens.

Budget Statement 2 provides for individual departmental inputs and therefore has chapters for each vote within the province. Budget Statement 2 provides a summary of the departmental annual performance plan to a level at which the general public and the legislatures can engage the department.

The period between 1 June 2007 and 31 August 2007 is again critical in the provincial budget process. It is expected that the various intergovernmental fora, in particular, the various sector 4X4s, 10X10s and MinMecs will firm up sector priorities for the following year.

It must be acknowledged that the province's specific budget process will differ from other provinces. However, all provinces are expected to submit the first draft of the budget together with their APPs for 2008 on **31 August 2007**. Provincial treasuries at this stage are expected to have had preliminary discussions with provincial departments at two levels. The first level should involve discussions around the 2006/07 Annual Reports and Annual Financial Statements (AFS) and around the first quarter spending of the 2007/08 financial year at the second level.

The National Treasury also visits provinces in July/August of every year. These two-day visits for the 2007/08 financial year will take place between 26 July 2007 and 15 August 2007. The main purpose of these visits is to discuss quarterly performance reporting, non-financial information and its associated databases and first quarter spending of the 2007/08 financial year with provincial departments. Table 2 provides a timeline of the budget process from June to August 2007.

Table 2: Key budget process dates between June 2007 and August 2007

Date	Event
1 June 2007	National Treasury to issue draft budget format guideline for the 2008 budget to provincial treasuries
4 July 2007	Education 10 X 10 meeting
5 July 2007	Social development 10 X 10 meeting
6 July 2007	Health 10 X 10 meeting
26 July and 15 August 2007	National Treasury visits to provinces. Province's specific date will be finalised with the province concerned

Date	Event
31 August 2007	National Treasury issues new guidelines for provincial departments on the Strategic Planning for 2008 Budget. If no new guidelines are going to be issued, provincial treasuries and departments will be notified accordingly.
31 August 2007	Provincial departments submit **2008 infrastructure plans** to Provincial Treasury in terms of Section 40(1) of the Division of Revenue Act, 2007

August 2007 is a critical month in the provincial budget process. The Extended MinComBud (MinComBud together with the MECs for Finance from the nine provinces) meets in the first week to agree on the final recommendations that will be tabled at the National Cabinet for the 2008 Budget.

During August 2007 and September 2007, provincial departments and provincial treasuries will submit 2008 draft budgets and Strategic Plans and Infrastructure Plans to the National Treasury for purposes of the Medium-Term Budget Policy Statement (MTBPS) and the Budget Council Lekgotla.

Provinces will conduct their own Budget Makgotla or Izimbizo from September 2007 through to December 2007. Provincial MTEC hearings are also expected to take place during this period to consolidate the draft budgets based on provincial and national priorities. Three allocation letters will be issued to provinces. The first allocation letter will be issued on 1 November 2007 (Equitable share). The second will be issued on 15 November 2007 (conditional grants).The final allocation letter will be issued in February 2008, after the Budget Council meeting.

The National Treasury will conduct a three-day visit to provinces during late October 2007 to early November 2007. These visits include infrastructure sites (based on the infrastructure reports submitted to the National Treasury) and include bilaterals between treasuries and selected departments. All provinces are expected to table their 2007 Adjustment Estimates within a 30-day period after the National Adjustment Estimate has been tabled.

Second-draft budgets should be submitted to the National Treasury on 3 December 2007. The set of data contained in these budgets is mainly used for the 2008 Budget Review and forms the basis for the provincial benchmark exercise discussions, which are scheduled for the second week in January 2008. The Budgets submitted at this stage are based on the second allocation letter issued to provinces on 15 November 2007. The results of the benchmark exercises will be tabled at the Budget Council meeting in February 2008 and will be adjusted later, in line with the final allocation letter issued to provinces shortly thereafter.

The Minister of Finance will table the national budget on 27 February 2008, while provinces will table their budgets within the two weeks after the national budget has been tabled. The final Strategic and Performance Plans will also be submitted and checked for quality and alignment with budget allocations, before being tabled in the provincial legislatures.

This generic guideline should be read together with the Provincial Budget Process Schedule circulated to provinces on 15 May 2007.

Appendices

- Guidelines on amending programme structures

CONTENTS OF A BUDGET STRUCTURE

A Budget Structure

A Budget structure of four basic structures, namely:

1. Objective structure
   - Main division / programme
   - Sub-programme
   - Elements
   - Activities (the smallest component of an objective that is pursued by an identifiable organisational component which can be cost as a separate entity).

2. Responsibility structure
   Establishment

3. Economic classification structure
   Standard Chart of Accounts (SCOA)

4. Fund structure
   National Revenue Fund

This guideline deals with the first component on objective structure only.

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GUIDELINES ON THE OBJECTIVE STRUCTURE AS ONE OF THE SECTIONS OF A BUDGET STRUCTURE

A. General

1. The objective structure can only be developed after the *aim of the vote* (department) has been established. Expenditure not in accordance with the purpose of a vote will be regarded as unauthorised expenditure. The aim must be continuously examined.
   Aim of the vote (department) will include the following:

   - The needs to be satisfied;
   - Problems to be dealt with;
   - Benefits or result to be achieved; and
   - The outcome that is to be expected.

2. A strategic plan must be developed in terms of Treasury Regulation 5 to achieve the goals (objectives) set within the aim of the vote.

3. The *main divisions /programmes (also called the objective structure)* of a Department are identified through its strategic plans and budget documents. The importance of a clearly defined and concise objective structure that is unique to a Department can not be over emphasised.

   The names and descriptions of each main division must be unique in such a way that it can be immediately linked to a specific department. The Objective structure must be developed to be fixed for at least 5 years. It will serve no purpose to allow departments to amend their objective structures on an annual basis while Government utilises five year strategic plans and three year expenditure plans. Departments change their objective structure almost every year, mostly due to changes to the establishment. *Changes to an establishment will have an effect on the Budget Structure* ***but mainly on the responsibility structure***.

   Changes to an objective structure must be limited to policy decisions that lead to the delivery of a new service or the expansion of an existing service. The objective structure must be seen as a fixed foundation and not something that can be change each time the management of a department changes.

   A clearly defined and concise objective structure will improve:

   - accountability, financial management, monitoring and control;
   - management practice;
   - planning and budgeting; and
   - statistical information.

B. Objective structure features

1. *Main divisions (programmes*):
   - The main divisions (programmes) can be categorised according to a support function or a line function.

   Support function

   Programme 1 will always be "Administration". Activities classified under this main programme refer to those centralised activities that support the Department as a whole.

   This must always be indicated as the first main programme and will include sub-programmes such as:

   - Minister (salary and car allowance only)
   - Deputy Minister (salary and car allowance only)
   - Management (vested on programme 1: DG, DDG, other administrative expenditure of Minister and Deputy Minister)
   - Corporate Services (financial administration, human resources, procurement, legal services, information technology, registry)
   - Property Management
   - SETA's

   Line function

   - Programmes classified under this function contribute directly to the aim of the department, and normally form the key functions of the department.
   - The names and descriptions of these main divisions (programmes) must be unique in such a way that it can be immediately linked to a specific department.
   - The main divisions must be developed to be fixed for at least 5 years.
   - Expenditure may be incurred under the provision of a particular programme only when the aim and programme description include the specific service on which the amount is expended.
   - Expenses not covered by the aim and programme descriptions of the vote will be regarded as unauthorised in terms of Section 34 of the PFMA, therefore the programme descriptions must be examined continually

C. Reasons for changes to an objective structure

1. *Expansion of an existing programme*. (Where a provision arises from the application of a legal requirement, reference to the latest Act and, where appropriate, the section must be inserted in the programme description). A priority classification must be given for the expansion of a programme

    - Due to a policy decision
    - Due to the transfer of functions between Votes or the shifting of funds within a Vote [Section 30 (e) of the PFMA]
        - Between Votes [Section 42 and 33 of the PFMA] [Section 6.5 of the Treasury Regulations]
        - Within [Section 30 (e) of the PFMA

2. *Existing programme becomes redundant*.

    - Due to a policy decision
    - Due to the transfer of functions between Votes or the shifting of funds within a Vote [Section 30 (e) of the PFMA]
        - Between Votes [Section 42 and 33 of the PFMA] [Section 6.5 of the Treasury Regulations]
        - Within Votes [Section 30 (e) of the PFMA

3. Merging or segregation of different Votes

    - Due to a policy decision

4. Changing the name of a programme

    - Due to a policy decision
    - Existing programme name is not unique and need to be refined to be concise and clearly linked to the department

D. Approval of changes to the objective structure

The **form and contents** of a Vote may not be amended without the **prior** approval of National Treasury (Division: Public Finance). The department needs to submit a request to the National Treasury for the approval of a new or changes to their objective structure.

It is essential that changes to an objective structure be done before the start of a financial year and not during a financial year.

The reason being that if an objective structure is changed during a financial year numerous journal corrections need to be passed on the financial system to reallocate expenditure to the new approved objective structure. This always leads to great difficulty with the correct reporting of expenditure and the compilation of financial statements. It also places an extra burden on the financial system because the old objective structure together with the new objective structure need to be kept active until the end of the financial year.

New or changes to an objective structure for ***a new financial year***

The department needs to discuss and finalise any changes to their objective structure with the National Treasury before or together with their MTEF submission (July/ August).

The MTEC deliberations should be based on the new objective structure. By the end of September, the objective structure of a department must be finalised and approved. Changes to objective structures **will not** be considered after this date.

The expenditure trends in the Estimate of National Expenditure (ENE) database should be comparable with the outer years.The department must therefore keep in mind that changes to the objective structure of a department will have an impact on the financial data of historical, current and future financial years. Departments are responsible to revise these figures per programme / sub programme according to the new approved structure.

Changes to an objective structure ***for a current financial year***

Requests for changes to the objective structure for a current financial year are not recommended and will not necessarily be favourable considered by the National Treasury. Only in exceptional circumstances will such a request be considered.

Examples:

- Function shift between Votes which necessitates the creation of a new sub programme or element or activity
- Additional funding received for *unforeseeable and unavoidable expenditure* for which no sub-programme or element or activity existed.
- Funds received for emergency situations (section 16 of the PFMA) for which no sub-programme or element or activity existed.

In order to accommodate these changes in the Adjusted Estimate process the Department should obtain the necessary Treasury approval before the start of the Adjusted Estimate process. A copy of the approved structure change must be submitted together with the Department's Adjusted Estimate input by mid September.

Since changes to the objective structure have to be reported to the Standing Committee on Public Accounts (SCOPA), departments must compile explanatory memoranda containing details of changes with reference numbers and dates of all approvals given by National Treasury.