



MFPFA Circular No. 1: Introduction to the Municipal Fiscal Powers and Functions Act No. 12 of 2007

Purpose of this Circular

The purpose of this circular is to provide guidance on the implementation of the Municipal Fiscal Powers and Functions Act.

1. Overview of the Municipal Fiscal Powers and Functions Act

What is the purpose of the Act?

The purpose of the Act is 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 gives effect to sections 229(1)(b) and 229(2)¹ of the Constitution and is one of the last building blocks in the process of creating a regulatory framework that will facilitate proper coordination of macro-economic tax policy objectives across all spheres of government.

In 2003, the Provincial Tax Regulation Process Act was enacted that sets out the regulatory framework for provincial taxes. The Municipal Fiscal Powers and Functions Act sets out a similar framework for municipal taxes (including surcharges).

What does the Act cover?

The Act regulates municipal taxes and surcharges referred to in section 229 of the Constitution, other than rates on property².

¹ Section 229 of the Constitution provides as follows:

- (1) Subject to subsections (2), (3) and (4), a municipality may impose—
 - (a) rates on property and surcharges on fees for services provided by or on behalf of the municipality; and
 - (b) if authorised by national legislation, other taxes, levies and duties appropriate to local government or to the category of local government into which that municipality falls, but no municipality may impose income tax, value-added tax, general sales tax or customs duty.
- (2) 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—
 - (a) may not be exercised in a way that materially and unreasonably prejudices national economic policies, economic activities across municipal boundaries, or the national mobility of goods, services, capital or labour; and
 - (b) may be regulated by national legislation.

² Rates on property are regulated in terms of the Local Government: Municipal Property Rates Act, 2004 (Act No. 6 of 2004).

The Act does not list or identify specific taxes which municipalities may enact. Responsibility for initiating a municipal tax proposal rests with municipalities and organised local government and they may propose any tax not prohibited by the Constitution.

The Minister of Finance is also empowered to of his own accord, authorise a municipal tax.

The Act 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 and regulates the exercise by municipalities of their power to impose surcharges on fees for services under section 229(1)(a) by empowering the Minister to prescribe norms and standards.

What is a municipal tax?

In general a tax (levies and duties has the same meaning as a tax) may be defined as a government impost which is not in turn for a specific benefit. There is not necessarily a direct relationship between the benefits provided by government to taxpayers and the tax payable. Taxes are taken into general revenue and used for general purposes. The taxpayer receives no specific service in return for his/her/its payment, but receives a set of general services normally referred to as public goods, such as municipal roads, street lighting and the like.

Taxes may be contrasted to fees or user charges. Fees or user charges, while it might be compulsory, are generally requited, in the sense that there is a link between the amount paid and the benefit provided.

What is a municipal surcharge?

A surcharge on a municipal service is an additional charge levied by a municipality in addition to the fee or tariff charged for the provision of a municipal service. A surcharge can therefore be viewed as 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.

A “*municipal surcharge*” is defined in the Act as a charge in excess of the *base tariff* that a municipality may impose on fees for a *municipal service* provided by or on behalf of a municipality in terms of section 229(1)(a) of the Constitution.

“base tariff” & “municipal service” is defined in section 1 of the Act.

Who is affected by the Act?

The Act has a direct impact and places various responsibilities on all municipalities (category A, category B and category C municipalities).

The Act will have positive spin-offs for end-consumers as the Act ensures –

- a proper and transparent process for introducing new municipal taxes; and
- that surcharges on municipal services are affordable.

The Act also has indirect and/or *ad hoc* implications for other local government stakeholders, such as organised local government, the Financial and Fiscal Commission

(FFC) and sector departments regulating municipal services, such as the Departments of Minerals and Energy, Water Affairs and Forestry and Environmental Affairs and Tourism. For example, the National Electricity Regulator of South Africa (NERSA) will need to review their current regulatory processes to exclude the surcharge component which currently forms part of the electricity reticulation tariff, i.e. only regulate the “base tariff”, as soon as regulations are issued to prescribe norms and surcharges on electricity reticulation services.

How does it differ from and / or relate to other local government legislation?

The Act focuses on municipal surcharges and taxes other than property rates and user charges (tariffs).

Municipal property valuation and rating are dealt with through the Municipal Property Rates Act and municipal user charges (tariffs) are dealt through the Municipal Finance Management Act, Municipal Systems Act and sector legislation.

The Act, however, will impact on budgeting, financial management and service delivery as the Act regulates when and how new municipal taxes and surcharges may be imposed.

Why do we need the Act?

Municipalities may in terms of section 229(1)(b) of the Constitution impose taxes, levies and duties (“taxes”), other than rates on property, income tax, a value-added tax, general sales tax and customs duties, appropriate to local government or to the category of local government into which that municipality falls, **if authorised by national legislation**. Without this Act municipalities cannot legally impose any new taxes.

Section 229(1)(a) of the Constitution empowers municipalities to impose municipal surcharges on fees for services provided by them or on their behalf. Section 229(2) subjects these powers to regulation by national legislation and policy.

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

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

When did the Act take effect?

The Act was enacted on Friday, 7 September 2007 and published in Government Gazette No. 30271.

The Act also commenced on that date. A copy of the Act is attached to this Circular.

What are the immediate implications of the Act for municipalities?

Municipalities, must -

- ⇒ if considering the introduction of any new municipal tax, comply with the process prescribed in section 5 of the Act;
- ⇒ in respect of existing municipal taxes, put in place a process to identify all taxes currently levied or imposed, whereafter an application for the continued imposition of the tax must be made in terms of section 12 of the Act; and
- ⇒ in respect of surcharges, 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 Local Government: Municipal Systems Act No. 32 of 2000. Once the norms and standards for surcharges have been prescribed municipalities must also comply therewith.

2. Municipal taxes

Who can apply for a new municipal tax?

A municipality, group of municipalities, organised local government and/or the Minister of Finance on his or her own accord may apply for the introduction of a new municipal tax in terms of section 5 of the Act.

When can this application be made?

As the Act commenced on 7 September 2007, a municipality, group of municipalities or organised local government may, as and when it deems it appropriate, make applications for the authorisation of a new municipal tax or taxes, subject that the process prescribed in section 5 of the Act.

When can a new municipal tax be introduced by a municipality?

A municipality may introduce a new municipal tax only after the Minister of Finance has -

- ⇒ notified the municipality, group of municipalities or organised local government and the Minister responsible for local government in writing of his or her approval or disapproval the municipal tax in respect of which an application was submitted; **and**
- ⇒ prescribed regulations regarding the imposition and administration of a municipal tax or taxes. The regulations will *inter alia* determine the date from which the municipal tax may be imposed (which date must coincide with the start of a municipal financial year), the collecting agent of such tax, the tax base as well as any limitations placed on such tax (section 6 of the Act).

What is the process to be followed by a municipality or municipalities to introduce a new tax?

The Act provides for the process and procedure necessary for the authorisation of taxes, levies and duties in a manner that allows for the evaluation of applications for consistency with national economic policy and other constitutional requirements.

The application process and procedure are set out in sections 4, 5 and 8 of the Act.

Section 7 lists the matters that must be addressed in an application.

What will happen to existing municipal taxes?

All existing municipal taxes will be subjected to a verification process to determine whether the existing taxes 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 a tax imposed by that municipality prior to 7 September 2007 (other than a regional establishment levy or regional services levy imposed under the Regional Services Council Act No 109 of 1985 or the KwaZulu and Natal Joint Services Act No 84 of 1990).

An application must include the matters listed in section 5 of the Act

A tax will lapse on 6 September 2009 if a municipality fails to apply for authorisation thereof or six months after the Minister of Finance has notified the municipality that an application is not approved.

What is the relationship between this Act and possible permanent sources to replace RSC and JSB levies?

Any permanent replacement(s) for the RSC and JSB levies will be dealt with under this Act.

Various medium- to long-term options to replace RSC and JSB levies were proposed in a discussion document that was released for public comment by the National Treasury during December 2005.

Replacement options, as listed in the discussion document, as well as those 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(s) have limited negative economic impact, provide adequate revenue at acceptable rates and are easy to administer.

The intention is to announce long-term options to replace RSC and JSB levies as part of the 2008 (or possibly 2009) Budget.

3. Municipal surcharges

What are the implications of the Act for existing surcharges levied on municipal services?

Although municipalities can continue to levy current surcharges on municipal services as budgeted for, municipalities will have to re-assess current practices as and when the regulations are made. In the interim, municipalities are however urged to ensure that surcharges on fees are affordable to all category of users on all municipal services.

What norms and standards may the Minister prescribe?

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 of municipal services, levels of municipal services, categories of users, debtors and customers, consumption levels and geographic areas and determine -

- ⇒ maximum municipal surcharges that may be imposed (express as a ratio, a percentage of the municipal base tariff or a Rand value and provide bands or ranges within which municipal surcharges may be imposed);
- ⇒ determine the basis and intervals for increasing municipal surcharges; and
- ⇒ determine matters that must be assessed and considered by municipalities in imposing municipal surcharges on fees.

What are municipalities' obligations in respect of municipal surcharges?

Municipalities must comply with any norms and standards prescribed by the Minister of Finance when imposing a surcharge on fees for services.

Municipalities must annually as part of its budget preparation process review any municipal surcharges and comply with section 75A(2), (3) and (4) of 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 the norms and standards, or his or her own accord or on application by a municipality, or a group of municipalities or organised local government, by notice in the *Gazette* exempt a municipality from complying with any norms and standards for a period and on the conditions determined in the notice.

4. Enquiries

Any enquiries on the implementation and interpretation of the Municipal Fiscal Powers and Functions Act may be directed at Ms Wendy Fanoë at:

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