



# A Guide to Municipal Finance Management for Councillors



National  
Treasury

REPUBLIC OF SOUTH AFRICA



**National  
Treasury**

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**A Guide to  
Municipal Finance Management  
for Councillors**

March 2006

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# Introduction

## What it means to be a councillor

We congratulate all councillors on being elected to represent their communities. Councillors will find the responsibilities of this role both challenging and rewarding, and we know that they will uphold the trust that the community has placed in their abilities to serve them well.

Councillors have an important oversight and policy setting role, and a wide range of responsibilities that include community leadership, representing citizens, and making decisions about the provision of services for the betterment of communities. Collectively, councillors are responsible for decisions that affect the lives and livelihoods of individuals, organisations and businesses.

The *Guide to Municipal Finance Management for Councillors* has been developed to ensure that the municipality councillors represent has sound financial management systems and procedures. We trust that it will be informative, helping both new and more experienced councillors to further deepen their understanding of the legal framework and policies that govern the activities of municipalities. We hope it will assist all councillors in modernising municipal planning, budgeting and reporting that collectively will lead to improved financial management and service delivery.

The financial reform process started in the national and provincial spheres of government, and has more recently extended into the local government sphere. The Local Government: Municipal Finance Management Act (MFMA) is a key component of the broader legislative framework governing municipalities, and forms a major part of the reform package to bring about financial management reforms in municipalities. The act aims to strengthen financial management to support municipalities in moving towards an even more sustainable future. We know that through better planning and financial management we will get better at delivering sustainable municipal services to all residents, customers, users and investors.

The legal framework empowers the mayor or the executive mayor or committee to provide political leadership by being responsible for policy and outcomes, and holds the municipal manager and other senior managers responsible for implementation and outputs. Councillors are empowered to play key policy setting and oversight roles in each municipality. Two crucial functions are approving the IDP and budget for the effective delivery of services to communities.

Once these policies, procedures, budgets and service delivery plans are approved, councillors exercise important oversight responsibilities for monitoring and evaluating

## Introduction

the resulting outcomes. Thus, councillors are responsible for oversight and managers are responsible for managing and implementing. This principle is key to effective service delivery at the municipal sphere of government. Officials are held accountable for their performance by regular and consistent reporting to councillors through the formal structures within municipalities. Councillors should use the regular in-year reports, reviews and annual reports as the tool to ensure effective oversight. The challenge is to improve the efficiency and effectiveness of municipalities through the best use of management practices.

Every decision-maker in the sphere of local government (mayor, executive committee member, non-executive councillor or official) must take full ownership of the actions required to ensure successful and sustainable financial management that can only improve service delivery to the people they serve.

Councillors make decisions about how funds will be spent to progressively improve the lives of the citizens they serve. Councillors are required to account for how those funds have been used. We hope all councillors will find this guide a useful resource to help them carry out their important responsibilities.

We thank other role-players in their efforts to empower councillors in their roles and responsibilities. This guide serves as a useful source of information and learning, and we trust that councillors will make constant reference to it. We thank our colleagues in SALGA, national and provincial departments, and donors for making this booklet freely available to all councillors.

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### Acronyms

DoRA	Division of Revenue Act (annual)
DPLG	Department of Provincial and Local Government
IDP	integrated development plan
MFMA	Municipal Finance Management Act (2003)
MSA	Municipal Systems Act (2000)
SALGA	South African Local Government Association
SDBIP	service delivery and budget implementation plan

## About this guide

This guide is designed to help executive mayors or committees and non-executive councillors, working together with municipal officials, to implement legislation that will bring about reform of municipal financial management practices across South Africa. The guide explains how the municipal finance system works and councillors' role within it. The guide takes users through relevant legislation, highlights the need for a more modern, performance-driven approach to municipal financial management, discusses the roles of the national and provincial spheres of government, and looks at the different role-players within municipal structures.

### Municipal government and the Constitution

A new system of government has emerged since 1994 that requires dedicated councillors to play an active role in bringing about the democratic and accountable government of local communities envisaged by the Constitution of the Republic of South Africa (the Constitution). The Constitution outlines other goals for municipalities:

- to ensure the provision of services to communities in a sustainable manner
- to promote social and economic development
- to provide safe and healthy environments
- to encourage public involvement in matters of local government.

The Constitution sets out the mandate for each municipality to strive to achieve these goals, within its financial and administrative capacity.

### Relevant legislation

In order to accomplish objectives for the local sphere of government, Parliament has enacted the Local Government: Municipal Finance Management Act (2003) (MFMA), the Local Government: Municipal Structures Act (1998), as amended, and the Local Government: Municipal Systems Act (2000) (MSA), as amended, as well as other legislation, to lead municipalities to reform and modernise financial management practices. This legislation supplements conventional procedural financial management rules with a performance-based system focusing on outputs, outcomes and measurable objectives. With the leadership of executive mayors or committees and non-executive councillors (whether full-time or part-time, ward councillor or proportional representative), and the active involvement of municipal officials, this legislation will make municipalities more participatory, transparent and accountable. It is essential for councillors to have a solid foundation and understanding of the MFMA, which is the centrepiece of national legislation underpinning municipal finance management reform.

## About this guide

The MFMA aims to modernise financial management practices by placing local government on a financially sustainable footing and supports co-operative government between all spheres of government. Successful implementation of the provisions of the act will maximise the capacity of municipalities to deliver services to their residents, users and customers.

This guide, together with the MFMA's introductory guide, *Modernising Financial Governance...Implementing the Municipal Finance Management Act*, seeks to help councillors understand the links between the MFMA, the Municipal Structures Act and the MSA. These acts (and regulations) form the basis for revamping municipal management. These acts and other related acts, including the Intergovernmental Fiscal Relations Act, (1997), the Intergovernmental Relations Framework Act (2005), the Property Rates Act (2004), the annual Division of Revenue Act (DoRA), and legislation regulating water and electricity and other national legislation planned for 2006 and the medium term, provide the foundation for the reforms in municipalities. They are all intended to maximise the capacity to deliver sustainable services.

### **Performance-driven approach to service delivery**

The benefits of municipal finance management reform will materialise only if the municipality genuinely transforms itself by making a fundamental break from past practices and focuses its efforts on a performance-driven approach to service delivery.

### **The roles of the national and provincial spheres of government**

The MFMA develops supportive roles for National Treasury and provincial departments to assist municipalities in implementing the MFMA. National Treasury chairs a working group consisting of the relevant national and provincial departments, to promote a consistent and coherent approach to the interpretation and implementation of the act. This initiative also aims to develop other support measures to assist municipalities.

There are also different roles and responsibilities assigned to the Minister of Provincial and Local Government, and the MECs for finance and local government. While the primary responsibility of provincial treasuries is to manage the financial affairs of the provinces, the MFMA provides for greater involvement of provincial treasuries in the regulation and management of the finances of municipalities. Provincial treasuries are expected to take appropriate measures to monitor, support and assist with municipal capacity building.

Municipalities are encouraged to contact National Treasury or their provincial treasury where there is uncertainty about the various roles or responsibilities required under the MFMA.

## About this guide

### The different role-players within a municipality

The legislation promotes a governance framework that clarifies and separates the roles within a municipality. As representatives of the people, councillors are ultimately responsible for the type and quality of services provided to the community.

### Oversight and political leadership

By focusing on specific policy and oversight responsibilities, councillors will provide political leadership and direction to the municipality's operation.

Councillors' role of overseeing the financial management and service delivery of their municipality means that they will consult with the community, set priorities and give direction, determine policies, approve budgets for development of the community and delivery of essential services, and monitor the outcomes of policy and budget implementation. Councillors need to take ownership of the implementation of the MFMA and financial management reforms that it will bring about. For councillors to have a complete understanding of the legislation and the financial reforms that need to be implemented, the roles of the municipal manager, the chief financial officer, and other stakeholders will be briefly presented.

### The parts of the guide

The guide is divided into the following 14 parts:

- PART ONE: The governance system in South Africa
- PART TWO: Municipal government in South Africa
- PART THREE: Modernising municipal finance management
- PART FOUR: The process of financial management reform
- PART FIVE: Political and administrative accountability
- PART SIX: Managing assets, liabilities, revenue and expenditure
- PART SEVEN: Municipal budgets and strategic planning
- PART EIGHT: The service delivery and budget implementation plan
- PART NINE: Service delivery mechanisms and municipal entities
- PART TEN: Supply chain management
- PART ELEVEN: Financial reports: councillors' tools for oversight
- PART TWELVE: The audit committee and internal audit unit
- PART THIRTEEN: Forbidden activities and financial misconduct
- PART FOURTEEN: Resolving financial problems

### How to use the guide

The guide is not a legal document, nor does it provide legal opinion or interpretation on any matter contained in the legislation. In providing councillors with an understanding of their responsibilities for municipal finance management, the guide is not intended to

## About this guide

be a 'how-to' book on the various aspects of finance management. Rather, it should be used for general advice and assistance that is intended for mayors, councillors, and municipal officials to develop a broader understanding of their roles in keeping with the spirit of the legislation. It should be read together with the national legislation supporting municipal financial management reform and information posted to the National Treasury website periodically.

### **Other publications**

In addition to the MFMA introductory guide, issued when the act was passed, this guide forms part of a series of publications which have been published by National Treasury to help all stakeholders understand the changes brought about by the enactment of legislation affecting municipal finance management. Annexure 1 provides a list of publications and other information that has been developed to assist municipalities to implement the MFMA. This information is presented on the National Treasury website.

## **PART ONE**

### **The governance system in South Africa**

In 1994, a new system of government for the Republic of South Africa was introduced. Its aim was to democratise state institutions, redress inequality and extend expanded services to the broader population. The new system of government has the following features:

- There is a significant decentralisation of powers, functions and budgeting, through three distinct, interrelated and interdependent spheres of government: national, provincial and local.
- National Parliament comprises two houses: a national assembly; and a national council of provinces, which represents provincial legislatures and organised local government.
- Each of the nine provinces has its own legislatures and executive committees, as well as administrative structures.
- With the recent demarcation of municipalities, there are now 283 municipalities. There are three categories of municipality: metropolitan (category A), district (category C) and local (category B). Each municipality has both political and administrative components. The political components vary, with some municipalities having executive mayors and others having executive committees, each with distinct powers and functions.
- Provincial executives and administrations are accountable to provincial legislatures, and municipal executives and administrations are accountable to municipal councils. The legal framework provides for provincial oversight, support and capacity building.
- The system of election for local government is a mix of directly elected representatives and proportional representation.

#### **How does the Constitution facilitate municipal finance management reform?**

The Constitution provides the legislative framework for the system of governance in South Africa. This framework establishes the three spheres of government. The constitutional framework for the local government sphere covers all municipalities in the country. The Constitution gives each municipality the right to govern, on its own initiative, the local government affairs of its community, subject to national and provincial legislation and oversight.

Recent amendments to the Constitution affect municipal financial management reform in two ways:

First, the amendment adding section 230A provides for municipal borrowing.

The second significant amendment relates to section 139 that gives the relevant province the right to intervene in a municipality's affairs under certain circumstances. If a municipality fails to meet certain obligations, the province may take appropriate steps to rectify the situation. The province may also dissolve a council in certain situations. Chapter 13 of the MFMA provides the supporting processes and procedures.

### **An example of when a municipality fails to meet a legislative obligation**

A municipal council may fail to approve a budget or the revenue-raising measures necessary for implementing the budget before the start of a financial year. A provincial intervention could become necessary if there is a persistent material breach by the council of its obligations to provide basic services or if it persistently fails to meet its financial commitments. An intervention could involve the imposition of a financial recovery plan as an emergency measure or to rectify financial problems in the long term. The Municipal Finance Management Act (MFMA) provides details on the criteria for provincial and national interventions and what processes need to be followed if there is one. The act also regulates the establishment of a municipal financial recovery service to assist in preparing recovery plans.

### **How is the MFMA linked to the MSA and other legislation?**

The MFMA and the Municipal Systems Act (MSA) are very closely linked and aligned. It is important to recognise this early on to better understand, correctly interpret and apply these two pieces of legislation. The two acts complement each other in many areas, and should therefore be read together. Both the MSA and the MFMA deal with internal systems, consultative processes, performance systems and reporting and mechanisms to enhance accountability. For example, chapter 5 of the MSA deals with integrated development plans (IDPs) and their preparatory process, while chapter 4 of the MFMA deals with budgets and their preparatory process. The IDP and the budget must be consistent with each other. This means that the consultative and technical processes should be aligned early so that they become one process.

Important complementary links between the MFMA and the MSA include:

- consistent definitions for municipal services, service delivery agreements, local community, and other important concepts
- planning and budgeting processes that are integrated as ONE process
- credit control and related measures
- adoption by the municipality of a performance system

## PART ONE: The governance system in South Africa

- the annual service delivery and budget implementation plan (SDBIP) with measurable performance objectives
- the annual report, reporting on both financial and non-financial performance
- the procurement of goods and services
- details on municipal entities, including the type of entities and the governance arrangements for such entities
- consultation with the local community for important decisions like budgets, borrowing, IDPs, performance systems, annual reports, entities or alternative service delivery mechanisms
- roles and responsibilities of councillors and officials, including the code of conduct for both.

### ***Other specific legislation***

Table 1 below lists national legislation that may impact on finance management reform in local government. When researching legislation it is important to take into account any amendments.

<b>Table 1 – National legislation impacting on local government</b>
• Electricity Act (1987)
• Labour Relations Act (1995)
• Constitution of the Republic of South Africa (1996)
• Financial and Fiscal Commission Act (1997)
• Intergovernmental Fiscal Relations Act (1997)
• Water Services Act (1997)
• Municipal Demarcation Act (1998)
• Municipal Structures Act (1998)
• National Environmental Management Act (1998)
• Remuneration of Political Office bearers Act (1998)
• Skills Development Act (1998)
• Municipal Systems Act (2000)
• National Land Transport Transition Act (2000)
• Preferential Procurement Policy Framework Act (2000)
• Municipal Finance Management Act (2003)
• Property Rates Act (2004)
• Intergovernmental Relations Framework Act (2005)
• Division of Revenue Act (enacted annually)
• Pension and Medical Aid Legislation
• Other legislation to be enacted in 2006 and beyond

## **PART ONE: The governance system in South Africa**

It should be noted that national legislation overrides existing provincial ordinances. Government has been tasked to look at the repeal of provincial ordinances that are in conflict with the MFMA.

The Intergovernmental Fiscal Relations Act establishes the process of consultation for allocations in the national budget, including the role of the budget forum. The forum is chaired by the Minister of Finance, with representation from the Minister of Provincial and Local Government, provincial members of executive councils (MECs) for finance and the South African Local Government Association (SALGA).

The Intergovernmental Relations Framework Act contains provisions that support the principles of co-operative government. The act introduces mechanisms for inter-sphere planning and co-operation, and formalises the President's Co-ordination Council as a body which consults local government on the implementation of national policy and legislation, among other things.

DoRA is one of the most important pieces of budget legislation for local government, as it provides national allocations for each municipality over the next three years. The Financial and Fiscal Commission Act is also important for the local sphere. The Financial and Fiscal Commission makes recommendations on the fiscal transfers and has the right to comment on matters affecting shifts in powers and functions of municipalities.

Other legislation that impacts on local government and which should be read together with the MFMA is the sectoral legislation dealing with areas such as water, electricity and transport. The Water Services Act contains provisions relating to norms or standards, and the development of plans and tariff mechanisms. The Electricity Act, as amended, contains provisions relating to electricity regulation, such as aspects of licensing, and the sale and supply of electricity within municipalities and tariffs. The National Land Transport Transition Act affects municipalities that are required to perform transport related functions.

The Property Rates Act contains further related provisions that deal with the adoption and contents of a rates policy, rate and tariff increases and documentation that must accompany the budget as outlined in the MFMA. It also requires alignment with community participatory processes and specifically publication of information with the budget. The period for which rates are levied is the same as the budget, unless imposed as part of a recovery plan. The limitation on increases in rates is directly aligned with the MFMA. Councillors also need to be familiar with the supporting regulations for each act.

Other links will be discussed in the budgeting and financial management sections of this guide.

### What does co-operative government mean?

The MFMA fosters a greater level of co-operation across (and within) the different spheres of government, based on systems of mutual support, information sharing and communication and co-ordination of activities – each aiming to add value to the others' responsibilities with a view to improving outcomes for all.

### ***Municipalities and other organs of state must promote co-operative government***

For example, national and provincial spheres of government must meet their financial commitments to municipalities, while municipalities must provide other municipalities, provincial and national government with certain performance, budget and financial information. Municipalities must inform neighbouring municipalities and provincial or national organs of state about any material financial and budget matters that may impact on them directly or indirectly, such as on their planning processes for related services.

The functions of provincial treasuries are to:

- promote co-operative government among role-players
- assist National Treasury in implementing the MFMA
- monitor municipal budgets and outcomes
- monitor and publish reports by municipalities
- assist municipalities with budget preparation
- take intervention measures for breach of the act by a municipality
- exercise powers and perform duties as delegated
- share all information received.

National and provincial treasuries will assist with and support a municipality's compliance with the MFMA, and will help to build a municipality's capacity and help to identify and resolve its financial problems where necessary. Around February and March of each year, the national and provincial spheres of government have to publish three-year allocations per municipality, with their budgets. This is to allow municipalities to devise strategic plans and improve implementation measures for the functions they perform, from July of each year. The act also establishes a timeframe for parastatals, bulk suppliers and national departments to advise municipalities of any tax and tariff policies; it provides for national or provincial departments that supply bulk resources to municipalities, like electricity and water, to consult with those municipalities.

District municipalities have municipal executive and legislative authority in areas that include more than one municipality, and are described in section 155(1) of the Constitution as category C municipalities. District municipalities have a supporting role to play in planning and co-ordinating activities within their boundaries. It is therefore

imperative that allocations between district and local municipalities are resolved during the period of consultation on the budget. The relevant provincial government also supports the co-ordination and monitoring of these plans and programmes.

The MFMA requires the mayor to report to national and provincial government at any time when the municipality does not comply with the act. It describes the consultative process required by municipalities on various financial matters and lays out the process for interventions into any municipal financial problems.

### **Summary - Councillor accountability and oversight**

The Constitution established a framework for local government and the oversight role of provincial and national government. It places very important responsibilities on the councillors that govern each municipal council. Councillors are given the right to govern, on their own initiative, the local government affairs of their community, subject to provincial and national legislation.

Recent amendments to the Constitution and other national legislation, and the enactment of the MFMA, increased the accountability and oversight responsibilities of councillors for municipal financial management reform. The councillors' oversight role becomes more important because new provisions of the Constitution and the MFMA allow the provincial executive to take appropriate steps, including the power to dissolve a council, if a municipality fails to fulfil an executive or legislative obligation. Therefore, the municipal council is responsible for identifying and providing remedies for the municipality's own financial problems.

The MFMA and other national legislation will provide direction to councillors in contributing towards municipal financial management reforms. As financial management improvements are implemented through more effective oversight of the outcomes of its decisions, municipal councils will contribute to improving the delivery of municipal services to all residents, customers and users.

# PART TWO

## Municipal government in South Africa

The Constitution provides the structural framework for municipalities including their purpose, duties and functions.

The Constitution vests in the municipal council the legislative and executive authority to administer local government matters (listed in part B of schedules 4 and 5 of the Constitution) and any other matter assigned to it by national or provincial legislation. A municipal council may make and administer by-laws for the effective administration of its lawful responsibilities and any matter that is reasonably necessary for, or incidental to, the effective performance of these responsibilities. However, a municipal by-law that conflicts with national or provincial legislation is invalid.

### **What are the principal responsibilities of local government?**

The objectives of local government are based on a co-operative government framework that encourages participation with other councils within the district, as well as the provincial and national spheres of government, in public policy setting, development planning and the delivery of services.

The constitutional mandate for municipalities is that they strive, within their financial and administrative capacity, to achieve the objectives and carry out the developmental duties assigned to local government. The municipal council therefore takes on the following principal responsibilities:

- to provide democratic and accountable government without favour or prejudice
- to encourage the involvement of the local community
- to provide all members of the local community with equitable access to the municipal services that they are entitled to
- to plan at the local and regional level for the development and future requirements of the area
- to monitor the performance of the municipality by carefully evaluating budget reports and annual reports to avoid financial problems, and if necessary to identify the causes of financial problems and resolve them as they arise
- to provide services and facilities, and financial capacity, within the constitutional and legislative authority, that benefit ratepayers and residents, and visitors to its area. These would include, but are not limited to, general public services or facilities (such as electricity, water and sanitation services, waste and refuse removal), community services or facilities, and cultural or recreational services or facilities, while focusing on core functions as a priority

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- to provide infrastructure for the community and for development within the area by promoting an attractive climate and locations for the development of business, commerce, industry and tourism
- to manage, improve and develop resources available to the council.

In its oversight role, the municipal council takes responsibility for the financial affairs of the municipality. The council must establish that the municipality is meeting and will continue to meet its financial commitments and that it will avoid financial problems. If serious financial problems persist, the council must be active in its oversight role to identify the causes of the problem and ensure that appropriate remedies are instituted.

### **What is the municipal council and how does it function?**

Each municipality covers a defined geographic area, which varies in size, population, and land use. The area may be rural or urban and the population may vary from fewer than 20 000 inhabitants to several million. These differences aside, all municipal councils have the same responsibilities over the governmental affairs of its community. The MFMA recognises the right of the council to govern and reinforces its responsibilities of policy approval and oversight over the activities of the municipality.

The residents and ratepayers of a municipality elect the municipal council to decide on their behalf, on the overall direction and policies for the municipality. The municipal council is regarded as a corporate body or legal entity, which can acquire rights and incur liabilities in a legal sense. It may take action against individuals and other bodies and in turn be sued. Individual councillors have no authority to make decisions or act on behalf of the council unless the council has made a specific delegation. The council members as a whole form the body that has the power to govern. Therefore, councillors need to understand that the best way to influence policy decisions is by giving input when council policies are formulated and approved at duly convened council meetings.

The Municipal Structures Act, the MSA and the MFMA prescribe the legal framework for the structure and operation of municipal councils. The municipal council operates by votes taken at formal meetings of the council. The municipal council makes decisions to ensure that its functions are performed correctly.

The municipal council must elect its speaker, and may elect an executive committee and other committees, subject to national legislation. The speaker presides at meetings, ensures that the council meets at least quarterly, maintains order during meetings and performs other duties delegated by the council. The speaker or another councillor may perform the role of a mayor, if so delegated, depending on the type of municipality prescribed in the Municipal Structures Act.

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A majority of the members of a municipal council must be present before a vote may be taken on any matter. Matters include:

- passing by-laws
- approving budgets
- approving policies imposing rates and other taxes, levies and duties; and
- approving loans.

For example, if a municipal council consists of 51 members, then it would take 26 members present in any meeting before the council could take formal action on a matter. The municipal council may not delegate decision making on any of the issues listed above.

For instance, in order to consider and adopt a by-law, the municipal council must ensure that all the members of the council have been given reasonable notice and that the proposed by-law has been published for public comment. A municipal council may make by-laws which prescribe rules for internal council arrangements, conducting council business, and establishing committees. When a committee is being set up, the municipal council determines its composition, procedures, powers and functions.

The Municipal Structures Act requires a municipal council and its committees to conduct business in an open manner. In an open and democratic society, municipal councils or council committees must make provisions for notifying the public about meetings and how they can attend and participate. They may close their sittings only when the nature of the business being conducted demands this. Members of a municipal council are entitled to participate in all council and council committee proceedings. Consistent with the principles of democracy, all interest groups are allowed to be fairly represented in all matters before the council.

Larger municipal councils have an executive committee and a mayor. The Municipal Structures Act prescribes the right of the council to elect an executive committee from its members. Once elected, the executive committee must elect a mayor. The MFMA, the MSA and the Municipal Structures Act prescribe certain duties and responsibilities to executive mayors and committees of municipalities that will be discussed further on.

### **What are the councillors' responsibilities in relation to municipal staff?**

#### ***Municipal manager, executive mayor and municipal employees***

The Municipal Structures Act requires a municipal council to appoint a municipal manager. The municipal manager is responsible for ensuring that the policies of council are implemented. The municipal manager is the accounting officer of the municipality

and is accountable to the executive mayor or council for implementing specific agreed outputs, and to the council for the overall administration of the municipality. The municipal manager reports directly to the executive mayor and indirectly through the mayor to council. The executive mayor is responsible for approving the annual performance contract for the municipal manager and monitors actual performance. All other municipal employees report directly to the municipal manager.

### ***The organisational structure***

Organisational structure refers to the way a municipality and its separate units are organised in order to optimise delivery of services to the community. In essence, when councillors adopt the annual budget, they are funding the organisational structure.

As head of administration, the municipal manager has the principal responsibility of forming and developing an effective, efficient and accountable organisational structure. The organisational structure of a municipality is a policy decision that must be made by the municipal council. It is often established in line with authorisations agreed at the time the budget is adopted. Each year, when councillors consider the municipality's budget, they should also review its organisational structure and related staff complement.

Two important elements of an organisational structure are the way in which responsibilities are managed and the number of staff required for carrying out various municipal responsibilities. Councillors have important responsibilities in relation to both. Setting employment equity policy and targets is the mechanism for council to exercise its oversight role. Councillors do not have a role to play in recruiting, selecting and appointing staff below the top management structure, but they will establish certain parameters or principles for recruitment and selection of staff in a human resource management policy.

### ***Appointing senior managers who report directly to the municipal manager***

First, councillors are involved in appointing managers who report directly to the municipal manager. Section 56 of the MSA prescribes that the municipal council appoints senior managers, after consultation with the municipal manager. These managers make up the municipality's senior management team and will be limited to the top structure of the municipality.

Council should take utmost care in exercising this responsibility. The MSA further states that the managers to be appointed must have the relevant skills and expertise to perform the duties required by the position in question. The senior management team has a critical role in the delivery of municipal services to the local community in a sustainable and equitable manner. Because of this, the municipal council should give

considerable attention to the selection criteria for such positions developed by the municipal manager and to consulting with the municipal manager. If the municipal manager does not have satisfactory input in selecting candidates, establishing a good working relationship may be very difficult and could undermine service delivery outcomes. The municipal council and the municipal manager must take responsibility and be held accountable for the success or failure of the senior manager.

### ***Setting the optimal number of staff for efficient and effective service delivery***

Second, in setting the organisational structure at the same time that the annual budget is adopted, the municipal manager, in consultation with the council, must seek to approve the optimal number of staff required to meet municipal service objectives within its fiscal ability to sustain services. The organisational structure must be both efficient and effective. Efficiency requires the number of staff to be as low as possible, while effectiveness requires that the number of and type staff are at least at the level that will be successful in accomplishing assigned responsibilities. Poorly skilled staff is often the reason for failure to adequately deliver services to the community. On the other hand, if too many staff members are assigned to an organisational unit, this can be wasteful and may hinder productivity. The overall goal is to strive to balance staffing requirements for both efficiency and effectiveness.

In addition, a municipality's risk management system and its system of internal controls often rely on an adequate number of qualified and well-trained municipal staff. It is important that vacancies be kept to a minimum in order for the risk management programme to function properly.

### ***Human resource management***

The municipal manager acts as an advisor to the executive mayor or committee and council in relation to the organisational structure. Once councillors have authorised the organisational structure, the municipal manager must administer municipal units in accordance with the policy directions set by the council. The municipal manager is responsible for the appointment, performance, management and disciplining of all employees of the municipality, including the senior management team. The municipal manager must ensure that sound principles of human resource management are applied to all aspects of employment in the municipality. Human resource management practices must include fairness and due process.

Councillors have no formal or informal authority to direct or in any way interfere with an employee in the performance of the employee's duties. It is important to understand that to do so would be a violation of the MFMA prohibitions on interference by a councillor and the Code of Conduct for Councillors (MSA, schedule 1). Therefore, councillors must work through the municipal manager in all matters involving both

service delivery and municipal employees. An effective working relationship based on mutual respect between councillors, the municipal manager, and the senior management team, and municipal employees in general, will better achieve council's objectives and policies. A working relationship that values all contributions by the municipal staff will foster a team approach and boost employee morale. It is important for councillors and the municipal manager to work together to both understand their respective roles and responsibilities and encourage municipal employees to meet the needs of the community.

While neither the council nor the mayor has administrative responsibilities in relation to staff, the MFMA requires the mayor to take all reasonable steps to ensure that annual performance agreements for the municipal manager and all senior managers, comply with the MFMA and the MSA. The annual performance agreements should promote sound financial management and the mayor must ensure that they are linked to measurable performance objectives approved by council in the IDP, budget and SDBIP.

### **Why is effective community consultation important?**

Effective community consultation, or participatory democracy, and developing mechanisms to better engage with communities, is a central theme of the MFMA. The aim is to create greater community awareness and promote more accountable decision-making processes by government in line with good financial governance principles.

The MFMA promotes a participatory, consultative approach to municipal decision-making, and prescribes very specific matters in which a council must formally engage its community. This approach is intended to engender a greater understanding of community needs and promote a system of accountability that will lead to a more autonomous, empowered and responsive council.

### ***The process for effective community participation***

The process for effective community participation is described in both the MFMA and the MSA. Municipal councils must be open, fair and transparent. There are a number of ways for councillors to accomplish open and transparent government. For example, council and committee meetings must be held in public except in special and very limited circumstances. The duty to hold meetings in public does not make informal gatherings involving councillors, members of committees, or councillors and staff unlawful, provided that matters dealt with in the informal meetings do not result in a decision outside of formally constituted meetings.

Minutes of all meetings must be prepared and submitted to councillors on a timely basis. After councillors have reviewed the minutes, they are formally adopted and must

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be made public to anyone who requests access to them. Minutes of council and committee meetings are not verbatim records of everything said, rather they are a record of decisions reached and actions taken.

The minutes of every council or committee meeting must include:

- the names of everyone present, and the times they entered and left the meeting
- details of all motions and amendments, including the names of the mover and seconder and the outcome of the motion or amendment
- any disclosure of interest made by a councillor or any personal explanation by a councillor.

Each councillor, after a council or committee meeting, must be supplied with a copy of the minutes of the proceedings of the meeting. The minutes of the meeting are to be adopted at a council or committee meeting, but may be amended before being confirmed. Decisions to take action resolved at a council meeting and recorded in the minutes should not, however, be delayed until after the minutes are confirmed.

It is expected that officials will provide technical support to councillors to strengthen public participation across the municipality.

### **Summary - Councillors' right to govern**

The legal framework gives councillors of a municipality the right to govern the affairs of the council. A municipal council may make and administer by-laws for the effective administration of its lawful responsibilities and any matter that is reasonably necessary for, or incidental to, the effective performance of these responsibilities.

It is the council members as a whole that form the body and have the power to govern. The municipal council operates by votes taken at formal meetings of the council. A majority of the members of a municipal council must be present before a vote or action may be taken on any matter. A municipal council is required to take all actions concerning the following functions by a supporting vote of a majority of the municipal council for: passing by-laws; approving budgets and policies that impose rates and other taxes, levies and duties; and approving loans.

The MFMA and other legislation require municipal councils to be open and encourage the involvement of the local community. Council and committee meetings are held in public except in special circumstances. Informal gatherings involving councillors, members of committees, or councillors and staff may be held provided that no decisions are made except in formally constituted meetings. Closing council or council

committee meetings to the public may only be done when the business being conducted makes it reasonable and justifiable to do so.

The organisational structure of a municipality is a policy decision made by councillors. Normally the organisational structure is established in line with authorisations envisaged in the adopted budget. Councillors must work through the municipal manager in all matters involving both service delivery and municipal employees.

A working relationship that values all contributions by the municipal staff will foster a team approach and boost employee morale. Councillors working co-operatively with the municipal manager help to encourage municipal employees to meet the needs of the community.

### PART THREE Modernising municipal finance management

The MFMA recognises that financial management systems, processes and policies in local government must be modernised to help strengthen the municipality's ability to function effectively.

#### **What was wrong with the old system of finance management?**

In the past, budgets were incremental (one-year) and backward-looking, as they were based on the previous year's budget. The budgeting and planning processes were not integrated, often operating completely separately. Budgets were presented in considerable financial detail, hampering effective policy and planning processes, and making understanding difficult and consultation unwieldy. Revenue and capital estimates were unrealistic, which resulted in poor service-delivery performance and failure to meet community expectations. There appeared to be little or no link to a comprehensive long-term fiscal or financial strategy and little co-ordinated community development. In addition, financial reporting was often inaccurate or ineffectual and internal controls were poor or non-existent. These are some of the tendencies that the reforms seek to eradicate.

#### **How is the MFMA used to modernise municipal finance management?**

Implementing the MFMA thoroughly will lead to better accountability, oversight and transparency, and there will be more clarity over roles and responsibilities of municipal councils. Under the MFMA, councillors have greater responsibility in overseeing municipal financial management and will need to account to their communities for the financial performance of their municipality. The legislation promotes a more strategic approach to financial management, linking the municipal budget, the IDP and resources. Councillors will be able to assign resources in line with strategic priorities, linking plans and budgets to long-term goals and providing a process that allows resources to be reallocated as policy objectives change.

The legislation advocates a separation of oversight, fiduciary, operational and other responsibilities of the various stakeholders in order to develop more operational accountability. Operational efficiency will be improved as managers have the authority to run their operations, subject to clear statements of policy and strategy. The act demands more accurate and timely financial reporting to better inform councils and communities of the results of implementing decisions and the progress made in meeting approved objectives. As the roles of political office bearers and officials are more clearly defined with the separation of oversight and operational responsibilities, the various stakeholders will be more accountable for the results produced.

Given the significance of the reforms, and being mindful of each municipality's capacity to implement them, certain sections of the act have been phased in. Some key sections took effect immediately after 1 July 2004 because of the importance of the provisions and their underlying principles for good financial management practices. Other sections have been phased in over a longer period. The key point is that all municipalities must have started to implement the act in a sequenced and prioritised manner, recognising the need to reform internal processes, practices and policies. The MFMA implementation process will be further described later in the guide.

### ***A performance-based management culture***

The MFMA and other related national legislation aim to help municipalities establish a new performance-based management culture. Modernising municipal finance management will mean that municipalities will perform better, and have better measurable outcomes, well crafted, credible budgets, reformed practices, improved disclosure and reporting, and more sustainable service delivery. (The term 'sustainable services' is very important for councillors).

When passing a budget, municipalities must have realistic revenue expectations to ensure that outcomes can be achieved. Unrealistic revenue projections have often undermined the ability of municipalities to deliver effective services. The various sources of revenue available to municipalities - grants or transfers from national and provincial government, special purpose conditions, equitable share, property rates, user charges and so on - must be optimised and used effectively for the betterment of communities. Avoiding a deficit budget is necessary for improving service delivery. The MFMA only permits long-term borrowing to fund capital expenditure on property, plant and equipment, including infrastructure expansion. Councillors should note that borrowing cannot be used to fund operating shortfalls. The municipal budget and treasury office will be able to assist council with realistic revenue projection forecasts based on past performance.

Therefore in terms of the MFMA, budgets must accommodate all the operational and maintenance costs that the municipality anticipates. Budgets will operate as control mechanisms, and as such, expenditures that are made that were not contemplated in the budget will be unauthorised, unless council specifically authorises them in an adjustments budget. The application of the MFMA will be a powerful tool for the executive mayor or committee, municipal manager and senior managers to achieve stable finances each year. But financial stability will materialise only if councillors and officials genuinely commit to transforming and making a fundamental break from past practices. The resulting outcome will be not only municipalities with financial stability, but also a more performance-driven approach to service delivery.

### **How will national legislation lead to a more strategic approach to municipal budgeting?**

The reforms of the MSA could only be properly implemented with reformed budgeting practices. So after 2000, municipalities were required to adopt long-term IDPs. But these were often based on unrealistically high revenue projections and not linked to budgetary resources. This meant that municipalities were unable to implement their IDPs, since they were not prioritised into yearly measurable outputs.

The MFMA addresses these deficiencies by requiring a more strategic medium-term approach to budgeting. This will require all municipal councils to adopt new approaches to budget preparation, monitoring and implementation. These approaches must be considered in conjunction with the provisions of the MSA and the Property Rates Act, as the budget and the IDP must be aligned every year, which means that the IDP has to be revised. Also, all budget-related policies, such as resolutions setting taxes, tariffs for services, and other revenues, must be reviewed and approved with the budget.

By approving three-year budgets linked to longer-term IDPs, municipalities can adopt more forward-looking and better-informed approaches and make better judgements about future priorities for capital development and service delivery in their communities.

As with the national and provincial governments, municipalities will now be required to table medium-term budgets, by vote or function, such as electricity and water, subdivided into programmes. Municipalities will manage their finances across a three-year timeframe, through a continuous cycle of forecasting, implementation and review. This approach will promote a performance management culture. Together with the SDBIP, which must include measurable performance objectives, when implemented, these important reforms will contribute to a growing culture of accountability and performance-driven service delivery. By taking a more strategic approach to budgeting and financial management, councillors will now be able to consider the impact of their decisions into the longer term. The SDBIP will be used as a tool to measure the performance of senior managers, since specific ward level deliverables should also be captured into managers' SDBIPs. This will also make it easier for effective ward-based performance measures to be introduced sooner.

### **How does the MFMA make it easier to detect financial problems sooner?**

The MFMA requires more regular and accurate financial reporting to councils to create an environment in which potential or real financial problems are detected as quickly as possible. Timely reporting informs council and allows it to remedy problematic situations.

### ***Frequent and regular reporting***

The municipal manager must submit monthly and quarterly budget progress reports to the mayor. These reports are to include information relating to financial and non-financial performance. The mayor must table the quarterly reports in council and provide copies to the provincial treasury and National Treasury. The municipal manager must also submit a mid-year budget report and performance assessment to the mayor, the provincial treasury and National Treasury by 31 January each year. The mayor tables these reports in council and, if necessary, makes recommendations for an adjustment budget. Each of these reports must follow prescribed formats and set out actual against budget as well as the projection for the remainder of the year.

While the council will generally see quarterly reports, circumstances may necessitate more frequent reporting. Councillors must have or develop the ability to review and comprehend the in-year reports and be alert to trends that, if left unchecked, will lead to deteriorating financial stability that will manifest itself in reduced service delivery.

Councillors must be able to ascertain that the implementation of the budget and SDBIP is going according to plan (this means according to the budget approved by council and the SDBIP approved by the mayor). These reports will facilitate the preparation of performance reports even at a ward level, and also allow councillors to be informed early on impending distress if the municipality has financial problems.

### ***Early warning indicators***

Timely budget reports by a municipality to its administration, council, and provincial and national governmental agencies are very useful as an early warning of actual or impending financial distress. Such indicators must highlight whether or not the council is operating a continuous bank overdraft, creditor payments are made within 30 days, outstanding accounts are being collected, and capital expenditure is consistent with plans, among a number of other issues. A maximum of five to ten high level indicators will give council a good sense of financial and service delivery performance. If any of these indicators show negative variance, then the municipal manager must table corrective measures immediately for council consideration and approval. This may include a planned reduction in expenditures if revenue collections are less than projected.

### **What is the key to sound governance in the public sector?**

Governance principles of accountability, responsibility and separation of structures are applied in both the public and private sectors. In the public sector, governance principles aim to ensure democratic and accountable government that is open, fair and transparent. The keys to sound governance in the public sector are therefore:

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- separation between legislative and executive powers and administrative functions
- clear distinction of roles between policy making and policy implementation
- appropriate delegations of authority and responsibility for efficient and effective public administration
- adequate, cost effective systems of internal control and reporting
- clear and unambiguous accountability mechanisms
- codes of conduct for political office bearers and officials.

The Municipal Structures Act provides the legislative basis for the establishment of governance structures in municipalities in line with the above principles of sound governance.

### **What is financial governance and why is it important?**

The MFMA and the MSA are central to improving the financial governance framework within a municipality by clarifying and separating the roles of mayors, councillors and officials, and developing a system of accountability and oversight that is a part of the overall administration of municipal affairs.

The MFMA and other national government legislation aim to improve financial governance within every municipality. This means developing a comprehensive financial governance system that clarifies (and separates) the responsibilities of mayors, councillors and officials. The framework must be built around responsibilities of accountability and oversight, which are in turn possible only if there is a culture of transparency and regular reporting in that municipality.

A financial governance framework is a structure in which a municipality takes decisions, strengthens accountability and manages its affairs in relation to the collection, distribution, allocation, utilisation, control and monitoring of resources. This means establishing a comprehensive system of checks and balances that fosters sufficient oversight and accountability to ensure that government carries out its responsibilities effectively.

### ***Accountability and oversight***

Accountability and oversight are only possible when there is clear separation between the legislative (council/mayor/executive committee) powers of the municipality and the administration. Confusing or duplicating responsibility weakens accountability and oversight mechanisms, hence the need for separating responsibilities. The executive mayor or committee is responsible for providing the municipality with political leadership, proposing policy and overseeing that the municipal manager implements the policy. The council is responsible for approving policy and exercising oversight over

its mayor, and the administration is accountable to the council via the municipal manager. Officials are responsible for implementation and providing the executive mayor or committee with advice.

***The mayor and the municipal manager***

The council holds the mayor responsible for promised outcomes and the municipal manager for specific outputs. The mayor is expected to oversee that the municipal manager is indeed delivering on the mandate of council and that the agreed outputs are met. The mayor must ensure that these outputs form part of the municipal manager’s performance agreement, which must be revised at the start of the financial year to be consistent with the IDP, budget and the SDBIP. The municipal manager co-ordinates the administrative resources of the municipality to implement policies established by council. The municipal manager (the accounting officer under the MFMA) is accountable to the executive to produce agreed outputs. Both then contribute to the delivery of certain policy outcomes.

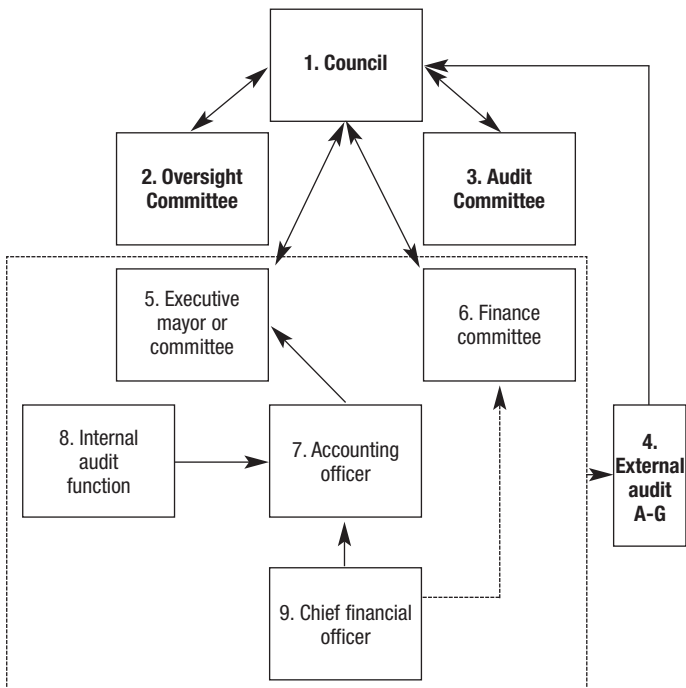
The MFMA stipulates certain procedures and assigns specific responsibilities to the council, mayor, and municipal officials (in particular the municipal manager as accounting officer). This financial governance framework is summarised in table 2 below.

<b>Table 2 - The financial governance framework</b>			
	<b>Responsible for:</b>	<b>Oversight over:</b>	<b>Accountable to:</b>
Council	Approving policy, budget and budget-related plans	Mayor	Community
Mayor	Policy, budgets, outcomes, policy and management/ oversight over municipal manager	Municipal manager	Council
Municipal manager	Outputs and implementation	Administration	Mayor; council
Chief financial officer	Outputs	Financial management	Municipal manager

**How does the organisational structure separate executive and administrative roles?**

The following diagram illustrates the separation of oversight, executive and administrative roles in a municipal organisational structure.

**Diagram 1 - Structures for financial governance**



### ***Oversight elements***

The oversight elements are numbered 1 to 4. The oversight elements include the council (1), which has overall responsibility for financial oversight. The other elements support council and include the council committees of oversight (2) and audit (3). The external audit element (4) reviews the executive and administrative elements and reports to council. The relevant processes and summary of oversight functions performed are discussed later in the guide.

### ***Executive and administrative elements***

The executive and administrative elements are numbered 5 to 9 inside the dotted frame and are made up of the political executive and administrative management. The role of the executive mayor or executive committee (5) and the finance committee of council (6) have powers and responsibilities delegated by council or specifically provided in the MFMA. These represent the executive functions as they relate to the financial governance of a municipality.

The administrative elements include the municipal manager (the accounting officer under the MFMA) (7), who is supported by an internal audit function (8), and the chief financial officer (9), who has responsibilities delegated by the accounting officer. The chief financial officer may also support the finance committee directly. The chief financial officer and the internal audit unit are accountable to the accounting officer, who in turn is accountable to the executive.

The two external and independent bodies shown in diagram 1 - the audit committee and the Auditor-General - play key roles in ensuring sound governance and accountability. These two bodies give the council independent and impartial advice on the state of financial affairs within the municipality.

### **Summary - Councillors' role in modernising municipal finance management**

The MFMA recognises that municipalities must modernise financial management systems, processes and policies to help strengthen their ability to function more effectively. Municipalities will thus have better performance, measurable outcomes, reformed accounting practices, improved disclosure and reporting, and more sustainable service delivery.

This will be possible only if councillors take their oversight roles seriously. Councillors need to ensure that municipalities will have stable finances year after year. Councillors set policies, directions, and budgets for the municipality. This gives the municipal manager and officials the direction and the authority for implementing council's policy. The municipal council and individual councillors may not interfere with matters of

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administration, but focus on a performance-driven approach to service delivery. With greater responsibilities for overseeing municipal financial management, councillors will be more accountable to their communities for the outcome of a municipality's financial and non-financial performance. Operational efficiency should improve as managers are given the authority to run their operations, subject to clear statements of policy and strategy.

As a part of finance management reform, the MFMA addresses past deficiencies of municipal budget preparation, implementation and monitoring. Councils must now table three-year budgets linked to longer-term IDPs. This approach allows the municipalities more forward-looking and better-informed approaches to planning and implementation, thus ensuring appropriate financial management practices. Councillors will be able to make more informed decisions about the future priorities for capital development and service delivery in their communities.

Councillors must set out policies that require realistic revenue projections and enable officials to collect the amounts due to the municipality. Cash flow will depend on the ability of the municipality to collect the revenue billed for property rates and service charges. Regular reports will be tabled in council to ensure that councillors are appropriately informed about revenue collections, problems relating to overly optimistic revenue projections and/or under-collection will be detected early. If these problems are not immediately resolved, councillors should expect an adjustments budget to be tabled for them to consider and adopt. Councillors will normally be required to reduce expenditures in order to prevent a budget deficit.

Councillors monitor promised outcomes and specific outputs through the mayor, who has the responsibility of overseeing the municipal manager. In order to perform their oversight role, councillors must receive timely financial reports. Councillors should read and understand the contents of these reports. The MFMA requires the municipal manager to report to the mayor monthly on the state of the budget and on any material variation from the SDBIP. The mayor then reports quarterly to the council on the progress in implementing the budget and SDBIP. A mid-year budget review must also be presented to council highlighting any need for an adjustments budget. Each of these reports must follow prescribed formats and set out actual against budget as well as the projection for the remainder of the year. Copies of these reports are to be submitted to the provincial treasury and National Treasury, which administer the implementation of the MFMA.

While the council will generally see quarterly reports, circumstances may necessitate more frequent reporting. To fulfil the oversight role, councillors should try to understand these reports and check that the implementation of the budget and SDBIP is going

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according to plan (according to the budget approved by council and the SDBIP approved by the mayor). These reports will facilitate the preparation, and performance reports even at a ward level, also allow councillors to be informed early about possible impending distress if the municipality has financial problems.

## **PART FOUR**

### **The process of financial management reform**

#### **How will the MFMA be implemented?**

All municipalities were surveyed during 2003 and 2004 in relation to their financial management skills and capacity. For the purposes of implementing the MFMA, they were then classified as high, medium or low capacity municipalities. This classification was based on each municipality's ability to implement the reforms, using information collected from the municipalities themselves. Due regard was given to the development of staff and organisational capacity through participation in financial management reform programmes. Municipalities with a higher capacity are required to comply earlier than those with lower capacities. Phase-in schedules have been established for the reforms, with the earliest plans set for high capacity municipalities and longer timetables for medium and low capacity municipalities. As the MFMA is progressively implemented, the capacity levels will fall away. However, all municipalities are encouraged to implement sooner. This will show that the municipality is serious about the reforms.

The effective dates for MFMA implementation were published in the Government Gazette. The gazette announces that the MFMA takes effect on 1 July 2004, excluding a relatively small number of sections that will take effect on specified later dates. An additional Government Gazette lists certain sections of the act which have been delayed or exempted. The delays and exemptions are based on whether a municipality has been determined as having a low, medium or high capacity to implement the MFMA. The gazettes show the capacity of each municipality and then individually list which exemptions are applicable to them. Several other gazettes providing exemptions have been published and can be viewed at the National Treasury website.

#### ***The MFMA phase-in plan***

The MFMA phase-in plan allows municipalities adequate time to fully implement the reforms envisaged in the act. While some sections of the act have been delayed or exempted to later dates, most sections became effective at 1 July 2004. This is because nominal compliance with these sections will not be very difficult – the real challenge will be to implement the qualitative improvements envisaged in the act. For example, while all municipalities should be able to establish a single primary bank account very easily, it may take a municipality longer to establish systems to more regularly reconcile its accounts.

#### ***Twelve urgent implementation priorities***

The introductory guide to the MFMA outlined steps that a municipality should take

when preparing its implementation plan. These steps were formally introduced in National Treasury MFMA circular number 5 of 2004. The circular identified 12 urgent priorities and included an implementation and monitoring checklist to help officials and councillors with implementing the MFMA. The checklist for each step or priority will allow the municipality to assess it at the present time, and give the target date for accomplishing it. Once the municipal manager and other senior officials have prepared the urgent implementation priorities checklist, the mayor should endorse each step. The checklist will provide councillors with a useful tool for monitoring implementation of the MFMA. The checklist needs to be updated regularly and submitted to council and National Treasury.

### ***The MFMA implementation plan***

National Treasury MFMA circular number 7 of 2004 was provided to help municipal councils take stock of the requirements necessary to implement the act. The circular includes a template for an MFMA implementation plan, which allows the municipality to plan the necessary actions for every step of the implementation process. The implementation plan guides the municipality through these steps, determines actions required, identifies who is responsible for what, makes any necessary delegations, and establishes final target dates for completion. The implementation plan should be reviewed and updated at least on an annual basis and submitted to council and National Treasury.

Implementing the MFMA is a collective learning exercise for councillors, other political office-bearers, and municipal officials in all municipalities. Therefore, municipalities should build their own internal capacity, and do so on a sustainable basis, without incurring unnecessary costs. Municipalities have been given a reasonable period in the phase-in plan to fully comply with the MFMA, taking into account their current capacity, and the need to improve this capacity. Councillors should use the MFMA implementation plan as a key tool for reviewing and monitoring the progress of the municipality in finance management reform.

In implementing the MFMA, municipalities should also implement DoRA as part of the same process. The act contains requirements that will assist municipalities to fully comply with the MFMA and progress the reforms in different ways. The act addresses conditional and unconditional grant frameworks, its system, reporting and disclosure, and audits in the use of public funds.

### ***Finding additional information to help councillors and officials implement the MFMA***

The table in Annexure 1 lists the publications and other information provided by National Treasury to help municipalities implement the MFMA. The list has been

updated with the latest available information at the time of publication, which can be viewed at [www.treasury.gov.za/mfma](http://www.treasury.gov.za/mfma).

### **Summary - Councillors' role in MFMA implementation**

In order for the MFMA to be implemented properly, councillors must take ownership of the implementation process. This legislation aims to significantly reform municipal finance management to ensure the improved and sustainable delivery of municipal services.

The MFMA will be implemented according to a phase-in plan based on the capacity of a municipality. Municipalities with a higher capacity are required to comply earlier than those with lower capacities. While the dates in the phase-in plan are intended as mandatory, municipalities that have the capacity are encouraged to comply with the MFMA sooner wherever possible, and to apply the spirit of the act by going beyond the prescribed finance management reforms.

The steps in the implementation plan were formally introduced in National Treasury MFMA circular number 5 of 2004. The circular identified 12 urgent priorities and included an implementation and monitoring checklist to help council implement the MFMA. The checklist for each priority will allow the municipality to assess the priority at the present time, and give the target date for accomplishing it.

National Treasury MFMA circular number 7 of 2004 provides a template for the implementation plan that allows municipalities to plan actions for every step of the process. The implementation plan will guide the municipality through the steps required by the MFMA, determine the action required, designate responsibility, make any necessary delegations, and establish a final target date for completion.

Once the 12 urgent priorities checklist and the implementation plan are prepared, they should be widely circulated across the municipality. Councillors should use the documents as tools in their oversight role to monitor the ongoing progress of the MFMA implementation. Councillors should require periodic reports on the progress of meeting the targets set out in the documents. In addition, councillors should be alert to in-year reports required by the MFMA. Reviewing and understanding these reports enables councillors to perform their oversight role. The municipal manager must be able to provide council with updates in this regard.



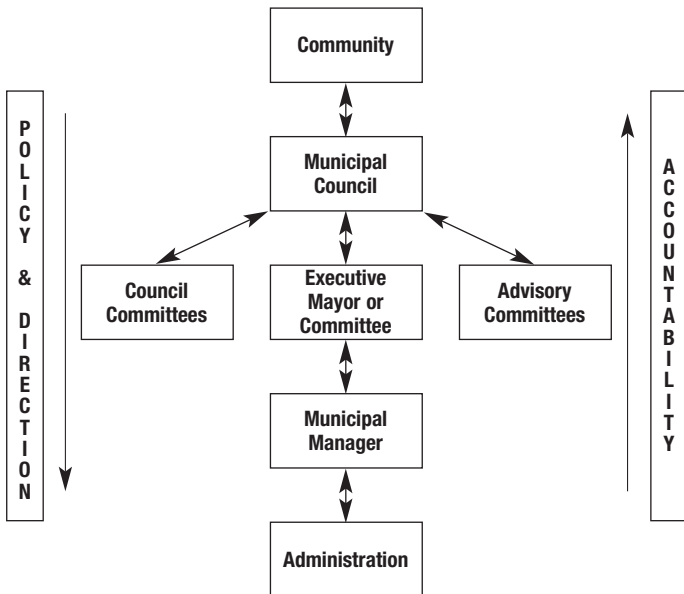
## PART FIVE Political and administrative accountability

**How does the legislation affect the roles and responsibilities of councillors and officials?**

The MFMA, together with the Municipal Structures Act and the MSA, provides clear guidance on the roles and responsibilities of councillors and officials.

Diagram 2 illustrates certain aspects of the political and administrative structures required for accountability.

**Diagram 2 - Political and administrative accountability**



### *Lines of authority*

In accordance with the financial governance principles that have already been covered, the MFMA clearly establishes separation of roles and responsibilities between the mayor and council, and between the mayor and the municipal manager and other senior officials.

It thus creates clearer lines of authority between the council, which must approve council policy; the mayor, who must provide political leadership; and the municipal manager, who is accountable to the mayor and council for implementing those policies. The following discussion will illustrate this as well as highlight how delegating authority, consistent with the provisions of the MFMA, can work to make sure that the municipality operates efficiently. It will also be stressed that the delegation of a certain duty does not divest the person delegating the duty from taking ultimate responsibility and maintaining accountability in relation to that duty.

### **How has national legislation expanded the role of the non-executive councillor?**

Apart from the speaker, non-executive councillors generally function in a part-time capacity and are expected to play a political role of representing residents and other stakeholders in the municipality. Councillors have important policy setting and oversight roles, expressed in both the MFMA and the MSA. These relate in particular to budgets, IDPs, budget-related policies, tariff setting for services, indigent policies, credit control and long-term borrowing policies. Councillors also set the parameters to guide municipal services, strategic objectives and priorities, and the outcomes and outputs that are to be achieved. They also monitor the implementation of the policies and priorities.

Both the MSA and the MFMA strengthen councillors' oversight role through council (or committee) meetings. But their oversight role means that they cannot play an operational role, as this would interfere with the role of the executive (mayor or committee) and municipal manager and weaken the accountability of officials of the council. It is important for councillors to understand that they cannot be both player and referee. This is in line with the role of elected representatives in Parliament and the provincial legislatures, who do not become involved in the day-to-day activities of the executive.

As this oversight role is so important, both the MSA and the MFMA protect the councillors' policy making role by very clearly separating it from the municipal officials' implementation or operational role. Councillors are therefore not allowed to be members of the boards of entities, and neither can they be members of a tender or bid committee. Government will also amend other planning legislation appropriately to ensure that councillors do not serve on planning and other approval forums, as this falls within the area of implementation. The MFMA also anticipates that each municipal

council will strengthen its oversight role by forming portfolio committees within the council, like the parliamentary portfolio committees in Parliament. The Municipal Structures Act can be used for this as it allows a council to form a budget and finance committee, an oversight committee, a municipal services committee (to cover water, electricity and refuse removal), and others.

To fulfil their policy setting and oversight functions under the MFMA, councillors are expected to oversee a number of financial management tasks. These include:

### ***Setting the direction for municipal activities***

- consider views of the community and other stakeholders in the planning of services, budgeting and reviewing performance
- make sure that the budget allocates resources consistent with the council's policy objectives and the priorities and needs of the community
- consider the views of the community and government before revising the IDP, adopt the budget or adjustments budget, establish a municipal entity and authorises service delivery contracts.

### ***Setting policies that impact on***

- capital programmes and contracts with financial implications of more than three budget years
- incurring debt and security over debt
- the sale, disposal or transfer of all capital assets
- cost to the municipality of salaries, allowances and benefits of political office bearers, councillors, municipal manager, and senior officials
- building capacity within the council and to train finance officials and other officials with financial responsibilities.

### ***Setting strategic objectives and priorities***

- adopt the annual budget and any amendments to the IDP, and ensure the alignment of the budget and the IDP
- make sure that the budget is realistic and financially sound before it is adopted and/or adjusted
- reconsider the budget or an amended version of the budget within seven days of the council meeting that failed to adopt the budget; and repeat the process until a budget is adopted
- adopt resolutions together with the budget as may be necessary to impose any municipal tax; set municipal tariffs; approve measurable performance objectives for revenue and expenditure; adopt any changes to the IDP; and approve any changes to other budget-related policies, such as indigent policies, credit control and supply chain management

## PART FIVE: Political and administrative accountability

- consider measurable performance objectives for revenue from every source, and for every vote in the budget.

### ***Monitoring the implementation of policies and priorities***

- consider each quarterly report on the implementation and/or performance of the budget and related service delivery and the financial state of affairs of the municipality
- review the budget and performance of entities under council control
- consider the annual report of the municipality and of any municipal entity under the municipality's sole or shared control; adopt an oversight report containing the council's comments on the annual report, which must either approve the annual report with or without reservations; accept or reject the annual report; or refer the annual report for revision of those components that can be revised.

### ***Other matters***

- through the municipal manager, investigate or review any instances of unauthorised, irregular and unforeseen expenditure, and allegations of financial misconduct and take appropriate action where necessary
- empower ward councillors with ward-specific information on implementation commencement and progress of projects, revenue collection levels, and service delivery performance.

By focusing on these critical responsibilities, councillors will be able to provide appropriate political leadership and direction to the municipality's operations, oversee the preparation of budgets and oversee the achievement of financial and non-financial objectives expressed in the budget and IDP.

### **What are the principal responsibilities of the executive mayor or committee?**

As the political head of the municipality, the mayor provides political guidance in the fiscal and financial affairs of the municipality. This includes consultation, setting the strategic framework and policy, and overseeing the proper co-ordination of the budget process. The mayor must ensure that the municipality complies with its obligations under national legislation. While he or she is not involved in the day-to-day administration of the municipality, the mayor monitors and oversees the municipal manager and senior managers as they prepare and implement budgets and do the financial reporting. The mayor must make sure that the officials are carrying out their duties properly. The main tools for doing this are the SDBIP and performance agreements, with clear measurable outputs followed by monthly budget statements, and quarterly and mid-year performance reviews.

The mayor is accountable to council for proposing and implementing policy and overseeing the implementation of this policy by the administration.

Responsibilities of the executive mayor or committee include:

### ***General responsibilities***

- provides political guidance over the fiscal and financial affairs of the municipality
- oversees the exercising of responsibilities by the accounting officer and chief finance officer, as they have been assigned by the MFMA, but not interfering with the exercising of these responsibilities
- makes sure that the municipality performs its constitutional and statutory functions within the limits of the approved budget
- exercises other powers and duties that may be assigned by the MFMA or delegated by the council.

### ***Budget preparation process***

- tables in council by 31 August, a schedule outlining the key steps and deadlines for -
  - the preparation, tabling and approval of the annual budget
  - the annual review of the IDP and budget related policies
  - the tabling and adoption of any amendments to the IDP
  - any consultative processes required for the above steps.
- co-ordinates the process for the preparation of the annual budget with the municipal manager, and tables a proposed operational and capital budget
- reviews IDP and budget-related policies and ensures consistency with the budget, taking into account realistic revenue and expenditure projections for future years
- makes sure that the municipality takes into account the national budget, the relevant provincial budget, the national government's fiscal and macro-economic policy, DoRA and any agreements reached in the Budget Forum; and complies with the legislative deadlines for the tabling and approval of the budget
- consults any national, provincial and municipal organs of state (including relevant sectoral departments) on the budget process as may be prescribed, such as National Treasury, the provincial treasury, the district municipality and all local municipalities within the area
- approves the SDBIP within 28 days after the approval of the budget, and approves the performance agreements of the municipal manager and senior management
- makes sure that the annual budget, the SDBIP, and the performance agreements are made public no later than 14 days after approval of the SDBIP, and ensures processes are in place to improve budgetary control and to help in the early identification of financial problems

## PART FIVE: Political and administrative accountability

- monitors the financial performance of the municipality in terms of the SDBIP through monthly financial reports submitted by the municipal manager
- provides council with quarterly budget reports and proposes an adjustments budget and revisions of the SDBIP when necessary
- reports instances of potential or real non-compliance with the budget process, any part of the MFMA, or in relation to any emerging or impending financial problems that may necessitate provincial intervention
- promptly responds to and initiates remedial or corrective steps proposed by the municipal manager to deal with financial problems, which may include steps to reduce spending when revenue is less than projected, and tabling an adjustments budget
- makes sure that any revisions of the annual budget and SDBIP are made public promptly
- tables in council an annual report of the municipality and any municipal entity under the municipality's sole or shared control within seven months after the end of the financial year.

### ***Exercising rights and powers over municipal entities***

- guides the municipality in exercising its rights and powers over the municipal entity in a way that ensures that the municipal entity has complied with the MFMA and has been accountable to the municipality
- monitors the operational functions of the entity, but does not interfere in the performance of those functions.

### **Why is the municipal council required to establish a system of delegations?**

The MFMA, in accordance with the MSA, relies on the management practice of establishing a system of delegations that will maximise administrative and operational efficiency. The system of delegations should be in writing and provide accountability through performance measures with adequate checks and balances. The municipal council's system of delegations helps it provide services in a sustainable manner within a municipality's financial and administrative capacity. Delegations to foster effectiveness and efficiency are mostly related to financial administration, management, and procuring goods and services.

The MFMA and the MSA set out a specific framework for the system of delegation by a municipal council, in which delegations:

- must not conflict with the Constitution, the MFMA, the MSA or the Municipal Structures Act
- must be in writing

## PART FIVE: Political and administrative accountability

- may be subject to any limitations, conditions and directions that may be imposed by the municipal council, the municipal manager or other delegating authority
- may include the power to sub-delegate a delegated power (which allows the person who has been delegated a task to again delegate that task to another person)
- must not take away the responsibility concerning the performance of the duty from the council or other delegating authority
- must be periodically reviewed in terms of specified performance measures.

The MFMA and the MSA also set out exclusions of powers, which list what responsibilities may not be delegated by a municipal council. These include:

- a power mentioned in section 160(2) of the Constitution and the power to set tariffs
- a power to enter into a service delivery agreement in terms of the MSA, section 76(b)
- a power to approve or amend the municipality's IDP.

### **An example of the process for a delegation**

For example, the MFMA assigns many specific duties and responsibilities to the mayor and also to the accounting officer. But the number of responsibilities assigned to each is so great that it would not be possible for either person to exercise these responsibilities alone. This is why a good system of delegations allows a planned sharing of responsibilities and enables other political office bearers or staff members of the municipality to help to execute the delegated responsibilities.

The 'system of delegations' described here refers to a schedule of tasks that are allowed under legislation to be delegated to another person – this schedule is generally in the form of a register, which lists all tasks, the delegating person, the delegated person, and certain conditions applying to the delegation of that particular task. It is important that all delegations are in writing and are maintained and updated regularly, as persons are only able to exercise certain power to perform their delegated tasks under a clear and written authority.

Delegations of powers, duties and functions transfer the authority necessary to take any required action to the delegated person. It does not necessarily take away the responsibility of the delegating person to ensure the power, duty or function is carried

out. If a delegating authority delegates or sub-delegates a power or duty to a political structure, political office bearer, councillor or staff member of a municipality, they must report to the delegating authority on any decisions taken or their performance at intervals prescribed by the delegating authority. In addition, sometimes the political structure, political office bearer, councillor or staff member, to whom a delegating authority has delegated or sub-delegated a power, may have to refer specified matters back to the delegating authority for a decision. Because of the time this may take, it could defeat the original objective, which was to delegate so that a duty can be performed more efficiently and effectively.

A person whose rights have been affected by a decision taken in terms of a delegated power or duty, may appeal against the decision. The appeal authority must begin the appeal within six weeks and decide the appeal within a reasonable period. The appeal authority may confirm, vary or revoke any decision taken in consequence of a delegated power, duty or function, provided that no such variation or revocation of a decision may detract from any rights that may have accrued as a result of the decision.

Delegations and sub-delegations may be withdrawn, amended, or may lapse (if made for a specified period). If a delegation is withdrawn, amended, or lapses, this does not invalidate the consequences of a decision taken in relation to the delegation or sub-delegation. This means that the change or removal of a delegation or sub-delegation may not detract from any rights that may have accrued while the delegation was in force.

### **Can the mayor or council delegate the powers and duties assigned in terms of the MFMA?**

The MFMA prescribes that the powers and duties assigned to the mayor of a municipality, may be delegated as follows:

- In the case of a municipality which has an executive mayor, powers and duties may be delegated by the executive mayor to another member of the municipality's mayoral committee.
- In the case of a municipality which has an executive committee, powers and duties may be delegated by the council of the municipality to another member of the executive committee.
- In the case of a municipality which has designated a councillor to exercise the powers and duties assigned to a mayor, the council may delegate the mayoral powers and duties to any other councillor.

### **What are the codes of conduct for councillors and officials?**

Formal codes of conduct for councillors and officials are an important element of sound

governance and accountability principles. All political parties contesting the local government elections have some form of code of conduct that councillors must adhere to. Apart from this party-specific code, councillors are also subjected to the code of conduct in the MSA. Political office bearers are elected to represent communities on municipal councils, to ensure that municipalities have structured mechanisms of accountability, to meet the community's priority needs and to operate in a transparent manner. In fulfilling this role, councillors must be accountable to the local communities and report back to constituencies on council matters, including the performance of the municipality.

Apart from the codes of conduct for councillors and officials required under the MSA, accountability and good governance are further reinforced through the code of conduct in the MFMA regulations issued in terms of supply chain management, which contain additional principles for ethical behaviour specifically relating to procurement and supply of goods and services. These codes primarily aim to ensure transparency in decision-making and ethical behaviour. They also aim to remove any conflicts of interest and behaviour leading to personal gain, and ensure fairness in decision making, for example in the allocation of resources or setting priorities in the budget process.

### ***Disclosure requirements***

Apart from the consequences outlined in the legislation for breaches of the code, if conflicts of interest are not disclosed by the council or committees, legal action may be taken against the councillor and municipality. There are other disclosure requirements contained in annual financial statements and annual reporting standards that further support the accountability principles in the MFMA.

### ***Fighting corruption***

The Minister of Finance reinforced the message from the President's State of the Nation Address, about the necessary tools and procedures government is to apply to fight corruption and waste. Besides the supply chain management reforms that include rules to prohibit illegitimate business activity of public employees and elected office bearers, improved tender practices, transparency, prompt payment and performance management will be monitored more closely.

The role of the speaker in rooting out and reporting corrupt practices by public office bearers, and the role of the municipal manager to do the same in relation to employees of municipalities, is key to success here.

Although the risks of misconduct or unethical behaviour are lower during budget preparation and greater during budget implementation, such as when implementing contracts, disposal of assets and bidding processes for supply chain management, the

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code of conduct must be applied during all steps of the budget and financial management processes.

The IDP and budget processes involve many choices in allocating municipal resources. Decisions made in relation to budget allocations provide benefits to the community according to municipal priorities. This means that some sections of the community may stand to benefit more than other sections, in particular periods. While it is the role of councillors to strongly represent their constituencies, it is important that decisions are not biased to favour particular interests or individuals, particularly where councillors may have personal interests.

Councillors must withdraw from the decision proceedings. The processes for ensuring ethical decision-making are facilitated by the requirements for declarations of interest. A register of interests that is kept up to date ensures that all interests are disclosed before any council or committee proceedings are likely to be undertaken.

Schedule 1 of the MSA sets out the provisions for the code of conduct for councillors in relation to the financial and budget processes. A councillor must:

- perform functions of office in good faith, honestly and in a transparent manner
- at all times act in the best interests of the municipality
- participate fully in meetings of the municipal council
- disclose within 60 days of election, financial interests held by the councillor and periodically thereafter
- disclose immediately any direct or indirect personal or private business interest in any matter that may come before the council
- refrain from using the position or privileges of councillor, or information gained as a councillor for any personal gain or to improperly benefit any other person
- refrain from requesting, soliciting, or accepting any rewards, gifts, or favours arising out of the role of councillor
- refrain from improperly disclosing privileged or confidential information obtained out of the role of councillor
- refrain from intervening, interfering, or obstructing management or the implementation of any decision of council or direct or give any instruction to any employee of the municipality except when authorised to do so
- refrain from using, taking, acquiring or benefiting from any property or asset owned, controlled, or managed by the municipality.

Municipal employees are bound by similar code of conduct requirements to councillors. The code of conduct for municipal staff members is set out in schedule 2 of the MSA.

Councillors are specifically prohibited from participating in the supply chain management function. This means that they cannot be involved in selecting tenders, quotations, or

purchasing or disposing of any goods or services. Nor can a councillor, or any business that they work for or control, do business with any municipality or municipal entity. Part 10 of this guide contains more detail on supply chain management issues.

Councillors, the municipal manager and all other staff members must at all times act honestly and with reasonable care and diligence when they perform their official duties. Councillors and all staff members are also required to disclose any interest in matters which they act on in the course of their official duties.

### **What are some restrictions on the role of municipal councillors in the MFMA?**

The MFMA includes an important way of improving financial governance and accountability, which restricts the role of the executive mayor or committee and non-executive councillors. The MFMA restricts the role of councillors in the procurement process to strictly oversight by barring councillors from serving on the municipal tender committee or any other committee evaluating or approving tenders, quotations, contracts or other bids. This restriction tries to remove the real or even perceived possibility of councillors being involved in a conflict of interest in the procurement process. The MFMA also prohibits any person from interfering with the supply chain management system of a municipality or municipal entity and any unauthorised amending, or tampering, with any tender, quotation, contract or bid after they have been submitted by the vendor. This is why the MFMA restricts councillors from attending any meetings, even as an observer, where tenders, quotations, contracts or other bids are being evaluated or approved.

The perception of bias or unethical discriminatory decision-making is just as damaging to the municipal council and councillors as actual misconduct.

Two other provisions of the MFMA help to prevent the appearance of bias or unethical discriminatory actions by municipalities.

#### ***Unsolicited bids***

A municipality or municipal entity is not obliged to consider an unsolicited bid received outside its normal bidding process. If a municipality or municipal entity decides to consider an unsolicited bid received outside a normal bidding process, it may do so only in accordance with a prescribed framework. The framework must strictly regulate and limit the power of the municipality and municipal entity to approve unsolicited bids received outside the normal tendering or other bidding processes.

#### ***Approving a tender that has not been recommended***

The MFMA prescribes how a tender that has not been recommended in the normal

course of the supply chain management policy may be approved. If such a tender is approved, the accounting officer of the municipality or municipal entity must notify the Auditor-General in writing, the relevant provincial treasury and National Treasury and, in the case of a municipal entity, also the parent municipality, of the reasons for deviating from the recommendation. This provision highlights actions that do not follow the established policy.

Severe penalties have been prescribed for breaches of supply chain provisions. Breaches will be investigated and measures imposed to rectify the situation, and this may include instituting criminal proceedings against individuals.

### **What are the principal responsibilities of the municipal manager (the accounting officer)?**

The municipal manager is responsible for the financial management of the municipality, ultimately ensuring that all financial systems are in place and are properly maintained.

The municipal manager is the chief administrative official of the municipality. As the accounting officer in terms of the MFMA, the municipal manager is responsible to the mayor and council for the successful implementation of council policies and objectives. In this capacity, the municipal manager must generally take on all of the responsibilities assigned to the accounting officer under the MFMA. The accounting officer must also be fully informed about the financial management reforms required in the MFMA and other legislation to provide the mayor, councillors, senior officials and municipal entities with the appropriate guidance and advice on financial management and budget issues.

As the accounting officer, the municipal manager is required to take on specific financial management responsibilities, which include, but are not limited to, the following:

#### ***Fiduciary responsibilities of the accounting officer***

- acts with honesty and integrity and in the best interests of the municipality in managing the municipality's financial affairs
- provides full disclosure to the council and the mayor of all material facts, and which in any way might influence the decisions or actions of the council or the mayor
- attempts as far as possible to prevent any prejudice to the financial interests of the municipality
- acts at all times in a manner that is consistent with the duties assigned to the position of accounting officer in terms of the MFMA
- does not use the position or privileges of the position, or confidential information obtained as accounting officer for personal gain or to improperly benefit another person.

### ***General financial management functions***

The accounting officer of a municipality is responsible for managing the financial administration of the municipality, so must try and ensure that:

- resources of the municipality are used effectively, efficiently and economically
- full and proper financial records of the municipality are kept
- the municipality has and implements an appropriate -
  - tariff policy
  - rates policy
  - credit control and debt collection policy
  - supply chain management policy
- the municipality has and maintains effective, efficient and transparent systems of -
  - financial management
  - risk management
  - internal control
- unauthorised, irregular or fruitless and wasteful expenditure and other losses are prevented
- disciplinary or, when appropriate, criminal proceedings are instituted against any official of the municipality who has allegedly committed an act of financial misconduct or an offence.

### ***Asset and liability management***

The accounting officer of a municipality must take all reasonable steps to ensure that the municipality has and maintains:

- all bank accounts of the municipality
- the assets and liabilities of the municipality, including systems to safeguard, maintain, value and account for those assets and liabilities (specifically to maintain an assets and liabilities register).

### ***Revenue management***

The accounting officer of a municipality is responsible for the management of the revenue of the municipality and must take all reasonable steps to ensure that:

- the municipality has effective revenue collection systems consistent with legislation
- revenue due to the municipality is calculated on a monthly basis
- accounts for levies and charges for municipal services are prepared at least on a monthly basis
- all money received is promptly deposited into the municipality's primary bank account
- a management, accounting and information system is maintained, which recognises revenue when earned, accounts for debtors and accounts for receipts

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- a system of internal control in respect of debtors and revenue is maintained
- the municipality charges interest on arrears (except where the council has granted exemptions)
- all revenue received by the municipality, including revenue received by any collecting agent on its behalf, is reconciled at least on a weekly basis.

In managing the municipal revenue system, the accounting officer must immediately inform National Treasury of any payments due by an organ of state to the municipality for municipal tax or for municipal services, if such payments are regularly in arrears for more than 30 days. The accounting officer must also ensure that funds collected by the municipality on behalf of another organ of state are transferred to that organ of state at least on a weekly basis; and that such funds are not used for municipal purposes.

### ***Expenditure management***

The accounting officer of a municipality is responsible for the management of the expenditure of the municipality and must take all reasonable steps to ensure that:

- the municipality has and maintains an effective system of expenditure control, including procedures for the approval, authorisation, withdrawal and payment of funds
- a management, accounting and information system is maintained which recognises expenditure when it is incurred, accounts for creditors of the municipality and accounts for all payments made by the municipality
- a system of internal control in respect of creditors and payments is maintained
- payments by the municipality are made directly to the person to whom due (unless agreed otherwise) and either electronically or by non-transferable cheques
- approved invoices or statements are paid within 30 days of receipt
- the municipality complies with its tax, levy, duty, pension, medical aid, audit fees and other statutory commitments
- any dispute concerning payments due by the municipality to another organ of state is disposed of in terms of legislation regulating disputes between organs of state
- available working capital is managed effectively and economically in terms of the prescribed cash management and investment framework
- the supply chain management policy is implemented in a way that is fair, equitable, transparent, competitive and cost effective
- all financial accounts of the municipality are closed at the end of each month and reconciled with its records.

### ***Expenditure on staff benefits***

The accounting officer of a municipality must report to the council on all expenditure

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incurred by the municipality on staff salaries, wages, allowances and benefits, and in a manner that discloses the expenditure by type:

- salaries and wages
- contributions for pensions and medical aid
- travel, motor car, accommodation, subsistence and other allowances
- housing benefits and allowances
- overtime payments
- loans and advances
- any other type of benefit or allowance related to staff.

### ***Budget preparation***

The accounting officer of a municipality must:

- assist the mayor in performing the budgetary functions assigned to the mayor and
- provide the mayor with the administrative support, resources and information necessary for the performance of those functions.

### ***Budget implementation***

The accounting officer of a municipality is responsible for implementing the municipality's approved budget, including taking all reasonable steps to ensure that:

- spending of funds is in accordance with the budget and is reduced as necessary when revenue is anticipated to be less than projected in the budget or in the SDBIP
- revenue and expenditure are properly monitored
- an adjustments budget is prepared and submitted to the mayor for consideration and tabling in the municipal council
- no later than 14 days after approval of the annual budget, a SDBIP together with drafts of the annual performance agreements for senior managers are submitted to the mayor for approval.

### ***Impending shortfalls, overspending and overdrafts***

The accounting officer of a municipality must report in writing to the municipal council of any impending shortfall in budgeted revenue or overspending of the municipality's budget; and steps taken to prevent or rectify such shortfalls or overspending.

If a municipality's bank account, or the consolidated balance of more than one bank account shows a net overdrawn position for a period exceeding a prescribed period, the accounting officer must notify National Treasury of the amount by which the account or accounts are overdrawn, the reasons for the overdrawn account or accounts; and the steps taken or to be taken to correct the matter.

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When determining the net overdrawn position, the accounting officer must exclude any amounts reserved or pledged for any specific purpose or encumbered in any other way.

### ***Reporting and publishing role***

- Reporting unauthorised, irregular or fruitless and wasteful expenditure
- Reporting impending shortfalls or overspending, and any overdraft position
- Reporting on monthly and mid-year budget progress
- Reporting other matters as prescribed, including staff expenditure
- Making public and inviting comment on draft contracts with a term greater than three years
- Ensuring information is supplied to council and the public on borrowing proposals
- Making public any proposal to establish or participate in a municipal entity
- Preparing the annual financial statements for audit, verifying salaries and benefits paid
- Making public the annual report and the council's oversight report
- Monitoring entities to ensure that their reporting obligations are met.

### **What are the principal responsibilities of the chief financial officer?**

The chief financial officer of a municipality has been assigned the following responsibilities in terms of the MFMA, and is required to:

- administer the budget and treasury office
- provide advice to the accounting officer on the exercise of powers and duties assigned to the accounting officer
- assist the accounting officer in the administration of the municipality's bank accounts and in the preparation and implementation of the municipality's budget
- advise senior managers and other senior officials in the exercise of assigned powers and duties in terms of the MFMA or delegated to them by the accounting officer.

In addition, the chief financial officer must perform any other duties delegated by the accounting officer. These would relate to budgeting, accounting, financial analysis and reporting, cash management, debt management, supply chain management, financial management, and other duties as may be delegated.

### **Can the municipal manager and chief financial officer delegate powers and duties?**

Councillors should be well informed about the responsibility of the municipal manager and chief financial officer in relation to the delegation of certain powers and duties.

### ***The accounting officer (municipal manager)***

The accounting officer (municipal manager) must develop an appropriate system of delegations that will both maximise administrative and operational efficiency and provide adequate checks and balances in the municipality's financial administration. The accounting officer has many responsibilities, which are very important for sound financial management of the municipality. The accounting officer must create a system of delegations to appropriately delegate many of the powers or duties assigned to an accounting officer in terms of the MFMA, to members of the municipality's top management or any other official of the municipality. The accounting officer must delegate any powers or duties reasonably necessary so that the objectives of the MFMA or other legislation are met. It should be clear that the municipal manager cannot delegate any of his or her responsibilities to any political office bearer, and can only delegate to a staff member or official who is formally employed by the municipality.

While the municipal manager may delegate many tasks to the chief financial officer or to other senior officials, this must be done carefully to ensure that all tasks are completed appropriately. The municipal manager must project manage the change management process at the highest level. As such, the municipal manager must establish appropriate objectives for senior staff, project milestones, timeframes and responsibilities that will produce effective outputs. He or she must also report regularly to the mayor and council on progress. A skilled and well-rounded senior management team, complemented by sound financial management knowledge and advice, is mandatory for good financial governance.

The accounting officer is also required to regularly review the delegations and make changes when necessary. The accounting officer may confirm, vary or revoke any decision taken as a consequence of a delegation or sub-delegation. But this cannot detract from any rights that may have accrued as a result of the decision.

### ***Chief financial officer***

The chief financial officer must regularly update senior management on finance-related policies and other relevant issues. The delegation of financial management tasks to junior officials should be carefully supervised and managed by other managers – remembering that while certain tasks may be delegated, the official who delegates the task is responsible for seeing that those tasks are completed accurately and on time.

The chief financial officer of a municipality may sub-delegate any of the duties that were delegated to him or her, (subject to limitations on the administration of bank accounts), to the following officials:

- an official in the budget and treasury office
- the holder of a specific post in that office

## PART FIVE: Political and administrative accountability

- to any other official of the municipality; or any person contracted by the municipality working in the budget and treasury office, with the concurrence of the accounting officer, and subject to certain restrictions.

If the chief financial officer sub-delegates any duties to a person employed by the municipality, the chief financial officer must be satisfied that effective systems and procedures are in place to ensure control and accountability.

As with delegations by the accounting officer, a sub-delegation must be in writing; it is subject to any limitations or conditions that the chief financial officer may impose; and it does not divest the chief financial officer of the responsibility for the delegated duty.

### **Summary - Councillors' oversight role and accountability in terms of the MFMA**

The MFMA clearly separates roles and responsibilities between the mayor (or executive committee) and council, and between the mayor and the municipal manager and other senior officials. It creates a clearer line of authority between the council, which must approve council policy; the mayor, who must provide political leadership; and the municipal manager, who is accountable to the mayor and council for implementing those policies.

Councillors provide the critical link between the municipality and the community. Councillors have important policy setting and oversight roles, particularly in relation to budgets, IDPs, budget-related policies, tariff setting for services, indigent policies, credit control policies and long-term borrowing policies. Councillors also set the parameters to guide municipal services, set strategic objectives and priorities, stating what outcomes and outputs are to be achieved, and monitor the implementation of the policies and priorities.

The oversight role of councillors through council (or committee) meetings has been expanded by the MFMA and other legislation. Councillors' oversight responsibilities mean that they cannot play an operational role, because this would interfere with the role of the municipal manager and weaken the performance accountability of officials.

It is important for councillors to understand their roles and responsibilities to ensure effective performance management by officials.

The MFMA further emphasises councillors' policy making and oversight responsibilities by prohibiting councillors from being members of the boards of entities, and tender or bid committees. The MFMA anticipates that municipal councils will strengthen their oversight role by forming portfolio committees. The Municipal Structures Act allows a

council to form a budget and finance committee, and a municipal services committee (to cover water, electricity and refuse removal).

Under the MFMA, councillors' policy setting and oversight functions include:

- setting the direction for municipal activities
- setting policy parameters to guide the municipal directives
- setting strategic objectives and priorities stating what outcomes and outputs are to be achieved
- monitoring the implementation of policies and priorities.

Councillors' critical responsibilities include providing oversight and direction to the municipality's operations, overseeing the preparation of budgets and the achievement of financial and non-financial objectives expressed in the budget and IDP.

Delegation consistent with the provisions of the act can work to ensure that the municipality operates efficiently and effectively. However, delegation does not divest ultimate responsibility and accountability concerning the delegated duty.

Councillors and municipal staff are bound by a code of conduct which sets out standards of ethical behaviour and requirements for good governance. Schedule 1 of the MSA and MFMA regulations set out the provisions for the code of conduct for councillors.



## **PART SIX**

### **Managing assets, liabilities, revenue and expenditure**

#### **What are the MFMA requirements for administering municipal bank accounts?**

The accounting officer of a municipality is responsible for the safeguarding and maintenance of a municipality's assets and liabilities, and must implement an accounting and information system that accounts for the assets and liabilities in accordance with standards of generally recognised accounting practice (GRAP). The municipality also must have and maintain a system of internal control for assets and liabilities to ensure there is no theft or loss and that the assets are not misused in any way. The accounting officer must make sure that adequate funds are requested in the budget tabled for consultation, for the maintenance of facilities and equipment.

Every municipality must designate and maintain a primary bank account for the purposes of receiving certain funds including government appropriation, income from investments and income from municipal entities. A municipality should limit the number of bank accounts to only those which are reasonably necessary for business and efficiency reasons and all accounts must be in the name of the municipality.

Only the municipal manager, as the accounting officer, or the chief financial officer, acting on written authorisation of the accounting officer, may open a bank account in the name of the municipality. In addition, a municipality may not open a bank account abroad or with an institution not registered as a bank in terms of the Banks Act (1990).

It therefore follows that no councillor may open a bank account in the name of the municipality or withdraw funds from such an account.

#### ***The primary bank account***

The primary bank account must be used to deposit all moneys and/or receipts of the municipality, including: those made to the municipality for transmission to a municipal entity or other external mechanism which helps the municipality perform its functions; all income received by the municipality on its investments; all income received by the municipality in connection with its interest in any municipal entity, including dividends; all money collected by a municipal entity or other external mechanism on behalf of the municipality; and any other moneys.

The MFMA requires all organs of state in the national, provincial or local sphere of government to transfer any allocation of money to a municipality to the municipality's primary bank account. All allocations due by an organ of state to a municipal entity must be made through a parent municipality's primary bank account.

## **PART SIX: Managing assets, liabilities, revenue and expenditure**

All money received by a municipality must be promptly deposited in its primary bank account. The municipal council should establish a minimum time allowed for processing before funds are deposited in its bank account. There are two important reasons for establishing and monitoring the requirement for prompt deposit of receipts: First, cash collections are the most liquid asset of a municipality and internal control is strengthened when moneys are placed in official depositories; and second, it is important to invest idle cash as soon as possible.

### **What are the MFMA requirements for withdrawals from a municipal bank account?**

The MFMA specifies that the accounting officer may not authorise any official other than the chief financial officer to withdraw money or to authorise the withdrawal of money from the municipality's primary bank account. Any authorisation by the accounting officer for withdrawals from bank accounts must be in writing. The authorised officials may withdraw or authorise the withdrawal of money from the municipality's bank accounts for any of the following official reasons:

- expenditure appropriated in terms of an approved budget
- expenditure authorised in terms of an intervention
- unforeseeable and unavoidable expenditure authorised by the mayor in terms of the MFMA
- payments of money received by the municipality on behalf of a person or organ of state
- refunds of money incorrectly paid into a bank account
- refunds of guarantees, sureties and security deposits
- cash management and investment purposes
- other purposes as may be prescribed.

The accounting officer must table in the municipal council, within 30 days after the end of a quarter, a consolidated report of all withdrawals made from bank accounts for any reason other than an expenditure appropriated in an approved budget. The accounting officer must also submit a copy of the report to the relevant provincial treasury and the Auditor-General.

### **What should councillors know about cash management and investments?**

Councillors should NOT handle any cash or cheques on behalf of the municipality. Councillors should recognise that cash and cheques must be deposited by officials of the municipality into a municipal bank account as promptly as possible.

The MFMA requires municipalities to establish an appropriate and effective cash management and investment policy in accordance with any framework that may be

prescribed by the Minister of Finance. The key principles of protecting the principal (and therefore limiting risks and speculation), and security of public funds, are extremely important when handling public resources. The Municipal Investment Regulations, 2005 which were issued in terms of the MFMA, should be referred to for more information on the development of an investment policy.

### **Sound investment policy**

Because of the importance of investment income as a revenue source, the investment policy should encourage municipal operations to be designed to maximise cash flow. Maximising cash flow requires managers to schedule the timing of key expenditures and revenues. The accounting officer must make all senior managers aware of the objectives to accelerate the receipt of revenues, to promote robust revenue collections and to maximise cash flow through various methods. These objectives should be included in the cash management and investment policy.

The investment policy should address the following:

- how to maximise cash flow
- who has the authority to invest funds for the municipality
- appropriate investment instruments and spreading of risk
- liquidity (access to funds when needed)
- maturity (terms or length of investment)
- safety or default risk
- investment return objectives
- staff capabilities
- reporting requirements.

A municipal council must ensure that its investment policy is consistent with the investment regulations and appropriate delegations are in place for effective management of the funds available to council.

Adopting the 'prudent person' standard of investment is a useful method to help ensure sound investments. The prudent person standard requires that *'investments shall be made with judgement and care, under circumstances then prevailing, which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived'*.

This means that hedging and options are not allowed as they are speculative in nature. Investments should be made responsibly and intelligently, to ensure that they are safe and yield sound returns, and not for speculation.

## **PART SIX: Managing assets, liabilities, revenue and expenditure**

As with the MFMA restrictions on withdrawing money from bank accounts, the authority to invest should be placed specifically with the chief financial officer. The chief financial officer should be authorised to sub-delegate the authority to invest to a treasurer or an investment officer that would be acting on written authority of the chief financial officer.

Investment transactions must be undertaken in a competitive process only with reliable and reputable financial institutions. When selecting institutions for idle cash or selecting specific investment vehicles, for example, a competitive process is advised. The investment policy should also require those persons authorised to make investments to carefully evaluate the creditworthiness of depositories and credit issuers.

The investment policy should provide a framework for the safe investment of public funds. The primary goal is to obtain a market return on the investment while preserving capital at the lowest possible risk. Higher returns should only be acceptable when the risk-reward decision indicates that the investment can be made with a high degree of safety. Another important feature of investment safety is liquidity. Liquidity refers to the ability to have the capital returned when it is needed without penalty. Investment timing must therefore be linked with the municipality's cash flow needs.

### **What are the MFMA requirements for the disposal of capital assets?**

A municipality may not transfer ownership or otherwise permanently dispose of an asset that is needed to provide the minimum level of basic municipal services. The municipal council may sell and transfer ownership or dispose of an asset only after, in a meeting open to the public, it has decided on reasonable grounds that the asset is not needed to provide the minimum level of basic municipal services, and has considered the fair market value of the asset and the economic and community value to be received in exchange for the asset.

The accounting officer is responsible for determining the most appropriate means for ascertaining the fair market value. This may be through in-house or independent valuers or other records held by the municipality. This is required to help the council decide whether the asset can be released for sale and what the economic and community value is likely to be if disposed of. It is not the role of the council to call bids for the sale of the asset, or in any way participate, in the supply chain process. A municipal entity must obtain this resolution from the parent municipality and not the board of directors. Once a council has determined this and the asset has been sold, transferred or otherwise disposed of, the decision and actions may not be reversed.

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A municipal council may delegate to the accounting officer of the municipality its power to make the determinations outlined above for movable assets below a value that the council sets. A movable asset includes furniture, vehicles, equipment and the like. Immovable assets are land and buildings.

Any transfer of ownership of an asset in accordance with the requirements presented above, must be fair, equitable, transparent, competitive and consistent with the supply chain management policy, which the municipality must have and maintain.

It is also important that there is proper forward planning and community consultation when considering the disposal of assets. The public benefit aspect of these assets must be properly considered before any decision is made. Unsolicited bids for these assets must be referred to the proper processes in keeping with the principles of transparency and accountability.

### **What is risk and how can it be managed?**

An unavoidable part of operating a municipality that provides services to the community is taking on risk. Municipal exposure to risk may take many forms, such as: lost or damaged property, employee injury, physical or environmental hazards, legal liabilities to others and litigation, extra expenditure (replacement of damaged equipment), and crime and fidelity losses.

The goal of risk management is to create a safe workplace, to prevent catastrophic financial losses, and to provide budgetary stability. Effective risk management eliminates or reduces the detrimental effects of risks that cannot be avoided, and protects both the municipality and its employees. A comprehensive risk management programme:

- allows for the more effective use of government funds by saving money spent on insurance, replacement of damaged property or paying claims related to liability or workers' on-the-job injuries
- increases worker productivity by preventing workplace accidents and injuries, and reduces costs related to medical payments, lost workdays and replacement workers
- reduces uncertainties associated with future projects and budgetary uncertainties by controlling risks of new governmental amenities, such as a new park, or a change in service delivery mechanisms.

### ***The framework for an effective risk management programme***

In order to have an effective risk management programme, the framework will have at least the following elements:

## PART SIX: Managing assets, liabilities, revenue and expenditure

- identifying the potential exposure to losses
- evaluating the potential for loss on the basis of the frequency and severity of an event
- dealing with risk management by using appropriate tools and techniques, such as risk control and risk financing
- implementing the programme and other financing arrangements in order to prevent unexpected demands on the budget.

### ***Municipalities are exposed to particular kinds of risks***

Municipalities face unique risks usually not found in the private sector. This is true for a number of reasons.

First, some public-sector services are inherently high risk. For example, the activities of police and fire fighters are dangerous and involve the potential for financial loss. In addition, most municipalities cannot manage risk by discontinuing a service. A critical activity like road maintenance cannot be avoided or stopped, due to claims by citizens for damages, for example, if pot-holes are not fixed.

Second, the scope of the public sector is enormous. Even a small municipality provides, either directly or through its agents, a multitude of services. Geographically, the footprint of the municipality is broad as well. Through the range of spaces and areas under its jurisdiction, such as streets, pavements and parks, if it is not the largest landowner, it is certainly the largest property manager. A municipality cannot constantly monitor all activities in the public domain.

Third, if not well managed, a government typically can lose control over its physical environment. During normal business hours, a municipality does not restrict citizen access to most government buildings or facilities: municipal departments such as motor vehicle registration and licensing offices, pay-point facilities and community centres must be accessible to the public. Moreover, public spaces such as parks, streets and pavements are open 24 hours a day, seven days a week.

### ***How municipalities can manage risks***

A municipality can handle risk management in several ways:

- by purchasing insurance
- loss prevention and risk control measures
- carefully administering claims
- monitoring claims performance
- promoting a sense and culture of community ownership of municipal facilities.

### What is meant by credit control and debt collection?

A significant proportion of municipal income is derived from the levying of rates and other taxes and charging fees for municipal services. Councillors, with the assistance of their chief financial officer, should annually review the municipality's overall revenue structure to determine its stability, equity, efficiency and capacity to finance municipal services into the future.

Municipal councils tend to take the municipal revenue structure for granted. Municipal revenues are often considered to be inflexible and/or inequitable. For example, excessive reliance on property taxes may limit the growth potential of municipal services, and it may simultaneously shift tax burdens to persons who receive the fewest public services.

Fees and charges for municipal services are established to promote economic efficiency by shifting costs to users and to help reduce the reliance on general taxation. Care must be taken to ensure that affordability tests are regularly conducted. Municipalities are required to provide equitable services to communities. Councils are required to also ensure that service tariffs and credit control policies are put in place that take the needs of communities into account.

### ***Open communication and feedback mechanisms are the components of a sound customer management system***

In relation to levying rates and other taxes and charging fees for municipal services, a municipality must, within its financial and administrative capacity, establish a sound customer management system that aims to create a positive and reciprocal relationship between persons liable for these payments and the municipality, or other service provider. The customer management system must allow for users of services and ratepayers to give feedback to the municipality or service provider about the quality of service and performance.

The system must ensure that users are informed of the costs of the services, reasons for the service fees and how the moneys raised will be used. The municipality or service provider must ensure that consumption of services can be reasonably determined, measured or estimated per quantity used or per frequency of use. The municipality must ensure that the methods of calculating service charges are accurate and verifiable, and that the users of the services receive regular and accurate accounts of the amounts due. Customers must have access to persons to query, verify or appeal the charges levied them and to receive prompt corrective action by the municipality when appropriate. It is the responsibility of the municipality or service provider to establish accessible methods or pay points for settling an account and/or mechanisms for making pre-payments for services.

Some municipalities operate a call centre to log all enquiries. The response times and finality of enquiries should be reported on a regular basis to council so that councillors become aware of issues that the administration faces and can institute alternative measures to address service delivery challenges. Councillors should be aware of the length of queues or the amount of time that citizens spend waiting to be serviced by officials. Again, this information will allow management and councillors to institute corrective measures to address the principles of Batho Pele. To make these measures work, councillors and officials are requested to perform unannounced visits and test these facilities out themselves.

### **What is the credit control and debt collection policy?**

The MFMA and the MSA provide that a municipality must collect all money that is due and payable. The municipal council must adopt by-laws to give effect to the credit control and debt collection policy, making sure that it is implemented and enforced. The by-law for this policy may differentiate between different categories of ratepayers, users of services, debtors, taxes, services, service standards and other matters as long as the differentiation does not amount to unfair discrimination.

The credit control and debt collection policy should be reviewed in line with the council's policy on indigents. Quite often the credit control and debt collection policy and the indigent policy are not aligned, which results in confusion when implemented by officials. The MFMA is aiming for more coherence, requiring that all related policies should be reviewed when tabling and adopting the municipal budgets. These policies must be consistent with the municipality's rates and tariff policies and provide for:

- credit control procedures and mechanisms
- debt collection procedures and mechanisms
- provision for indigent customers that is consistent with its rates and tariff policies and any national policy on indigents
- realistic collection targets consistent, and the estimates of income set in the budget
- interest on arrears, where appropriate
- extensions of time for payment of accounts
- termination of services or the restriction of the provision of services when payments are in arrears
- matters relating to unauthorised consumption of services, theft and damages, and public disclosures of information.

Another reason for making sure that there is coherence in policies for revenue raising, credit control, debt collection and indigent customers is that it will facilitate realistic

## **PART SIX: Managing assets, liabilities, revenue and expenditure**

revenue budgets. If these policies are inconsistent, the forecast revenue will not be achievable.

Implementing the policies must include effective administrative mechanisms, processes and procedures to collect money that is due and payable to the municipality. The collection procedures must include internal controls for the protection of account records, custody of monies collected and deposits into the bank account of the municipality.

The collection policy must provide an authorised representative of the municipality or service provider access at reasonable hours to the premises in order to read, inspect, install or repair any meter or service connection for reticulation, or to disconnect, stop or restrict the provision of any service. In addition, a municipality may consolidate any separate accounts of persons liable for payments to the municipality, or credit a payment by such a person against any account of that person. The collection and credit control measures provided for in the collection policy may be used for the collection of any account in arrears.

A municipality may, with the consent of a person liable to the municipality for the payment of rates or other taxes, or fees for municipal services, enter into an agreement with that person's employer to deduct from the salary or wages of that person either outstanding amounts due by that person to the municipality; or regular monthly amounts as may be agreed. In addition, the municipality may provide special incentives for employers to enter into such agreement and/or to employees to consent to such agreements.

### **What are the MFMA requirements for management of revenue?**

The accounting officer of a municipality is responsible for the management of the revenue of the municipality. The accounting officer must take all reasonable steps to ensure that:

- the municipality has effective revenue collection systems consistent with the municipality's credit control and collection policy
- revenue due to the municipality is calculated on a monthly basis
- accounts for municipal tax and charges for municipal services are prepared on a monthly basis, or less often as may be prescribed where monthly accounts are uneconomical
- all money received is promptly deposited into the municipality's primary bank account
- the municipality has and maintains a management, accounting and information system which recognises revenue, accounts for debtors, and accounts for receipts of revenue

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- the municipality has and maintains a system of internal control over debtors and revenue
- the municipality charges interest on arrears, except where the council has granted exemptions in accordance with its budget-related policies
- that all revenue received by the municipality, including revenue received by any collecting agent on its behalf, is reconciled at least on a weekly basis.

The accounting officer must immediately inform National Treasury of any payments related to municipal tax or for municipal services due by an organ of state to the municipality, if these payments are regularly in arrears for periods of more than 30 days.

The accounting officer must take all reasonable steps to ensure that any funds collected by the municipality on behalf of another organ of state are not used for purposes of the municipality and are transferred to that organ of state at least on a weekly basis.

### **What are the MFMA requirements for managing expenditure?**

The accounting officer of a municipality is responsible for managing the expenditure of the municipality. The accounting officer must take all reasonable steps to ensure that:

- the municipality has and maintains an effective system of expenditure control, including procedures for the approval, authorisation, withdrawal and payment of funds
- the municipality has and maintains a management, accounting and information system which recognises expenditure when it is incurred; accounts for creditors of the municipality; and accounts for payments made by the municipality
- the municipality has and maintains a system of internal control in relation to creditors and payments
- payments by the municipality are made directly to the person to whom they are due, and either electronically or by way of non-transferable cheques, provided that cash payments and payments by way of cash cheques may be made for exceptional reasons only, and only up to a prescribed limit
- all money that the municipality owes be paid within 30 days of receiving the relevant invoice or statement, unless prescribed otherwise for certain categories of expenditure
- the municipality complies with its tax, levy, duty, pension, medical aid, audit fees and other statutory commitments
- any dispute over payments due by the municipality to another organ of state is disposed of in terms of legislation regulating disputes between organs of state

## **PART SIX: Managing assets, liabilities, revenue and expenditure**

- the municipality's available working capital is managed effectively and economically in terms of the prescribed cash management and investment framework
- the municipality's supply chain management policy is implemented in a way that is fair, equitable, transparent, competitive and cost effective
- the municipality's financial accounts are closed at the end of each month and reconciled.

### **Summary - Councillors' oversight of assets, liabilities, revenue and expenditure**

Councillors have a number of policy setting and oversight responsibilities for the management of a municipality's assets and liabilities, and revenue and expenditure. Councillors should, by receiving reports at council meetings, be aware that the municipality has and maintains the following:

- an accounting and information system that accounts for assets and liabilities in accordance with generally recognised accounting practice
- a system of internal control for safeguarding and maintaining assets and liabilities
- adequate cash management controls and policies
- an investment policy for cash and cash reserves
- a risk management policy in order to manage risks and minimise losses and litigation
- a sound customer management system, and credit control and collection policy
- reliable revenue and expenditure management systems and procedures.

Municipalities must maintain a primary bank account. Bank accounts should be limited to only those which are reasonably necessary for business and efficiency reasons. Only the municipal manager, as the accounting officer, or the chief financial officer, acting on written authorisation of the accounting officer, may open a bank account in the name of the municipality. The main reason for withdrawals from the municipality's primary bank account is for expenditures appropriated in terms of an approved budget.

The investment of cash and cash reserves that will be used for designated purposes at a future date can be a significant source of investment income. Regarding the cash management and investment policy, councillors should encourage municipal operations to be designed to optimise cash flow, including timing of key expenditures and revenues. The cash management and investments policy should include objectives for cash flow, such as accelerating the receipt of revenues by promoting effective revenue collection.

Exposure to risk is an unavoidable part of providing services to the community. Municipal risk may lead to additional costs, such as extra expenditure to replace

## **PART SIX: Managing assets, liabilities, revenue and expenditure**

damaged equipment and/or to re-establish a service. Councillors should establish policies that seek to reduce risk by creating a safe workplace, and preventing catastrophic financial losses by transferring risk.

Municipal councils are required to ensure equitable service delivery, and that affordable service tariffs and credit control policies are put into place that take their needs into account. In addition to a customer management system, councillors must adopt a credit control and collection policy. The policy may differentiate between different categories of ratepayers, users of services, debtors, taxes, services, service standards and other matters as long as the differentiation does not amount to unfair discrimination. Councillors must ensure that the policy contains provisions for indigent customers that are consistent with the municipality's rates and tariff policies and any national policy on indigents.

Councillors must ensure that realistic collection targets are set in order to make reliable income estimates in the municipal budget.

The municipal council must monitor the implementation and enforcement of the municipality's policy and any related by-laws by receiving regular progress reports on its implementation.

### **PART SEVEN**

### **Municipal budgets and strategic planning**

All councillors have an important responsibility in relation to approving the budget. The budget is the mechanism that translates plans into action. Therefore, council plays a critical role in ensuring policy priorities are reflected in the budget. Councillors should focus on allocating budget inputs (resources) between competing priorities consistent with the strategic direction set out in the IDP. A councillor's focus should be on high level votes representing municipal priorities. Councillors have an important role in facilitating consultation with stakeholders (especially the community) and ensuring that the budget reflects, as far as is practical, the needs of the community. The community and other stakeholders will hold councillors accountable for service delivery.

#### **What is the councillor's role in the budget process?**

Council must approve credible budgets, with realistic revenue and expenditure estimates. In accomplishing this objective, councillors will consider a longer-term view that will make financial stability possible in their municipality. Council must budget for the maintenance and replacement of operating equipment to ensure sustainable service delivery. In addition, council must determine the capital budget for the medium-term, and must consider the projected future operational costs of these authorised capital projects. Long-term borrowing must be closely examined, together with contracts exceeding three years, and proposals to participate in a municipal entity. Councillors must scrutinise and monitor performance on the budget and SDBIP through quarterly performance reports tabled by the mayor.

As councillors take on greater responsibility in monitoring municipal financial management under the MFMA, they will exercise greater diligence in the financial affairs of the municipality. Councillors have an increasingly disciplined role of accounting to their communities for the municipality's service delivery and financial performance.

#### **What is the mayor's role in the budget process?**

The budget process for the next financial year begins nearly at the same time as the implementation of the budget for the current financial year. The mayor is responsible for co-ordinating the plans and timetables for the next budget year and projections for two additional years with the municipal manager and senior officials. Although these activities are initiated by the mayor, the municipal manager and senior managers must help to prepare and/or carry out each activity. The mayor is required to table the budget

## PART SEVEN: Municipal budgets and strategic planning

plans and timetables in council by the end of August. The budget activities include the following:

- The municipal manager or delegated official, in conjunction with the mayor, should review past outcomes and financial position, and consider the impacts that the actual financial performance may have on the plans and preparations for the next year's budget.
- The municipal manager or delegated official, in conjunction with the mayor, should review policies, priorities and objectives and draft any changes for the next budget year.
- The mayor must table a time schedule outlining key deadlines for the next year's budget process in council by 31 August.
- Council is to consider and approve the plans and timetables and form committees for budget review and develop a plan for public participation.
- The mayor and council must determine strategic choices for the next three budget years and consider proposed revisions to the IDP.
- Council must finalise and approve tariff polices for the next budget year.
- Council receives the proposed budget, resolutions, plans and proposed changes to the IDP, which must be tabled by the mayor by the end of March (at least 90 days before the start of the next budget year).
- The mayor and council or committees appointed by council hold public hearings on the proposed budget, plans, and changes to the IDP, and debate these proposals in council.
- Council adopts the operating and capital budget, resolutions, plans and policies, capital implementation plans, objectives for the financial year, and changes to the IDP by 30 May at the latest, although these could be adopted sooner to allow for effective implementation by 1 July.
- The mayor approves performance contracts for the municipal manager, who also approves contracts of other senior officials for the next financial year in keeping with the objectives set by council.
- Council adopts the system of delegations for the next financial year, or amends current delegations.

### ***Mayor to co-ordinate the budget preparation process***

It is important for the mayor to maintain close oversight of the budget preparation process, from the initial planning, through to implementation. The municipal budget and treasury office plays a key role in this process along with senior managers, IDP and service delivery specialists and must be balanced with the need for broad consultation with numerous stakeholders, including councillors.

While the technical preparation of the budget is undertaken by the municipal manager,

chief financial officer and senior managers, it is important that the mayor meet with the municipal manager and officials on a regular basis after the priorities are set. Such political oversight is required to guide officials and to assist in making the hard trade-offs necessary to determine the budget. In order to co-ordinate such a large process it is recommended that the mayor establish and chair a budget co-ordination steering committee. Membership of this committee would ideally comprise at least the following:

- Mayor (chairman)
- Councillor for finance
- Councillor responsible for infrastructure
- Accounting officer
- Chief financial officer
- Senior manager responsible for the IDP.

### What is an integrated development plan?

Each municipal council, within a prescribed period after the start of its elected term, must approve a single, inclusive and strategic plan for the development of the municipality. This plan is known as the IDP. As far as possible, the planning must be aligned with and complement the development plans and strategies of other affected municipalities and provincial and national spheres of government. The IDP is an all-encompassing strategic plan for the municipality. It must be directed towards developing the community in order to ensure that it:

- works towards achieving the objectives of local government as set out in the Constitution
- gives effect to its developmental duties
- together with other spheres of government contributes to the progressive realisation of the fundamental rights contained in the Constitution.

The IDP must:

- link, integrate and co-ordinate plans and proposals for the development of the municipality
- align the resources and capacity of the municipality with the plan
- be compatible with national and provincial development plans and planning requirements binding on the municipality in terms of legislation.

The MSA and MFMA require the municipal council to review its IDP at least annually. The review of the IDP should consider past financial and budgetary performance and any changing circumstances. The council is required to amend the IDP based on its annual review. Each municipality, within 14 days of adopting or amending the IDP, must give notice to the public and make copies available for public inspection.

The IDP is a statement of the municipal council's vision for the long-term development of the municipality. The IDP must emphasise the municipality's most critical development and internal transformation needs. As such, it should assess the existing level of development in the municipality and identify communities and segments of the population which do not have access to municipal services.

### **What does the municipal budget process involve?**

The mayor, as the political head of the municipality, provides political guidance of the budget preparation process through a co-ordinated cycle of events that begins nearly one year before the start of each financial year. The financial management cycle is integrated into the other two key areas of the financial reforms: budget implementation and financial reporting.

A central element of the reforms is a change to the way that municipalities prepare their budgets. The MFMA requires council to table three-year capital and operating budgets that take into account, and are linked to, the municipality's current and future development priorities (as outlined in the revised IDP) and other budget-related policies (such as those relating to free basic service provision).

The budget must clearly set out revenue by source and expenditure by vote (defined as segments that the budget is divided into for the appropriation of money for different departments or functional areas, over three years). It must be accompanied by performance objectives for revenue and for each vote, a cash flow statement and particulars on investments, municipal entities and service delivery agreements, grant allocations, and details of employment costs and performance agreements.

It is important for all councillors to become aware of DoRA and its accompanying schedules, that provide details of all national allocations to municipalities projected over a three-year period – this provides actual amounts that municipalities should include in their own three-year revenue budget forecasts for conditional and unconditional grants from the national government. Provincial gazettes should also be consulted in order to obtain provincial allocations to municipalities, which must also be projected over a three-year period.

The significant steps for planning and preparing the budget include:

#### ***Budget preparation timetable***

The first step in the budget preparation process is to develop a timetable of all key deadlines relating to budget preparation and the review of the municipality's IDP and budget-related policy. The budget preparation timetable should be prepared with input

## **PART SEVEN: Municipal budgets and strategic planning**

from senior management and should start straight after the publication of the budget. The mayor must table the budget process plan for council to adopt by 31 August, 10 months before the next budget year begins.

The timetable must contain: key deadlines for the preparation, tabling and approval of the budget; the annual review of the IDP and policies; and tabling of related amendments and consultative processes with communities, government departments and key stakeholders.

### ***Budget preparation and review of IDP and policies***

The mayor must co-ordinate the budget preparation process and the review of council's IDP and budget-related policies, with the help of the municipal manager (supported by staff employed by the municipality). The mayor must ensure that the IDP review forms an integral part of the budget process and that any changes to strategic priorities as contained in the IDP document contain realistic projections of revenue and expenditure. In developing the budget, national and provincial policy must be considered as well as national fiscal and macro-economic issues. Other relevant agreements or acts of Parliament must also be taken into account. When preparing the budget, the mayor must consult with the relevant district and all other local municipalities in that district as well as relevant provincial departments and National Treasury, and provide information as required.

This part of the budget process should ideally occur from August to November, so that IDP amendments, consolidated three-year budgets, and policies can be made available early in December. This allows time during January and February for preliminary consultation and discussion on the budget.

### ***Tabling of the budget for consultation***

The MFMA requires the mayor to table the budget before council by 31 March. Following the tabling of the budget, the months of April and May should be used to accommodate public and government comment, and any revisions if necessary. Note that this budget as tabled for consultation must be a credible budget capable of being approved as is. The budgets must be balanced. This means that expenditure must be funded from reasonable estimates of revenue and cash-backed surplus funds from previous years, and borrowings (for capital programmes only).

### ***Publication of the budget tabled for consultation***

Once tabled at council, the municipal manager must make public the appropriate budget documentation, and submit it to National Treasury and the relevant provincial treasury, and any other government departments as required. At this time, the local community must be invited to submit representations in response to the budget.

### ***Opportunity to comment on the budget tabled for consultation***

When the budget is tabled, council must invite the views of the local community, National Treasury and the relevant provincial treasury, and other municipalities and government departments that may have made submissions on the budget. This may take the form of public hearings, council debate, formal or informal delegations, or any other consultative forums designed to address stakeholder priorities. It is advised that a budget consultation session takes a week or two weeks. This could take the form of specific sessions with communities through ward committee meetings, ratepayer associations, the business community, non-governmental agencies, academics and others, depending on the circumstances of a particular municipality.

### ***Opportunity for revisions to the budget tabled for consultation***

After considering all comments and submissions, council must provide an opportunity for the mayor to respond to the submissions received, and if necessary revise the budget and table amendments for council's consideration.

### ***Approval of the budget***

By 31 May, the council must consider the approval of the budget and must approve it by 30 June. Tabling the budget for consideration of approval well in advance allows council to ensure that service delivery is commenced immediately. Municipal officials will have this short time to finalise all plans and procurement for implementing the budget effectively and efficiently. Once the budget is approved, subsequent adjustments should not be made in an ad hoc manner, but be based on a well-planned and structured process, such as once a year after the mid-year review of performance is completed. The exception to this may be if there has been a material under-collection of revenue, which will necessitate a reduction in expenditure, to ensure a balanced budget is maintained throughout the financial year.

If a council fails to approve its budget at its first meeting to consider approval, it must reconsider it as is, or as amended, within seven days, and must continue to do so until it is finally approved - before 1 July. This is non-negotiable. Failure to approve the budget before the start of the budget year has serious consequences.

Once approved, the municipal manager must place the approved budget on the municipality's website within five days. Once finalised, the mayor has a short time to approve the SDBIP and annual performance contracts of all senior managers for the new budget year.

Councils may adopt capital programmes for durations of one to three years, to improve service delivery. This will imply that funding for such programmes are also consistent with this approval.

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### ***Review and adjustment of budget***

Throughout the year, there is an ongoing monitoring role undertaken by the mayor and the council to ensure that the budget remains on track. If necessary an adjustments budget may be considered by council.

Table 3 below summarises the budget process cycle.

	<b>Step</b>	<b>Process</b>
<b>1</b>	<b>Planning</b>	Schedule key dates, establish consultation forums, review previous processes.
<b>2</b>	<b>Strategising</b>	Review IDP, set service delivery targets and objectives for next 3 years, consult on tariffs, review indigent policy, credit control, and free basic services. Consider local, provincial and national issues, the previous year's performance, and current economic and demographic trends.
<b>3</b>	<b>Preparing</b>	Prepare budget, revenue and expenditure projections; draft budget policies; consult and consider local, provincial and national priorities.
<b>4</b>	<b>Tabling</b>	Table budget, IDP, and budget-related policies before council; consult and consider formal local, provincial and national inputs or responses.
<b>5</b>	<b>Approving</b>	Council approves budget and budget-related policies, and any changes to the IDP.
<b>6</b>	<b>Finalising</b>	Approve SDBIP and publish with budget and annual performance agreements and indicators.

### **What are municipal quarters?**

The four quarters of a municipal financial year are as follows:

- 1 July to 30 September
- 1 October to 31 December
- 1 January to 31 March
- 1 April to 30 June

### What is the municipal budget year?

The municipal financial year is:

1 July to 30 June

### What is the budget or financial cycle?

The cycles for the budget process and financial management run continuously and overlap over more than one year. At any particular time in a financial year, municipalities will effectively be involved in activities dealing with three different budgets. The major activities of the three different budgets are illustrated below, using September 2006 as the current date.

#### Scenario: the budget calendar

You have just finalised the annual financial statements for the *past financial year budget* for 2005/06, which has to be submitted to the Office of Auditor-General for audit, to discharge council's most critical accountability process. You are busy implementing the current budget, for 2006/07. And you are busy preparing the *next medium term budget*, for 2007/08 to 2009/10.

*Next financial year budget activities* cover planning and preparation of next year's budget with projections for an additional two years. These activities are undertaken during a large part of the current financial year.

*Current financial year budget activities* focus on monitoring, reporting, and evaluating performance of the year's budget. This involves monthly reviews and internal management reporting, taking action on variations from plans, and major quarterly reviews. Quarterly reviews during the current year are aimed at:

- During the first quarter review, due in October and which should be concluded by early November, councillors should ensure that all budget plans are being implemented.
- During the second quarter or mid-year review, due in January and February, councillors should ensure that implementation is well under way and has been accomplished on schedule, and identify any major shifts or shortfalls that might require an adjustments budget. It is important that whenever an adjustments budget is necessary, the council deals with the problems creating the need for an adjustments budget as soon as possible. It is also important to consider the possible impacts of any past and current year budget problems on planning activities for the next budget.

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- During the third quarter review, due in April and May, councillors should ensure that end-of-year projections are achievable and in line with the budget, as adjusted, and that any impact is factored into the next budget, due for approval in June and implementation in July.

*Past financial year budget activities* focus on accountability for the immediate past year's performance. Steps include community feedback, preparation of financial statements, audit of the financial statements by the Auditor-General, follow up on the auditor's findings, preparation of an annual report on municipal performance, and council's adoption of an oversight report.

### **What are the budget activities for the next financial year?**

Monthly summaries of the activities for planning and preparing the budget for the next financial year are shown in Annexure 2. This table should be reviewed and updated for the specific circumstances of a municipality. However, councillors should note that major changes will result in non compliance with the MFMA, as one process depends on the last, and any delays in one will have a knock-on effect for the others.

### **What are the budget activities for the current financial year?**

The implementation and monitoring activities of the budget for the current financial year are conducted at the same time as the planning and preparation of the budget for the next financial year. The monthly activities for the budget for the current financial year are shown in Annexure 3.

### **What are the budget activities for the past financial year?**

The activities for managing the closure of the budget for the past financial year provide councillors with information about the performance of the municipality during the past year. These facilitate and frame the simultaneous activities required in preparing for the next financial year. Monthly activities for managing the closure of the past financial year are shown in Annexure 4.

### **What consultation process is required when council is considering the budget?**

Municipalities must undertake the public information and consultation process when considering the budget, including the provision of any requested information. Before the budget is tabled and after the budget is tabled in council, the mayor must consult with:

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- the relevant district municipality and all other local municipalities within the area of the district municipality, if the municipality is a local municipality
- all local municipalities within its area, if the municipality is a district municipality
- the relevant provincial treasury, and when requested, National Treasury
- any national or provincial organs of state, as may be prescribed.

The municipality must also provide any information relating to the budget requested by:

- National Treasury
- national departments responsible for water, sanitation, electricity, and any other service as may be prescribed
- any other national and provincial organ of states, as may be prescribed
- another municipality affected by the budget.

### ***After the budget has been tabled in a municipal council***

Immediately after an annual budget is tabled in a municipal council, the accounting officer of the municipality must make public the annual budget and the supporting documents. The accounting officer must also invite the local community to submit comments on the budget.

The budget must be submitted in both printed and electronic formats to National Treasury and the relevant provincial treasury, and in either format to any prescribed national or provincial organs of state and to other municipalities that may be affected by the budget.

During debate and deliberation on the proposed budget, the municipal council must consider any views of the local community, National Treasury, the relevant provincial treasury and any provincial or national organs of state or municipalities that made submissions on the budget. After considering all budget submissions, council must give the mayor an opportunity to respond to the submissions; and if necessary, to revise the budget and table amendments for consideration by the council. The municipal budget and treasury office must play a supportive role to the mayor and council in this regard.

For functions not performed by the municipality, and to promote effective service delivery, the municipality should gather relevant feedback on service delivery weaknesses during its community consultation processes and forward this information to the respective sector department for action. For example, the municipality should direct feedback on weaknesses in the service delivery of education or lack of infrastructure for schools to the relevant provincial and national education departments. Similarly, feedback on issues affecting health, and safety and security, would be communicated to the relevant provincial and national departments.

National Treasury may issue further guidelines on the manner in which municipal councils should process their annual budgets, including guidelines on the formation of a committee of the council to consider the budget and to hold public hearings. These guidelines are binding on a municipal council if adopted by the council. The MSA sets out a process that must be followed for community consultation.

### **What happens if council fails to approve an annual budget?**

If a municipality fails to approve a budget including the revenue-raising measures necessary to give effect to the budget, the council must reconsider the budget and vote again on the budget, or on an amended version of it, within seven days of the council meeting that failed to approve the budget. This process must be repeated until a budget, including revenue-raising measures necessary to give effect to the budget, is approved. If a municipality has not approved an annual budget, including revenue-raising measures necessary to give effect to the budget by 1 July, the mayor must immediately report the matter to the members of the executive council (MECs) for finance and local government in the province. The consequences of continued failure to approve the budget or any revenue-raising measure necessary to give effect to the budget after the start of the budget year are severe.

If after all this, a municipal council still fails to approve a budget, the provincial executive of the relevant province must intervene in the municipality and take any appropriate steps to ensure that the budget or those revenue-raising measures are approved. These measures may include dissolving the council and:

- appointing an administrator until a newly elected council has been declared elected;
- and
- approving a temporary budget or revenue-raising measures to provide for the continued functioning of the municipality.

A budget approved by an administrator must, after the intervention has ended, be replaced by a budget approved by the newly elected council.

Until a budget for the municipality is approved, up to one-twelfth of the funds appropriated for the previous year may be used only to defray current and capital expenditure. This provision would require approval by the MEC for finance in the province. The maximum amount would have to be scaled back proportionately if revenue flows and collections are not at least at the same level as the previous financial year. In addition, any withdrawals under this provision would form part of the subsequently approved annual budget.

### What happens to unspent funds at the end of the budget year?

The appropriation of funds in an annual or adjustments budget lapses to the extent that those funds are unspent at the end of the financial year to which the budget relates, and increases the surplus funds of the municipality. The MFMA provides an exception for the appropriation for capital expenditure for a period not exceeding three financial years, provided a separate appropriation is made for each of those financial years.

In some instances at the end of the budget year, commitments may have been made under the supply chain management policy for acquiring goods or services for which delivery or completion has not occurred. These outstanding commitments must be reviewed to determine if the deliveries will be made in the next financial year.

In such cases, provisions must be made by appropriating money to honour the legal commitments in either the budget or an adjustments budget for the financial year in which the transactions will be completed. Because funds for outstanding prior-year commitments were unspent, cash-backed surplus funds should be available to pay for the expenditure in a subsequent financial year when delivery or contract completion occurs.

### What is a municipal adjustments budget?

It may be necessary for a council to consider a revision of its original budget, owing to material and significant changes in revenue collections, expenditure patterns, or forecasts of these for the remainder of the financial year. The process of passing an adjustments budget should not be seen as a regular event. This is limited to one or a maximum of two adjustments per year.

In these cases, an adjustments budget should be prepared by the municipal manager and submitted to the mayor for consideration and tabling at council. Only the mayor may table an adjustments budget in the municipal council. Councillors may consider and approve an adjustments budget to recognise under-collection of revenue and adjust revenue and expenditure downward.

In accordance with the MFMA, an adjustments budget may be tabled only within prescribed limitations in relation to timing and frequency for the following purposes:

- to appropriate additional revenue that has become available, but only to adjust spending programmes already budgeted for
- to authorise unforeseeable and unavoidable expenditures
- to authorise spending of unspent funds from the previous year that were not foreseen at the time of budget preparation

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- to use projected savings in one vote towards spending under another vote
- to correct errors in the annual budget.

Only the mayor may table an adjustments budget in the municipal council, which must be presented in a prescribed form. When an adjustments budget is tabled, it must be accompanied by an explanation of the effects of and reasons for material changes to the annual budget. If an adjustments budget increases spending, there must be an explanation about the impact of the increased spending on the current annual budget and annual budgets for the next two financial years, including the impact on tariff increases.

An adjustments budget may not increase municipal tax and tariffs during a financial year except when required in terms of a financial recovery plan.

### **How is unforeseen or unavoidable expenditure addressed in terms of the MFMA?**

The mayor of a municipality may in an emergency or other exceptional circumstances, authorise any unforeseeable or unavoidable expenditure for which no provision was made in the budget. Any such expenditure:

- must be in accordance with a framework that may be prescribed
- may not exceed a prescribed percentage of the approved annual budget
- must be reported by the mayor to the municipal council at its next meeting
- must be appropriated in an adjustments budget.

A mayor, acting in good faith, could authorise an unforeseeable or unavoidable expenditure and council could refuse to authorise the expenditure in an adjustments budget. If an adjustments budget is not passed within 60 days after the expenditure was incurred, the expenditure is unauthorised. The mayor would be responsible for the unauthorised expenditure and would be required to reimburse the municipality for the amount of the expenditure.

### **What must councillors consider when appropriating money for capital projects?**

A municipality may spend money on a capital project only if the money for the project, excluding the cost of feasibility studies conducted by or on behalf of the municipality, has been appropriated in the capital budget. The municipality must ensure that all processes and procedures are followed for contracts having budgetary implications beyond the three years, covered in the annual budget for the next financial year. We recommend that council approve a capital programme rather than capital projects.

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Before approving a capital programme, the municipal council must consider the projected cost covering all financial years; and the future operational costs and revenue, including municipal tax and tariff implications.

The funding for the capital programme must be available and not committed for other purposes.

Council should consider the merits of approving capital programmes rather than specific projects. This approach will assist in better performance and effective delivery. Internal and external reporting measures could be used to provide oversight information on matters of strategic importance to councillors.

### **Can council approve a contract beyond the three years?**

A municipality may enter into a contract for a capital programme/project that will impose financial obligations on the municipality beyond a financial year. If the contract will impose financial obligations on the municipality beyond the three years covered in the annual budget, then the municipality must follow strict requirements in terms of the MFMA.

The above provisions for approval of a multi-year contract do not exempt the municipality from any applicable supply chain management regulations.

### **Can council shift funds from one financial year to another financial year?**

When a capital programme has been properly appropriated for more than one financial year, expenditure for that programme during the current financial year may exceed the amount appropriated. But this can only happen provided the increased expenditure is not more than 20 per cent of the current year's appropriation, and is funded within the following year's appropriation.

In addition, the municipal manager must certify that actual revenue for the financial year is expected to exceed budgeted revenue, and sufficient funds are available for the increase without incurring borrowing beyond the annual budget. The mayor must approve the increase in spending in writing. Finally, the municipal manager's certification and mayor's written approval must be submitted to the provincial treasury and the Auditor-General.

### **Summary - Councillors' responsibilities in relation to municipal budgets**

Councillors should focus on allocating budget resources between competing priorities consistent with the strategic direction set out in the IDP. The IDP must be aligned with, and complement, the development plans and strategies of other affected municipalities,

## **PART SEVEN: Municipal budgets and strategic planning**

and provincial and national spheres of government. Facilitating consultation on the budget is critical. The community and other stakeholders will hold council accountable for the delivery of services and the corresponding resources utilised.

The council must review the IDP at least annually. The council may amend the IDP based on its annual review and the IDP, as amended, remains in force until the next elected council adopts its IDP. The IDP is a strategic statement of the municipal council's vision for the long-term development of the municipality.

The executive mayor, as the political head of the municipality, provides political guidance of the budget preparation process through a co-ordinated cycle of events and activities that start nearly one year before the beginning of each financial year. The budget preparation cycle is integrated into the other two key areas of the financial reforms: budget implementation and financial reporting. The MFMA provides for multi-year capital and operating budgets that take into account, and are linked to, the municipality's current and future development priorities as contained in the IDP.

The budget must clearly set out projected revenue by source and estimated expenditure by vote, or different departments or functional service areas. The budget should be accompanied by the SDBIP, which sets out performance objectives for revenue and for each vote, a cash flow and expenditure statement and particulars on investments, municipal entities and service delivery agreements, grant allocations, and details of employment costs and performance agreements.

The mayor must table the budget before council for consultation by 31 March. Following the tabling of the budget, the months of April and May should be used to accommodate public and government comment, and debate the budget and any revisions that may be considered. The mayor should respond to the submissions received and if necessary revise the budget and table amendments for council's consideration. The council considers approval of the budget by engaging with officials and thoroughly reviewing the contents of the budget, and possibly suggesting revisions before final approval. Once the budget is approved, subsequent adjustments may be made based on a well-planned and structured process, such as after the mid-year review is completed. This may be subject to other key processes, for example, the evaluation of current and projected revenue collections, to ensure that a balanced budget is maintained.

If a municipal council fails to approve an annual budget at its first meeting for consideration of approval, including revenue-raising measures necessary to give effect to the budget, the council must reconsider the budget and again vote on the budget, or on an amended version, within seven days of the council meeting that failed to approve

## **PART SEVEN: Municipal budgets and strategic planning**

the budget. Council must repeat the approval process until a budget, including revenue-raising measures necessary to give effect to the budget, is approved. However, if council has not approved an annual budget, including revenue-raising measures necessary to give effect to the budget by 1 July, the mayor must immediately report the matter to the MECs for finance and local government in the province. The MECs may determine an appropriate provincial intervention.

Councillors' major activities in relation to the budget during the financial year focus on monitoring, reporting, and evaluating performance against budget. This involves regular reviews and reports and three major quarterly reviews, and taking action on variations from plans. During the first-quarter review, councillors should make sure that all budget plans are being implemented. During the second quarter or mid-year review, councillors should make sure that implementation has been accomplished on schedule and determine whether there are any major shifts or shortfalls that might require an adjustments budget. It is important to note that, whenever an adjustments budget is necessary, council must deal with the problems causing the need for an adjustments budget as soon as possible.

During the third-quarter review, councillors should ensure that end-of-year projections are consistent with the budget, as adjusted, and that further adjustments, if needed, are considered. Councillors should be aware that the quarterly reviews and any problems that occur could also impact on the preparations for the following year's budget.

## **PART EIGHT**

### **The service delivery and budget implementation plan**

The service delivery and budget implementation plan (SDBIP) is primarily an implementation and management tool.

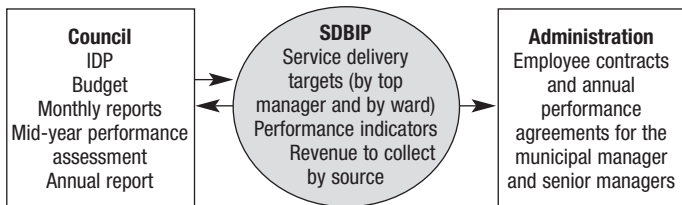
Councillors should be aware that the mayor will approve this, along with the annual performance agreements of senior managers, after council has approved the budget. The performance targets in the SDBIP and annual performance agreements must be aligned to the measurable performance objectives approved by council in the budget. The monthly projections of revenue and expenditure in the SDBIP must sum to the annual budget approved by council.

#### **What is a service delivery and budget implementation plan?**

Both the IDP and budget of the municipality are high-level strategic plans, and are not management or implementation plans. The budget sets end-of-year service delivery and budget targets. The end-of-year targets must be based on quarterly and monthly targets, and the municipal manager must ensure that the budget is built around this quarterly and monthly information. As a start-of-year planning and target tool, the SDBIP gives meaning to in-year reporting and end-of-year annual reports.

The SDBIP can be viewed as a 'contract' between the council and community, as well as between the municipality's administration and council. It promises the community on what the municipality will deliver in the coming year, and lays the basis for measuring performance and progress against end-of-year targets in service delivery and budget implementation (see diagram 3).

**Diagram 3 - The SDBIP contract**



## **PART EIGHT: The service delivery and budget implementation plan**

The SDBIP is a management and implementation tool, which sets in-year targets, such as quarterly service delivery and monthly budget targets. But it does much more than this. It also links each service delivery output to the budget of the municipality, and provides credible management information and a detailed plan for how the municipality will provide these services, as well as the inputs and financial resources to be used. The SDBIP indicates the responsibilities and outputs for each of the senior managers in the top management team, the inputs to be used, and the time deadlines for each output. The SDBIP will therefore inform the performance agreements of the municipal manager and senior manager, including the outputs and deadlines for which they will be held responsible by the mayor. The SDBIP should also provide all expenditure information (for capital projects, services) per municipal ward, so that each output should also be broken down per ward where this is possible.

The SDBIP is also a critical monitoring tool for the mayor to monitor in-year performance of the municipal manager. It is also a tool to enable the municipal manager to monitor the performance of all managers in the municipality within the financial year, and to be pro-active and take remedial steps if there is evidence of poor performance. The SDBIP aims to ensure that managers are problem-solvers, who routinely look out for unanticipated problems and resolve them as soon as possible. The SDBIP enables the council and the public to monitor the performance of the municipality against quarterly targets on service delivery as progress is reported to council.

### **Why have an SDBIP?**

The SDBIP provides the critical link between the mayor, councillors and the administration, and facilitates the process for holding management accountable for its performance. The SDBIP is a management, implementation and monitoring tool that will assist the mayor, councillors, municipal manager, senior managers and community. A properly formulated SDBIP will ensure that appropriate information is circulated internally and externally for purposes of monitoring the execution of the budget, performance of senior management and achievement of the strategic objectives set by council. It enables the municipal manager to monitor the performance of senior managers, the mayor to monitor the performance of the municipal manager, and for the council and community to monitor the performance of the municipality. The SDBIP should therefore determine (and be consistent with) the performance agreements between the mayor and the municipal manager, and the municipal manager and senior managers, which are determined at the start of every financial year and approved by the mayor.

The SDBIP is a layered plan. The top layer of the plan deals with consolidated service delivery targets and in-year deadlines, and links these targets to each top manager.

## **PART EIGHT: The service delivery and budget implementation plan**

Each senior manager is expected to develop the lower layer of detail of the SDBIP. He or she must provide more detail on each output for which he or she is responsible, break up these outputs into smaller outputs and then link these to each middle-level and junior manager. Much of this lower-layer detail will not be made public nor tabled in council.

Only the highest layer of information of the SDBIP will be made public or tabled in the council. This information should also include per ward information, particularly for key expenditure items on capital programmes and projects and service delivery. This will enable each ward councillor and ward committee to oversee service delivery in their ward. Performance information relating to levels of service, frequency of service and quality of service could strengthen this process further.

Being a management and implementation plan (and not a policy proposal), the SDBIP should NOT be approved by the council. It is, however, tabled for the council and public for their information, and for purposes of monitoring.

### **Who is responsible for preparing the SDBIP?**

The municipal manager is responsible for preparing the SDBIP, which must be submitted to the mayor for approval once the budget has been approved by the council (around late-May or early-June). However, the municipal manager should start the process of preparing the top layer of the SDBIP no later than the tabling of the budget (around 1 March or earlier) and preferably submit a draft SDBIP to the mayor by 1 May for initial approval. Once the budget is approved by the council, the municipal manager should merely revise the approved draft SDBIP, and submit it for the final approval of the mayor within 14 days of the approval of the budget. Draft performance agreements should also be submitted with the draft SDBIP by 1 May, and then submitted for approval with the revised SDBIP within 14 days after the approval of the budget. The mayor should therefore approve the final SDBIP and performance agreements simultaneously, and then make the SDBIP and performance agreements of the municipal manager and senior managers public within 14 days, preferably before 1 July.

The council will hold the mayor to account for the outputs and goals made public in the SDBIP, on a quarterly basis during the financial year. It is important to note that such in-year monitoring does not suggest that council should interfere in the administration of the municipality. The council should undertake a more rigorous oversight role in relation to performance at the end of the financial year, when the mayor tables the municipality's annual report. The in-year monitoring is designed to pick up major problems only, and aimed at ensuring that the mayor and municipal manager are taking corrective steps when any unanticipated problems arise. By providing clear service delivery expectations, expenditure and revenue requirements, service delivery

## **PART EIGHT: The service delivery and budget implementation plan**

targets and performance indicators, the SDBIP plays a critical role in forcing both the administration and the council to focus on outputs.

### **What makes up the top layer of the SDBIP?**

The SDBIP is a detailed plan approved by the mayor of a municipality for implementing the municipality's delivery of services and executing its annual budget. It must include (as part of the top layer) projections for each month of:

- revenue to be collected, by source, and operational and capital expenditure, by vote, and
- service delivery targets and performance indicators for each quarter.

The information required on revenue, for example, is necessary because if the municipality is clearly not collecting as much revenue as anticipated in the first or second quarter (for example), it should be taking steps to ensure that it lowers its expenditure targets (through an adjustments budget) or improves its revenue-collection performance. Similarly, if expenditure is happening more slowly than expected, for example through underspending, the municipality needs to improve its capacity to deliver services or ensure that it is making its payments sooner and on time. The information required on revenue and expenditure will allow the mayor to assess the municipality's budget performance, using monthly and mid-year reports submitted by the municipal manager.

Determining the service delivery performance is much harder, and may occur with a lag of one month. This is different from financial information, which should be available within 10 days after the end of each month.

The SDBIP must also provide a mechanism to project and monitor inputs, outputs and outcomes for each senior manager (by department) by vote. Service delivery levels and standards for each ward or designated area must also be shown.

While the SDBIP is effectively a one-year detailed plan, it could easily be extended to cover multiple years. Municipalities are encouraged to include three-year (by quarter) service delivery targets. The municipality may also want to include past and current year information, in order to facilitate comparisons, and outline the remedial steps it is taking in response to problems in the past.

### **What are the different components of the SDBIP?**

The five key components of the SDBIP are:

#### ***Monthly projections of revenue to be collected for each source***

One of the most important and basic priorities for any municipality is to collect all its revenue as budgeted for. Failure to do this will undermine the municipality's ability to

## **PART EIGHT: The service delivery and budget implementation plan**

deliver on services. The municipality **MUST** have a monthly plan for the revenue it expects to be collected for each revenue source. Revenue projections relate to actual cash expected to be collected and should reconcile to the cash flow statement approved with the budget documentation. The reason for specifying actual revenue collected rather than accrued (billed) revenue is to ensure that expenditure does not exceed actual income.

The SDBIP information on revenue will be monitored and reported monthly by the municipal manager. For example, if there is lower-than-expected revenue and an overall cash shortage in a particular month, the municipality may have to revise its spending downwards to ensure that it keeps within its sustainable levels. More importantly, this kind of information requires the municipality to take urgent corrective steps to make sure it improves on its revenue-collection capacity if it wants to maintain its levels of service delivery and expenditure.

While these projections would be most useful as cash flow projections, it is also critical to understand the relationship between revenue billed and the amount actually collected in the context of tariff, credit control and indigent policies and any other relevant policies. Comprehensive, coherent revenue policies that take into account appropriate service delivery levels and standards, people's ability to pay, and collection efforts, will ensure realistic revenue projections and ultimately balanced budgets.

### ***Monthly projections of expenditure (operating and capital) and revenue for each vote***

These projections relate to cash paid and should reconcile to the cash flow statement adopted with the budget documentation.

Each key function is a 'vote' and must have associated with it as appropriate: operating expenditure; revenue; capital expenditure; and measurable performance objectives. Measurable performance objectives include service delivery targets and other financial and non-financial indicators.

The SDBIP should show monthly projections of revenue by vote in addition to revenue by source. When reviewing budget projections against actual, it would be useful to consider revenue and expenditure by vote in order to gain a more complete picture than provided by reviewing expenditure only. The monthly report will require a report against such monthly projections in the SDBIP.

### ***Quarterly projections of service delivery targets and performance indicators for each vote***

The development of appropriate service delivery and performance targets and indicators is a challenge facing all municipalities, and requires further development by

## **PART EIGHT: The service delivery and budget implementation plan**

practitioners. If not designed properly, service delivery objectives can have unintended outcomes, whereby targets are met at the cost of quality or other targets.

While the earlier section required projections of budgeted amounts for revenue and expenditure, this part requires non-financial measurable performance objectives in the form of service delivery targets and other performance indicators. The focus here should be on outputs, and not on inputs or internal management objectives.

Service delivery targets relate to the level and standard of service being provided to the community and include targets for reducing backlogs of basic services. The requirement for service delivery targets is consistent with national government policy requiring the public sector to be able to measure service delivery outputs and outcomes in addition to inputs (expenditure). For example, a service delivery target could be the number of households receiving the defined minimum basic level of clean water, or the level of sanitation, or the frequency and quantity of household refuse removal.

National Treasury has issued a number of guiding circulars over the past 24 months and these should be used for further information, if necessary. For example, the Annual Report Guidelines, which accompanies the annual report circular prepared in 2003 in consultation with the Department of Provincial and Local Government (DPLG), SALGA and National Treasury is applicable.

### ***Ward information for expenditure and service delivery***

It is important to recognise that councillors and the community will benefit greatly from a further breakdown of information on services into municipal wards. This may be achieved by incorporating ward data as follows:

#### *Director Technical Services – Electricity Distribution*

New electricity connections (overall)

- Ward 1 connections
- Ward 2 connections
- Ward 3 connections (and so on)

Alternatively, councillors could be provided with a separate quarterly report showing service delivery information for their respective wards.

### ***Detailed information on capital infrastructure programmes by ward over three years***

The SDBIP should include details of capital infrastructure programmes over three years by ward, reconciled to the budgeted capital expenditure estimates. This provides ward residents with an opportunity to clearly see the progress of capital infrastructure works in the ward. This represents a more transparent process in which residents can clearly see the performance of their municipality against budgeted commitments to the

## **PART EIGHT: The service delivery and budget implementation plan**

community. Such information should include: project number; name; the senior manager responsible; a short description of what the project will deliver; planned start date; actual start date; planned completion date; actual completion date; capital costs timed per month; and reasons for variances including if the project was completed but did not deliver to specification.

An efficient supply chain process is an important component to effective and timely infrastructure/capital service delivery. Appropriate indicators and targets need to be included in the supply chain process to enable the municipality to monitor performance in a way that suits municipal circumstances.

The municipality should ideally publish its draft SDBIP with its budget for consultation, or soon afterwards, as supporting documentation to assist its budget hearings process, which is normally held at the end of March or in April. The SDBIP should be submitted to the mayor by 1 May at the latest. If the draft SDBIP is to be provided for the budget hearings, the municipality may want to bring this date forward, or provide departmental SDBIPs (which are a subset of the SDBIP, based on an individual manager's department such as electricity, health or water) as supporting information to the relevant committee around the end of March. In this case, the mayor will need to approve these departmental or draft SDBIPs by mid-March.

It is up to the municipality to determine how much extra detail it requires, and whether it wants to bring forward its deadlines for submission and approval. A municipality could also opt to have a high level SDBIP complete with ward breakdowns for tabling and publication, but may also make available lower layer departmental SDBIPs and other information as requested by council.

Diagram 4 on page 85 shows the process for approving the SDBIP including how the departmental SDBIPs roll up into the draft SDBIP.

### **What is the format of departmental SDBIPs?**

#### ***Purpose (outcomes)***

- Define the service/s.
- Define the customer/s.
- Show how the service is linked to the IDP (outcomes).

#### ***Service delivery description (outputs)***

- Define the level of service planned for each customer group (outputs).
- Describe the improvements or reductions in service levels and standards planned over the medium term.
- List measurable performance objectives for the budget year, current and past years and at least two future years. Include quarterly projections of service

## **PART EIGHT: The service delivery and budget implementation plan**

delivery targets and other performance indicators in the same format as required for the municipality's SDBIP. Senior managers will refer to current year mid-year reports and the previous year's annual report to develop next year's SDBIP.

- A list of capital projects per ward to be implemented in the budget year in the same format as required for the municipality's SDBIP including: project number; name; short description of what the project will deliver; planned start date; and planned completion date. Include quarterly performance targets for percentage of projects to be completed on time, within budget and to specification also in the same format as required by the municipality's SDBIP.
- A review of past performance and how this impacts on future plans.

### ***Resources used (inputs)***

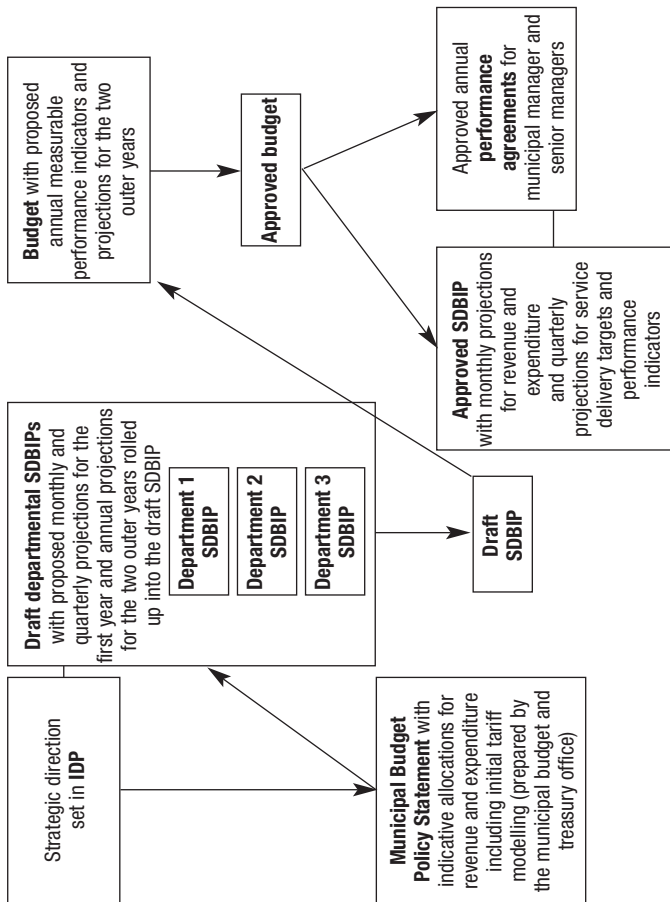
- Budgeted expenditure by vote and type (such as employee related costs or repairs and maintenance) for the budget year, past years and at least two future years. Include monthly projections of expenditure in the same format as required for the municipality's SDBIP.
- Comment on discretionary and non-discretionary expenditure. Non-discretionary items are considered to be costs that have to be incurred.
- Highlight major features of the inputs used in the service being delivered (are they highly mechanised or highly labour reliant, and so on?).
- Type of staffing (professionals, technical, clerical) number and rand value.
- Budgeted revenue by vote and source for the budget year, current year, past years and at least two future years. Include monthly projections of revenue in the same format as required for the municipality's SDBIP, including additional performance measures for revenue targets and collection rates.
- Comment on revenue dependencies, expected major shifts in revenue patterns and possible alternative sources of revenue for investigation.

### **Summary - Councillors' role in relation to the SDBIP**

The SDBIP is primarily an implementation and management tool. Councillors should be aware of the relationship between the budget as approved by council and the SDBIP and annual performance agreements of senior managers (both approved by the mayor after council approves the budget). During quarterly reviews, councillors should review whether the SDBIP is on track and that the mayor and municipal manager are taking appropriate action to correct any significant deviations.

The SDBIP provides operational content to the end-of-year service delivery targets set in the budget and IDP. It determines the performance agreements for the municipal manager and all top managers, whose performance can then be monitored through monthly reports, and evaluated through the annual report process.

**Diagram 4 - Process for preparing and approving the SDBIP**





## **PART NINE**

### **Service delivery mechanisms and municipal entities**

Councillors may be required to consider how certain services are to be delivered.

Various service delivery mechanisms are available to council, and the choice as to which one is used, will depend on individual circumstances and the type of service to be performed.

#### **What are service delivery mechanisms?**

A municipal service may be provided using either an internal or external service delivery mechanism.

#### ***Internal and external service delivery mechanisms***

An internal service delivery mechanism is a service performed through either a municipal department, internal municipal business unit, or other component of a municipal administration.

An external service delivery mechanism may be either a solely or jointly controlled municipal entity, an organisation established by an organ of state or recognised in terms of national legislation, a community-based or non-governmental organisation, or a public-private partnership.

#### ***Municipal entities as an external service delivery mechanism***

The MSA defines a municipal entity as one of three kinds of organisations:

- (a) a private company, that is controlled by one or more municipalities
- (b) a service utility
- (c) a multi-jurisdictional service utility.

#### ***A private company***

A private company is a corporate body established in accordance with section 20 of the Companies Act (1973). It must be either controlled by a single municipality or controlled jointly by two or more municipalities. A private company that meets the above requirements is defined as a municipal entity. Private persons or companies may only have a minority interest in a company that is a municipal entity.

#### ***A service utility***

A service utility is a municipal entity that operates under the sole ownership control of a municipality. It is not a corporate body. A service utility is established by a municipal by-law to provide a municipal service and is capable of suing and being sued in a court of law.

### ***A multi-jurisdictional service utility***

A multi-jurisdictional service utility is a municipal entity that operates under the joint control of two or more municipalities. It is also not a corporate body. A multi-jurisdictional service utility is established by the written agreement of participating municipalities, to provide a municipal service, and is also capable of suing and being sued in a court of law.

### **What is the legal relationship between municipalities and municipal entities?**

Municipalities are prohibited by the MSA from having interests in any types of corporate bodies (other than a private company), including trusts, for the purposes of delivering municipal services (service utilities and multi-jurisdictional service utilities are not corporate bodies.)

Municipal entity group structures that were created before 1 July 2004 are no longer permitted and therefore they must be disbanded or reorganised.

Corporate bodies established by municipal entities under section 21 of the Companies Act (commonly described as 'section 21 companies') are prohibited as of 1 July 2004. However, the amended MSA permits municipalities to convert previously established section 21 corporate bodies to either service utilities or multi-jurisdictional service utilities, depending on the initial ownership structure of such companies.

### **What is council's role in reviewing and selecting a service delivery mechanism?**

The MSA sets out a process that municipalities must go through when selecting a service delivery mechanism to deliver a service. The first step in this process is to review the merits of each of the service delivery mechanisms, whether internal or external. This review must be done on the following occasions:

- when preparing or reviewing the IDPs
- when considering a new municipal service
- when considering a significant upgrade, extension or improvement of an existing municipal service
- when a service delivery mechanism needs to be reviewed for the purposes of completing a performance evaluation
- when restructuring or reorganising in terms of the Municipal Structures Act
- when local communities have requested municipalities to undertake such action during previous community consultation procedures
- when provincial executives instruct municipalities to take such action.

When reviewing service delivery mechanisms, the municipality should review the

## PART NINE: Service delivery mechanisms and municipal entities

background of the existing service delivery mechanism. Councils are required to record the following information about their current service delivery mechanisms during the annual review of their IDPs:

- the rationale for the method(s) currently used in the delivery of all municipal services
- the key challenges, such as efficiency concerns or obstacles to expansion, for each municipal service
- the service delivery methods that could be considered if any changes are suggested in the annual IDP review process.

Municipalities are required by the MSA to assess the merits of using an internal service delivery mechanism before considering the use of an external service delivery mechanism. When assessing the merits of using an internal service delivery mechanism, the following must be considered:

- the direct and indirect costs and benefits associated with providing the service through an internal mechanism, including the expected effect on the environment and human health, well-being and safety
- the municipality's capacity and potential future capacity to furnish the skills, expertise and resources necessary to provide the service
- the organisational structure and human resource capacity that could be used to provide the service
- the likely impact on development, job creation and employment patterns in the municipality
- the views of organised labour
- any developing trends for the provision of sustainable municipal services generally.

Once the assessment of the internal service delivery mechanism has been completed, the municipal council must decide to either utilise the internal service delivery mechanism or defer a decision once an assessment of the merits of using an external service delivery mechanism is completed.

### ***When a municipal council selects an internal service delivery mechanism***

Municipal councils that choose to provide a municipal service through an internal service delivery mechanism must adopt an appropriate resolution. Following the approval of the authorising resolution, the council must put in place the necessary arrangements to provide the municipal service. When using internal service delivery mechanisms, municipalities are required to allocate sufficient human, financial and other resources necessary to establish the internal service delivery mechanism.

### **What must the council consider before providing a service by an external mechanism?**

Municipal councils must consider the following before making a decision to use an external service delivery mechanism:

- a cost benefit assessment; including an evaluation of prospective service providers
- a feasibility study
- an assessment of staff, assets and liability impacts
- the views of the community and other organs of government
- the views of organised labour.

The outcomes of these analyses, assessments and public comments should be presented to council in an evaluation report on the overall merits of delivering the service using an external service delivery mechanism. If the merits of providing a service using an external mechanism are to be explored, the municipal council must first notify its local community before taking any action.

### **What is the consultation process for establishing a municipal entity?**

After receiving the evaluation report, feasibility study and assessments, if the municipal council favours considering the establishment of a municipal entity, then it must undertake a separate process. The consultation may be taken by one municipal council or in conjunction with other municipalities.

Municipalities must prepare an information statement that sets out the results of all the assessments and feasibility studies undertaken. The municipal manager must make these publicly available at least 90 days before the municipal council may consider approval of the proposed municipal entity, or its participation in a proposed municipal entity. The MFMA also requires the municipal manager to invite a number of interested parties to comment on the proposed establishment of a municipal entity. These include:

- the local community, organised labour and other interested persons
- National Treasury
- DPLG
- the MEC for local government in the province.

Once the 90-day consultation process has been completed, the municipal council may formally consider the merits of establishing the proposed municipal entity. Municipal councils must take into account the following matters when making a decision about setting up a municipal entity:

- the results of the assessments/feasibility studies undertaken

## **PART NINE: Service delivery mechanisms and municipal entities**

- any comments or representations on the proposal received from the local community, organised labour and other interested persons
- any written views and recommendations on the proposal received from National Treasury, DPLG and the MEC for local government in the province.

Councils may decide by resolution to proceed with setting up a municipal entity, request further information before making a decision, or resolve not to establish the municipal entity.

### **How is a municipal entity established?**

Once the council has approved establishing a municipal entity, it must begin the process of formally setting out the organisational structure and operational matters for the entity.

If the municipality is establishing a private company, it must register the private company with the Registrar of Companies. The registration process involves filing the company's articles and memorandum of association that are prepared in accordance with the Companies Act and which must comply with applicable municipal finance legislation.

Municipal managers must confirm that the proposed articles and memorandum of association of the entity comply with all legal requirements. Although the Companies Act covers these matters, the municipal council should ensure that they include the organisational structure and operating matters that would be set out in a by-law for a service utility or a written agreement for a multi-jurisdictional service utility.

If the municipal entity is to be a service utility or a multi-jurisdictional service utility, then the council of a parent municipality or of two or more municipalities may establish the service utility. The council passes an authorising by-law in the case of a service utility, and for multiple municipalities, in the case of a multi-jurisdictional service utility authorises the execution of a written agreement. Multi-jurisdictional service utilities may also be established as a result of a request made by the Minister of Provincial and Local Government in consultation with the cabinet member responsible for the particular municipal function.

The MSA requires the council of the parent municipality or municipalities to determine and include the following matters in the by-law or written agreement:

- description of the municipal service or other function to be provided
- authorisation of the necessary powers and functions for the service utility to carry out its purpose

## **PART NINE: Service delivery mechanisms and municipal entities**

- necessary budgetary and funding arrangements for implementation of the by-law
- procedures for a board of directors to govern the municipal entity and supporting operating arrangements, including the procedures for appointing staff and directors
- appointment of a chairperson
- operating procedures of the board of directors
- delegation of necessary powers and duties to the board of directors
- any other matter necessary for the proper functioning of the board of directors
- procedures for acquiring infrastructure, goods, services, supplies or equipment by the service utility, or the transfer of infrastructure, goods, services, supplies or equipment to the service utility
- procedures for the appointment of staff by the service utility, or the transfer or secondment of staff to the service utility in accordance with applicable labour legislation, and terms and conditions of employment
- procedures for governance of and reporting by the service utility, including reports of activities and performance.

In addition, the by-laws and/or agreements for multi-jurisdictional service utilities must also cover the following:

- procedures for the amendment of the establishing agreement
- conditions for, and consequences of, the withdrawal from the agreement of a parent municipality
- conditions for, and consequences of, the termination of the agreement, including the method and schedule for winding up the operations of the multi-jurisdictional service utility, the distribution of proceeds, and allocation among the parent municipalities of any assets and liabilities.

The MSA limits the activities of service utilities and multi-jurisdictional service utilities to the purpose for which they were established and the activities that were set out in their establishment by-laws or agreements.

### **What are service delivery agreements?**

Once the municipal entity is established, the parent municipality or municipalities must authorise the execution of a service delivery agreement between the municipality or municipalities and the board of directors of the municipal entity. The service delivery agreement will include many of the elements of the by-law or multi-jurisdictional agreement that established the municipal entity.

Before a service delivery agreement may be completed, the parent municipality or municipalities must consult with their communities about the content of the proposed

## **PART NINE: Service delivery mechanisms and municipal entities**

service delivery agreements, which must be communicated to local communities through the media and placed on municipal websites.

The service delivery agreement must include mechanisms for amendment and dispute resolution to settle any disagreements that may arise between the municipality and the municipal entity.

The municipality must make provisions to ensure that the services continue, if for any reason the municipal entity is unable or fails to perform their functions in terms of the service delivery agreement. In such situations or if the service agreement is terminated, the municipality must assume the responsibilities for delivering the municipal service to the community.

It is imperative that the municipality is able to manage its arrangements with its entities effectively and responsibly. The municipality must have the capacity to monitor the service level agreement on a regular basis.

### **What are the responsibilities of the municipality in relation to service delivery agreements?**

A municipal council is fully responsible for a municipal service that is provided by a municipal entity and it must structure an appropriate service delivery agreement with the entity. The municipality must:

- regulate and monitor the performance of the utility under the service delivery agreement
- ensure that the entity performs its functions and powers
- establish a tariff policy to control the setting and adjustment of tariffs by the municipal entity
- ensure the provision of uninterrupted service delivery to the community.

A municipality may assign the following responsibilities to a municipal entity through a service agreement:

- service delivery plans within the framework of the municipality's IDP
- operational planning and management of the municipal service
- social and economic development directly related to the service
- customer management and collection of service fees in accordance with the municipal council's tariff and credit control policies
- accounting, financial management, budgeting, investment and borrowing activities by the municipal entity, within a framework of transparency, accountability, reporting and financial control determined by the parent municipality, and subject to applicable municipal finance management legislation

## **PART NINE: Service delivery mechanisms and municipal entities**

- subsidise services to the poor, through a transparent system for the audit of funds and performance monitoring
- transfer or second staff members to the municipal entity, subject to the agreement of staff concerned and applicable labour legislation
- taking over the municipal services, including all assets, when the service delivery agreements expire or are terminated.

### **How does a parent municipality appoint directors of a municipal entity?**

A municipal entity's board of directors must have the appropriate range of expertise to effectively manage and guide the activities of the municipal entity. At least one-third of the directors are to be non-executive directors with a non-executive chairperson. These requirements are consistent with generally accepted governance principles, which emanated from the 2002 King Report on Corporate Governance in relation to the composition of boards of directors and the qualifications of chairpersons of boards of directors. Non-executive board members will be completely independent of both the municipal entity and the parent municipality.

A parent municipality of a municipal entity, before nominating or appointing an executive or non-executive director, must ensure that:

- applications for nomination or appointment are solicited widely among the community
- a list of all applicants and any prescribed particulars concerning applicants is compiled
- the municipal council makes the appointment or nomination from this list.

The following persons are prohibited from being appointed to be an executive or non-executive director if he or she:

- holds office as a councillor of any municipality
- is a member of the National Assembly or a provincial legislature
- is a permanent delegate to the National Council of Provinces
- is an official of the parent municipality of the municipal entity
- presents certain prescribed moral, mental or financial concerns.

The municipal council of the parent municipality may remove or recall a director appointed or nominated by that municipality for unsatisfactory performance, failure or inability to perform the duties of a director; or if he or she is convicted of fraud or theft or offence involving fraudulent conduct, or breaches any legislation regulating the conduct of directors.

Once appointed, directors of a municipal entity must comply with South African

corporate governance standards. The MSA sets out the duties of the directors of a municipal entity board. The board of directors of a municipal entity must:

- provide effective, transparent, accountable and coherent corporate governance and conduct effective oversight of the affairs of the municipal entity
- ensure that the board and the municipal entity comply with all applicable legislation and agreements
- communicate openly and promptly with the parent municipality of the municipal entity
- deal with the parent municipality of the municipal entity in good faith at all times.

### **What are the responsibilities of parent municipality representatives, political office bearers and officials in relation to a municipal entity?**

The parent municipality is to establish a municipal representative or representatives to facilitate communications between the council and the board of directors. The council must designate an official, to be a representative of the parent municipality. The municipal representative or representatives attend meetings of the board of directors as a non-participating observer or observers on behalf. The municipal representative or representatives exercise the parent municipality's rights and responsibilities at shareholder meetings.

Although municipal representatives are appointed to facilitate communication, the official line of communication between a municipal entity and parent municipality is between the chairperson of the municipal entity's board of directors and the mayor or executive mayor, as the case may be, of the parent municipality. A mayor or executive mayor may at any time call or convene any meeting of shareholders or other general meeting comprising the board of directors and the representative(s) of a parent municipality or municipalities, in order for the board of directors to give account for their actions.

The mayor of a parent municipality must guide the municipal council in the exercise of its rights and powers over a municipal entity. The mayor ensures that the municipal entity complies with the MFMA and other legislation and is accountable to the parent municipality. The mayor, however, must not obstruct the municipal entity in the performance of its operational responsibilities. The mayor of the parent municipality may only monitor the operational functions of the municipal entity.

The mayor may delegate the powers and duties assigned under the MFMA relating to municipal entities to other councillors or council committees subject to the Municipal Structures Act.

## **PART NINE: Service delivery mechanisms and municipal entities**

Under the MFMA, the mayor has particular responsibilities in the processes for evaluating municipal entity budgets and dealing with municipal entity annual reports. The mayor of the parent municipality is responsible for tabling proposed and approved budgets of municipal entities in the council. The mayor of a parent municipality must, within seven months after the end of a financial year, table in municipal council the annual reports of municipal entities under their sole or shared control. The mayor must address any questions raised by the council when considering an oversight report. Council must consider the oversight report within two months from the date that the annual reports were tabled in council. The mayor is responsible for making sure that the municipal council addresses any issue raised by the Auditor-General in audit reports relating to the municipal entity.

The municipal manager, as accounting officer of a parent municipality, must provide guidance and advice on compliance with the MFMA to all parties with assigned responsibilities under the act. These include political structures, political office bearers and officials of the parent municipality and the municipal entity.

The municipal manager is the principal advisor to the parent municipal council on matters relating to a municipal entity. The municipal manager has oversight responsibilities in the financial management of a municipal entity. The municipal manager's fiduciary responsibilities are specified in the MFMA and apply to a municipal entity. Similarly, the general financial management responsibilities of a municipal manager that are specified in the MFMA also apply to the financial administration of a municipal entity.

The specific reporting responsibilities for municipal managers in relation to municipal entities under the MFMA are to:

- include municipal entities' plans and budgets, as well as their funding arrangements
- include municipal entities' adjusted budgets in the monthly budget statements submitted to municipal mayors, and provincial treasuries and National Treasury
- include assessments of the performance of municipal entities adjusted budgets in their mid-year budget and performance reports
- inform provincial treasuries and National Treasury in writing of any failure by municipal entities to adopt or implement supply chain management policies
- forward information on municipal entities' bank accounts to the Auditor-General, National Treasury and the relevant provincial treasuries.

### **Summary - Councillors' role in relation to entities and service delivery mechanisms**

Municipal services may be provided using either internal or external service delivery

## **PART NINE: Service delivery mechanisms and municipal entities**

mechanisms. An internal service delivery mechanism may be a municipal department, business unit or other component of municipal administration. An external service delivery mechanism may be a solely or jointly controlled municipal entity, an organisation established by an organ of state or recognised in terms of national legislation, a community based or non-government organisation or a public-private partnership.

The MSA sets out a process that municipalities must go through when selecting service delivery mechanisms. This must be done when the municipality prepares or reviews its IDP, when considering a new service (or upgrading or evaluating the performance of an existing service), when restructuring or when requested by the community or instructed by the province.

Before making a decision to use an external service delivery mechanism to provide a service, municipalities must consider the impacts that decision will have on staff, and on the assets and liabilities of the municipality. It must do a comprehensive cost-benefit analysis and feasibility study, and solicit the views of the community, organised labour and other organs of state. If after all the preliminary studies are undertaken, council wishes to go ahead with the establishment of a municipal entity, it must then consult with the community, organised labour, National Treasury, DPLG and the MEC for local government in the province.

Three types of municipal entity are permitted – a private company, a service utility or a multi-jurisdictional service utility. Each are established differently, and councillors must be aware of the characteristics, rights and obligations of each type of entity before they consider the most appropriate one to use.

The MSA provides details of how a municipal entity is established, and the ongoing operation of the entity. The MFMA provides the financial management arrangements for municipal entities. Together they create the legal framework and governance arrangements for council and the entity.

Councillors are not permitted to be executive or non-executive members on a board of directors of a municipal entity, although council may appoint an official of the municipality as council's representative to sit on the board as an observer.

A council is fully responsible for the services provided by the entity, and must develop a service delivery agreement with the entity to regulate and monitor the performance of the entity, through appropriate plans and policies that formalise the governance and management arrangements between the parties.

The mayor of a parent municipality must guide the municipal council in the exercise of its rights and powers over a municipal entity. The mayor ensures that the municipal

## **PART NINE: Service delivery mechanisms and municipal entities**

entity complies with the MFMA and other legislation and is accountable to the parent municipality. The municipal manager is the principal advisor to the parent municipality on matters relating to the municipal entity, and must provide guidance to the council in relation to compliance with the legislation.

## **PART TEN**

### **Supply chain management**

#### **What is a supply chain management policy?**

Supply chain management refers to the procurement and asset disposal system of a municipality or municipal entity. The MFMA recognises supply chain management as a crucial component of municipal financial management. The efficiency and effectiveness of the procurement function has a large impact across a municipality. If goods and services are of poor quality, overpriced or not available when needed, service delivery will suffer. The MFMA aims to eliminate conflicts of interest in the disposal of assets and procurement of goods and services utilising public funds and provides for open and transparent systems.

The objective for municipalities and municipal entities is to establish a supply chain management policy that is focused on integrity, efficiency, and obtaining the best value for money. This will secure public confidence that public funds are being spent prudently, on its behalf, and not for the personal benefit of public office bearers, officials or their friends. Diligent care must be taken to establish controls in order to eliminate even the perception of fraud or abuse, which can be just as destructive to the public trust as the real thing.

The MFMA requires every municipality or municipal entity to adopt a supply chain management policy that applies to:

- procuring goods and services
- selecting contractors and other external mechanisms to provide assistance in the provision of municipal services
- disposing of assets, including goods no longer needed.

A municipality or municipal entity may not dispose of an asset that is needed to provide the minimum level of basic services even if that service has been outsourced.

National Treasury has provided a model supply chain management policy to assist municipalities and municipal entities, which is supported by National Treasury MFMA circular number 22 of 2005. Once the municipal council or the board of directors of a municipal entity has adopted a supply chain management policy, the municipal manager/accounting officer is responsible for implementing it.

The municipal manager/accounting officer of the municipality or municipal entity must take all reasonable steps to ensure that proper procedures and separation of duties in the supply chain management system are in place to minimise the likelihood of fraud,

## PART TEN: Supply chain management

corruption, favouritism and unfair and irregular practices. The MFMA prohibits any person from obstructing the accounting officer in fulfilling this responsibility. The accounting officer must ensure that the municipality or municipal entity provides resources or opportunities to train officials and that those officials meet the competency levels required by the MFMA.

The supply chain management policy of a municipality or municipal entity must be fair, equitable, transparent, competitive and cost effective.

It must cover at least the following:

- the process for the requisition for acquiring goods or services and the delegated authority for making the request
- an effective system for the disposal or letting of assets, including unserviceable, redundant or obsolete assets, land and buildings
- stipulate that immovable assets, for example land, buildings and dams must be sold or let at market related prices, unless in the public interest or the plight of the poor demand otherwise
- the process for independent verification that funds have been budgeted for the goods or services and will remain available until delivered or completed
- the processes that must be followed including tenders, quotations, auctions and other types of competitive bidding or disposal options
- the procedures and mechanisms for each type of process and when they must be applied
- the procedures and mechanisms for more flexible processes where the value is below a prescribed amount
- open and transparent pre-qualification processes for tenders or other bids
- competitive bidding processes in which only pre-qualified persons may participate
- bid documentation, advertising for and invitations to bid
- the procedures and mechanisms for publicly opening, registering and recording bids
- the procedures and mechanisms evaluating bids to ensure best value for money, negotiating the final terms of contracts, and approving bids
- screening processes and security clearances for prospective contractors on tenders or other bids above a prescribed value
- compulsory disclosure of any conflicts of interests contractors may have in specific tenders and excluding them from those tenders or bids
- barring persons (both individuals and companies) from participating in tendering or other bidding processes who were convicted for fraud or corruption; or wilfully neglected, reneged on or failed to comply with a government contract during the past five years, or who have tax matters outstanding with the South African Revenue Service

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- measures for combating fraud, corruption, favouritism and unfair and irregular practices in municipal supply chain management
- measures for promoting ethics of officials and other role-players involved in municipal supply chain management
- invalidating recommendations or decisions that were unlawfully or improperly made, taken or influenced, including recommendations or decisions that were made, taken or in any way influenced by councillors or municipal officials
- the procurement of goods and services by municipalities or municipal entities through contracts procured by other organs of state
- contract management and dispute settling procedures
- the delegation of municipal supply chain management powers and duties, including to officials.

### **Can a councillor or a close family member do 'business' with a municipality?**

A municipality and municipal entity may not make any award to:

- a person who is in the service of the state if that person is a company or business then a director, manager, principal shareholder or stakeholder who is in the service of the state
- a person who is an advisor or consultant contracted with the municipality or municipal entity.

'In the service of the state' means to be:

- a member of any municipal council, any provincial legislature or the National Assembly of the National Council of Provinces
- a member of the board of directors of any municipal entity
- an official of any municipality or municipal entity
- an employee of any national or provincial department, national or provincial public entity or constitutional institution within the meaning of the Public Finance Management Act
- a member of the accounting authority of any national or provincial public entity
- an employee of Parliament or a provincial legislature.

The Minister of Finance has specifically exempted non-executive board members of a municipal entity from the prohibition for being in the service of the state but only in relation to supply chain awards by a municipal entity that they do not serve on.

Councillors should also be aware that notes to the annual financial statements of a municipality or a municipal entity must disclose particulars of any award of more than R2000 to a person who is a spouse, child or parent of a person in the service of the state, or has been in the service of the state in the previous 12 months, including the

name of that person, the capacity in which that person is in the service of the state and the amount of the award.

### **Does the MFMA require a municipality or municipal entity to consider an unsolicited bid?**

An unsolicited bid refers to a proposal received to supply a good or service or to dispose of an asset outside the normal bidding process. This generally implies that the proposal has not been called by the municipality and has not been subjected to a transparent and accountable process. A municipality or municipal entity is not obliged to consider an unsolicited bid and the legislation discourages this.

### **Can a different tender be approved from that recommended by the tender committee?**

If a tender other than the one recommended in the normal course of implementing the supply chain management policy of a municipality or municipal entity is approved, the accounting officer of the municipality or municipal entity must, in writing, notify the Auditor-General, the relevant provincial treasury and National Treasury and, in the case of a municipal entity, also the parent municipality, of the reasons for deviating from such recommendation.

This reporting requirement is to ensure proper transparency and accountability, and the Auditor-General may pay closer attention to these transactions during audits. This allows for appropriate checks and balances.

### **What does the MFMA require in terms of contracts and contract management?**

A contract or agreement procured through the supply chain management system of a municipality or municipal entity must be in writing and stipulate the terms and conditions for:

- termination because of unsatisfactory performance
- mechanisms to settle disputes between the parties
- procedures for periodic review of the contract or agreement.

The accounting officer of a municipality or municipal entity is responsible for managing contracts and agreements and must:

- take all reasonable steps to ensure that a contract or agreement is properly enforced
- monitor on a monthly basis the performance of the contractor under the contract or agreement

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- establish capacity in the administration to assist in carrying out the duties required by the supply chain management policy.

A contract or agreement may be amended, but only after:

- the reasons for the proposed amendment have been tabled in the council of the municipality or, in the case of a municipal entity, in the council of its parent municipality
- the local community has been given reasonable notice of the intention to amend the contract or agreement; and has been invited to submit representations to the municipality or municipal entity regarding the amendment.

The accounting officer is required to regularly report to the council of the municipality or the board of directors of the entity on the management of contracts or agreements and the performance of the contractors.

### **Can councillors serve on municipal tender committees?**

The MFMA requires a council or board of directors to adopt a supply chain management policy. The MFMA has separated the roles so that councillors and board members are required to concentrate on oversight and not on administrative activities. Therefore, councillors of municipalities and members of board of directors of municipal entities are barred from serving as a member of a bid committee or any other committee evaluating or approving tenders, quotations, contracts or other bids. They are also barred from attending any such meeting as an observer. This principle also applies to councillors serving on land approval committees.

The MFMA further stipulates that no person may interfere with the supply chain management system of a municipality or municipal entity, or amend or tamper with any tenders, quotations, contracts or bids after they have been submitted.

### **How does the municipal council authorise a public-private partnership?**

A municipal council may authorise a public-private partnership agreement, if the municipality can demonstrate that the agreement will:

- provide value for money to the municipality
- be affordable for the municipality
- transfer appropriate technical, operational and financial risk to the private party.

A public-private partnership agreement must comply with the Public-Private Partnership Regulations, 2005. If the public-private partnership involves the provision of a municipal service, then the municipality must also comply with the MSA, which deals specifically with municipal entities.

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The municipality must conduct a feasibility study before a public-private partnership is concluded. The feasibility study must describe the strategic and operational benefit of the public-private partnership to the municipality and set out in specific terms:

- the roles in the partnership agreement
- the legality of the partnership agreement
- the affordability and value to the municipality
- the provision of technical and operational expertise by the private party
- the transfer of financial risk to the private party
- the impact on revenue flows and current and future budgets of the municipality
- the capacity of the municipality to effectively monitor, manage and enforce the partnership agreement.

When a feasibility study has been completed, the accounting officer of the municipality must submit the feasibility study together with all other relevant documents to the council for consideration. The council will need to make a decision on whether the municipality should continue with the proposed public-private partnership. Before the council may consider the proposed partnership, the accounting officer must make public the particulars of the proposed partnership, including the feasibility study. The information must be made public at least 60 days before council may take action on the matter. In its deliberation of the proposed public-private partnership, the council must consider the views and recommendations of the community, National Treasury; and DPLG. If the public-private partnership involves the provision of water, sanitation, electricity or any other service, as may be prescribed, the council must also consider the recommendations of the responsible national department, and any other national or provincial organ of state.

### **Summary - Councillors' role in supply chain management**

Supply chain management incorporates both the purchasing of goods and services and the disposal and letting of assets. A supply chain management policy must be adopted by the council, or board of directors in the case of a municipal entity. The policy must provide the details on systems and procedures to be followed for supply chain management and include the steps to be taken to combat fraud, corruption and conflict of interest. The municipal manager or accounting officer is responsible to implement the policy and to report regularly to the council or board of directors on implementation of the policy.

One of the greatest impacts of the MFMA has been to strengthen governance principles, by separating the roles and responsibilities of key players in supply chain management.

## **PART ELEVEN**

### **Financial reports: councillors' tools for oversight**

Regular in-year financial and performance reports, annual financial statements, the audit report and the annual report are all useful oversight documents that will assist councillors in performing their oversight role.

Councillors will be required to use, understand and review in-year reports, annual financial statements, audit reports and annual reports in discharging their oversight over municipalities and municipal entities. The new approach to municipal financial management places increased importance on oversight and accountability for the executive mayor or committee and all non-executive councillors. This approach is being introduced at an opportune time in the transformation of local government.

These reforms, if properly implemented, will ensure timely in-year reports that provide up-to-date performance and financial information, and will assist councillors in policy making. Executive mayors or committees, non-executive councillors and other public office bearers and officials will be held accountable for municipal service delivery. With this new level of accountability, elected public officer bearers, residents, taxpayers and users of municipal services will be able to monitor whether public services are being delivered effectively and efficiently.

The continued pressure to do more for less will lead to a greater emphasis on monitoring performance through financial reporting that is linked to planning and budgeting systems. Improved financial reporting and a system of performance measurement is expected to increase service delivery capacity by ensuring that municipal programmes and services are achieving their intended results – in terms of outcomes, outputs and timing - at a reasonable cost to the taxpayer and municipal service user.

Another useful source of independent analysis on financial and other related matters could be a report from a credit rating agency. These ratings are regularly updated and council and officials can get a sense of whether or not their municipality's situation and status is improving.

#### **How can councillors use financial reporting to determine how well municipal programmes and services are being delivered to their constituents?**

Councillors' oversight responsibility is accomplished through the use of financial management reports that assess effectiveness, efficiency, service quality, and

municipal productivity and reports on SDBIP implementation that assess whether promised service delivery targets have been delivered.

In order to be properly accountable and oversee municipal programmes and services, councillors must determine how well these programmes and services are being delivered to their constituents. Councillors, board members, public office bearers and officials will need to measure service delivery. This is accomplished by a framework of financial and non-financial reporting on the achievement of performance measures established in the budget and the SDBIP.

The overall purpose of performance measures is not to monitor performance of individual employees, but to assess the cost and quality of municipal service delivery. More importantly, the oversight role of performance measurement relies on continuous improvement in the capacity to deliver services by identifying deficiencies in current work processes. As the deficiencies are eliminated service delivery becomes more efficient.

### **What reports should councillors use in their oversight role?**

The MFMA requires a range of reports to be prepared by the municipal manager, and/or the executive mayor or committee. The main reports to be considered by council should report against the IDP, annual budget, adjustments budget and the SDBIP. Reports include:

- in-year performance reports of the municipality
- annual performance agreements for the municipal manager and all senior managers
- reports on the remuneration and benefits of councillors, public office bearers, and staff remuneration
- all service delivery agreements
- all long-term borrowing contracts
- ward committee information on service delivery
- annual review of the supply chain management policy implementation
- public-private partnership agreements
- reports from internal audit and the audit committee
- annual financial statements of the municipality
- the Auditor-General's report for the municipality
- the municipality's annual report including disclosures of the municipality
- annual report for the municipality and any municipal entity under the municipality's control
- other reports and reportable matters as prescribed by the MFMA or other legislation.

In addition, the municipality should have reports pertaining to any municipal entity under the municipality's sole or shared control, including:

- the annual budget of the municipal entity
- in-year budget and performance reports of the municipal entity
- financial statements of the municipal entity
- annual report and required disclosures of the municipal entity
- other reports and reportable matters.

### **How can financial statements assist councillors in their oversight role?**

In addition to monthly, quarterly and mid-year budget reports and performance assessment reports, annual financial statements inform councillors about the financial health and performance of the municipality or the municipal entity for the previous financial year. The financial information, together with non-financial information, is used to evaluate service delivery accomplishments of the municipality or entity during the past year.

Financial statements represent management's assertions about the municipality's or municipal entity's finances. Financial statements are taken from the accounting records of the municipality or municipal entity. The annual financial statements of a municipality or municipal entity present the financial position at the end of the financial year: assets (the amount owned by the municipality or entity) and liabilities (the amount owed) resulting in net assets (or community wealth). The annual financial statements provide information about the financial position, financial performance, cash flows and changes in net assets or liabilities of a municipality or a municipal entity that is useful to a wide range of users. Financial statements also show the results of the stewardship of management, and the accountability of management for the resources entrusted to it.

### ***The objectives of annual financial statements***

- to assist the municipality to be publicly accountable and present information that -
  - shows whether current year revenues were sufficient to meet the cost of providing current year services
  - demonstrates whether resources were obtained and used in accordance with the municipality's or entity's legally adopted budget, and in compliance with other finance-related legal or contractual requirements
  - assists users to assess service efforts, costs, and accomplishments of the municipality or entity.
- to assist users to evaluate the operating results by presenting information about -
  - sources and uses of financial resources

## PART ELEVEN: Financial reports: councillors' tools for oversight

- how the municipality or entity finances activities and meets cash flow requirements
- the financial position and whether it improved or deteriorated as a result of the year's operations.
- to assist users to assess the level of services that were provided and whether it met obligations as they become due by providing information about -
  - its financial health
  - physical and other non-financial resources that extend beyond the current year, including information that can be used to assess the potential of those resources
  - legal or contractual restrictions on resources and the risk of potential loss of resources.

Financial statements that meet these objectives generally provide the required level of information sought by users. However, financial statements do not provide all the information that councillors need to make decisions since they largely portray the financial effects of past events. Accordingly, useful forward-looking financial and non-financial information must be added in the annual report.

### ***The contents of annual financial statements***

Councillors should use financial statements and the annual report to hold officials and senior management accountable for their stewardship responsibilities of safekeeping the municipality's resources and for their proper and efficient use. The financial statements help councillors to determine the certainty and sustainability of the municipality's service delivery. Information about recent past financial performance is useful in assessing the anticipated future financial performance of the municipality or municipal entity. The information is also useful in forming judgments about the effectiveness of the use of resources; whether there should be any changes to the way resources are used; or how additional resources might be employed.

The annual financial statements consist of:

- statement of financial position (or the balance sheet)
- statement of financial performance (or the income statement)
- statement of cash flows
- statement of net assets
- notes to the financial statements.

Resources, financial structure, liquidity and levels of sustainability are all elements that affect the financial position of a municipality or a municipal entity. Financial position is also affected by the capacity to adapt to changes in the operating environment. For example, when there is a major shift in functions to or from the municipality, councillors need to understand the financial and other implications for the municipality.

Information about the resources and the ability to change its resources in the past is useful in predicting the ability of a municipality to sustain service delivery in the future. Information about financial structure is useful in predicting future financing and borrowing needs; and in assessing the entity's capacity to cope with more financing.

Cash flow information is useful for assessing the municipality's investing, financing and operating activities during the reporting period. This information provides users with a basis to assess the ability of the municipality to generate and use cash and cash equivalents. Liquidity refers to the availability of cash in the near future and is useful in predicting the ability of a municipality or municipal entity to meet financial commitments as they fall due.

The component parts of the financial statements interrelate because they reflect different aspects of the operations. Although each statement provides information that is different from the others, no single statement alone provides all the information necessary for particular needs of users. For example, a statement of financial performance provides an incomplete picture unless it is used in conjunction with the statements of financial position, changes in net assets and cash flows.

An integral part of the financial statements are the notes, supplementary schedules, and other information. For example, they may contain additional information about the items in the statement of financial position and statement of financial performance that is helpful for users. The notes include disclosures about the risks and uncertainties affecting the municipality or entity and any resources and obligations not recognised in the statement of financial position. Information about service segments and the effect of changing economic conditions may also be provided in the form of supplementary information.

The notes to the annual financial statements of a municipality among other items of information must include particulars of:

- the significant accounting policies that set out the basis of recognition and measurement of material transactions included in the annual financial statements
- a list of all municipal entities under the sole or shared control of the municipality during the financial year and as at the last day of the financial year
- allocations received from an organ of state in the national or provincial sphere of government, another municipality or a municipal entity; how the allocations were spent per vote, and any particulars of non-compliance with the allocations
- allocations made to a municipal entity, another municipality or any organ of state
- the total amount of contributions to organised local government for the financial year, and the amount of any contributions outstanding as at the end of the financial year

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- the total amounts paid in audit fees, taxes, levies, duties and pension and medical aid contributions, and whether any amounts are outstanding as at the end of the financial year
- the salaries, allowances and benefits of political office bearers and councillors of the municipality, whether financial or in-kind, including a statement by the accounting officer whether or not those salaries, allowances and benefits are within the upper limits set for councillors
- any arrears owed by individual councillors to the municipality, or a municipal entity under its sole or shared control, for rates or services and which at any time during the relevant financial year were outstanding for more than 90 days, including the names of those councillors
- the salaries, allowances and benefits of the municipal manager, the chief financial officer, every senior manager and such categories of other officials as may be prescribed.

The notes to the annual financial statements of a municipal entity must include particulars of:

- allocations received from any municipality or other organ of state and any particulars of non-compliance with the allocations
- allocations made by the entity to a municipality or other organ of state
- the salaries, allowances and benefits of members of the board of directors of the entity
- the salaries, allowances and benefits of the chief executive officer, every senior manager and categories of other officials as may be prescribed.

Other information that must be disclosed in the notes to the annual financial statements of a municipality or municipal entity include:

- the name of each bank account held by a municipality or entity during the relevant financial year, the type of account and the opening and year-end balances in each of these bank accounts
- a summary of all investments of the municipality or entity as at the end of the financial year
- particulars of any contingent liabilities of the municipality or entity as at the end of the financial year
- particulars of any material losses and any material irregular or fruitless and wasteful expenditures, including in the case of a municipality, any material unauthorised expenditure that occurred during the financial year and whether these are recoverable, and whether criminal or disciplinary steps have been taken as a result of such losses or such unauthorised, irregular or fruitless and wasteful expenditures, or the amount of material losses that have been recovered or written off

- any particulars of non-compliance with the MFMA.

Management's assertions of the municipality's or municipal entity's finances in the annual financial statements are prepared by the accounting officers. The municipal accounting officer must prepare and submit the statements to the Auditor-General for auditing within two months after the end of the financial year. The accounting officer of a municipal entity must prepare the annual financial statements of the entity, and submit the statements to the parent municipality of the entity and the Auditor-General for auditing within two months after the end of the financial year.

The accounting officer of a municipality which has sole control of a municipal entity, or which has effective control, must also prepare consolidated annual financial statements incorporating the annual financial statements of the municipality and of the entity. The consolidated annual financial statements must comply with any other requirements as may be prescribed and be submitted to the Auditor-General for auditing within three months after the end of the financial year.

### **Why are the audit of annual financial statements and the Auditor-General's audit report important for the councillor?**

The goal of the independent audit of the annual financial statements is to assure councillors, officials, the public and other users of a municipality's financial information that the financial statements are fairly presented. The auditor's opinion on the fairness of the presentation of a set of financial statements is critical to discharging public accountability in a transparent manner. The accounting standards will be updated from time to time as government reforms unfold. These standards are applicable to all municipalities. All other entities under the ownership control of a municipality must comply with the new standards in order to facilitate preparation of consolidated financial statements by parent municipalities.

The Auditor-General may use a variety of methods to obtain the evidence needed to determine whether the financial statements are fairly presented. Auditors inspect relevant documentation; observe employee performance; enquire about and review policies, procedures, transactions, and events; confirm balances and transactions with outside parties; and perform analytical procedures to determine the reasonableness of transactions and balances.

The Auditor-General also examines and tests the municipality's or municipal entity's compliance with the system of internal controls as a basis for reliance on the records that make up the financial statements. Management is responsible for protecting the municipal or entity assets and for ensuring the integrity and comprehensiveness of the data recorded by the system.

The Auditor-General is concerned with determining that the municipality or municipal entity has complied with laws, regulations, and provisions of contracts, grant agreements, or allocations that could have a direct and material effect on the financial statements. The Auditor-General will report any findings of instances of non-compliance with each of the above obligations.

Within three months of receiving the statements, the Auditor-General is required to submit an audit report to the council of the municipality or board of directors of the municipal entity.

### **What is the meaning of an audit opinion?**

The Auditor-General's audit report communicates the Auditor-General's opinion or possibly disclaimer of opinion on whether the financial statements are fairly presented. Generally, this report will indicate the responsibilities of management and the Auditor-General: that management is responsible for the financial statements and the Auditor-General is responsible for determining if those statements are fairly presented. It provides the scope of the audit, which gives general information about the auditing standards followed, as well as the nature and limitations of a financial statement audit. Lastly, the report will set forth the Auditor-General's considered assessment of whether the financial statements are fairly presented in accordance with the auditing standards applied on a consistent basis.

The audit report may have an unqualified opinion, qualified opinion or disclaimer of opinion:

- An unqualified opinion is one in which the Auditor-General can state, without reservation, that the financial statements are fairly presented
- A qualified opinion expresses reservations by the Auditor-General about the fair presentation of the financial statements. One common reason for a qualified opinion may be an insufficiency of the underlying financial records to support some of the data in the financial statements. In this case the Auditor-General may conclude that the financial statements are presented fairly except for the insufficiently supported data
- A disclaimer of opinion is given when the Auditor-General does not have all of the underlying documentation needed to determine an opinion about whether the financial statements are fairly presented. For example, at some point the lack of underlying documentation and the amounts in question may be so great so that it is impossible to give any opinion on all, or a significant portion of the financial statements.

In addition to expressing an opinion on the financial statements, the Auditor-General is required to communicate all reportable conditions and findings discovered in the

course of the financial statement audit. These findings may include instances of non-compliance with laws, regulations or terms of grants and allocations, questioned costs that may have resulted from non-compliance, material weaknesses in the system of administrative and internal controls; material weaknesses in the system of performance measurement; and evidence of irregular, fruitless and wasteful expenditures. These findings may or may not impact on the decision on the fairness of the financial statements, and are included in the Auditor-General's report.

### **What is meant by internal control?**

Internal controls are the practical means that management uses to achieve the above objectives. A comprehensive framework of internal controls must do the following:

- produce a favourable control environment
- ensure the ongoing assessment of risk
- establish and maintain control-related policies and procedures
- facilitate communication
- provide for monitoring the effectiveness of control-related policies and procedures as well as the resolution of potential problems that may be identified.

### **What is the Auditor-General's report on the results of performance measurement?**

The Auditor-General also issues a report on the results of the performance measurement of the municipality or municipal entity for the financial year. The Auditor-General provides an assessment of the controls implemented by the municipal manager/accounting officer to develop and manage the municipality's or municipal entity's performance management system. The Auditor-General may comment on the following activities of a performance management system:

- objectives for performance management purposes have been clearly defined
- the performance management system has been implemented
- key performance indicators have been developed
- targets have been set for the key performance indicators
- internal monitoring and in-year reporting is part of the performance management system
- the system has a methodology for evaluation and revision of strategies and objectives.

### **What happens when the audit is not completed on time?**

If the Auditor-General is unable to complete an audit within three months of receiving the financial statements from an accounting officer, the Auditor-General must promptly submit a report outlining the reasons for the delay to the relevant municipality or

municipal entity and to the relevant provincial legislature and Parliament.

The annual financial statements, as audited by the Auditor-General, form part of the basis for the annual report, which must be prepared by the accounting officer within six months after the end of a financial year.

Once the Auditor-General has submitted an audit report to the accounting officer, no person other than the Auditor-General may alter the audit report or the financial statements to which the audit report relates.

### **What are the purposes and contents of the annual report?**

Some key purposes of the annual report are:

- to provide a record of the activities of the municipality or entity
- to provide a report on performance in service delivery and budget implementation
- to provide information that supports the revenue and expenditure decisions made
- to promote accountability to the local community for decisions made.

In the past, annual reports have often been used solely to promote the image of the municipality, with little focus on comparing actual with promised performance. The MFMA now requires the municipality to report on all aspects of performance providing a true, honest and accurate account of the goals set by council and the success or otherwise in achieving these goals. The annual report is a key performance report to the community and other stakeholders and, once approved by the council via its oversight report, must be placed on the municipal website. Copies must be sent to various authorities and it must be made available to the wider community.

The annual report requires the collection and consolidation of a range of financial and non-financial information about the municipality, whereas the annual financial statements and audit report are mostly financial. The annual report provides an authoritative record of the activities and performance of the municipality for each financial year. In time it will serve as a key historical record on each municipality, revealing the progress, growth and development of municipal services and performance.

Annual reports must be aligned with the planning documents and municipal budget for the year reported on. This means that the IDP, budget, SDBIP, in-year reports and annual report should have similar and consistent structures to facilitate understanding and to show the links between plans and actual performance.

The MFMA requires that the annual report of a municipality or municipal entity must

## **PART ELEVEN: Financial reports: councillors' tools for oversight**

include the following (unless otherwise stated, these requirements apply to all municipalities and municipal entities):

- the annual financial statements
- in addition, where a municipality has sole or effective control of a municipal entity, the consolidated annual financial statements
- the Auditor-General's audit report on the financial statements
- any explanations that may be necessary to clarify issues in connection with the financial statements
- an assessment by the accounting officer on any arrears on municipal taxes and service charges
- particulars of any corrective action taken or to be taken in response to issues raised in the audit reports
- other information as determined by the municipality or entity or as may be prescribed
- any recommendations of the audit committee.

The following provisions apply to municipalities only:

- the annual performance report of the municipality
- the Auditor-General's audit report on the municipality's performance report
- an assessment by the municipality's accounting officer on the municipality's performance against measurable performance objectives for revenue collection and for each vote; all relevant information on municipal entities
- the use of each conditional grant, including the details of spending. The Auditor-General will ensure that the audit process includes a proper assessment and reconciliation on all national grants received by a municipality
- the extent to which a municipality met the conditions of such grants
- the use of any donor funding support
- agreements, contracts and projects under private public partnerships
- service delivery performance on key services provided
- information on long-term contracts
- information technology and systems purchases and the effectiveness of these systems in the delivery of services and ensuring compliance.
- performance against its three-year capital budgets for addressing infrastructure backlogs
- list of all municipal entities, their purpose and disclosure of any financial contributions to and from the municipality are to be disclosed
- performance of municipal entities and municipal service providers.

Municipalities are encouraged to adopt the new reporting requirements as this will facilitate a more uniform sector wide approach. Further information on the content and

preparation of annual reports is provided in National Treasury MFMA circular number 11 of 2005.

### **What are the timelines for presenting the annual financial statements and annual report?**

#### ***Annual financial statements***

The annual financial statements must be completed and submitted to the Auditor-General within two months or by 31 August of each financial year.

A municipality which has sole control or effective control of a municipal entity in line with the meaning of the MSA must, in addition to preparing annual financial statements for the municipality, prepare consolidated annual financial statements incorporating the annual financial statements of the municipality and municipal entity. The consolidated annual financial statements must be completed and submitted to the Auditor-General within three months or by 30 September of each financial year. This consolidation provides a holistic picture of all the municipal operations.

#### ***The annual report***

The accounting officer of a municipal entity, must, no later than 31 December each year, submit the annual report of the municipal entity for that financial year to the municipal manager of the parent municipality.

The municipal manager must then incorporate the relevant information into the municipality's annual report and provide the report to the mayor. The mayor of a municipality must, no later than 31 January, table in the municipal council the annual reports of the municipality and of all municipal entity under the municipality's sole or shared control.

If the mayor, for whatever reason, is unable to table in the council the annual report of the municipality, or any municipal entity under the municipality's sole or shared control, within seven months after the end of the financial year to which the report relates, the mayor must promptly submit to the council a written explanation setting out the reasons for the delay, together with any components of the annual report that may be ready.

Immediately after the municipality's or municipal entity's annual report is tabled in the council, the accounting officer of the municipality must make public the annual report. He or she must also invite the local community to submit comments on the annual report; and submit the annual report to the Auditor-General, the relevant provincial treasury, National Treasury and the provincial department responsible for local government in the province.

### What is the oversight report?

The oversight report is the final major step in the annual reporting process of a municipality. Section 129 of the MFMA requires the council to consider the annual reports of its municipality and municipal entities and to adopt an oversight report containing the council's comments on each annual report.

The oversight report must include a statement on whether the council:

- has approved the annual report, with or without reservations
- has rejected the annual report
- has referred the annual report back for revision of those components that can be revised.

The oversight report is thus clearly distinguished from the annual report. The annual report is submitted to the council by the accounting officer and the mayor and is part of the process for discharging accountability by the executive and administration for their performance in achieving the goals set by council. The oversight report is a report of the municipal council and follows consideration and consultation on the annual report by the council itself. Thus the full accountability cycle is completed and the separation of powers is preserved to promote effective governance and accountability.

### *Managing the process and forming committees*

The processes for council oversight of the IDP, budget, annual report and preparing an oversight report may be complex for many councils, in particular where resources to support the functioning of the council are limited. For example, reviewing an annual report within full council meetings may not be practicable and may restrict the effectiveness of the analysis and discussions. Thus councils need to establish appropriate mechanisms to enable all councillors and the public to fully digest and discuss the annual report contents.

Once the annual report is tabled, the council effectively has two months in which to consider the report, invite public submissions and to finalise its oversight report. Given there are a number of steps and many stakeholders the review can be made more manageable if a committee process is established breaking it down into more easily managed parts.

It is recommended that councils consider the establishment of an oversight committee under sections 33 and 79 of the Municipal Structures Act 1998. This committee and, if needed, sub-committees, could be responsible for the detailed analysis and review of the annual report and then drafting an oversight report that may be taken to full council for discussion. Such a committee may receive and review representations made by the public and also seek inputs from other councillors and council portfolio committees.

## **PART ELEVEN: Financial reports: councillors' tools for oversight**

The oversight committee should be made up of only non-executive councillors and representatives of the community and can be formed each year to deal with the annual report. Municipal officials cannot be members of an oversight committee as this would pose a conflict of interest. Assistance from the municipality's audit committee in the review process is also recommended as a major source of independent specialist advice.

All meetings of council and the oversight committee at which an annual report is considered must be open to the public and a reasonable time must be allowed for discussion of any written submissions received and for members of the community and organs of state to address the meetings. Representatives of the Auditor-General are entitled to attend and to speak at any meetings held to discuss the annual report. Timely notice of meetings should be given to enable representations to be made. Making representations to the oversight committee should not necessarily preclude representations by the same individuals to the full council as this promotes transparency in the process.

At the same time that the committee is analysing the report in detail, other councillors should also be conducting their own review of the report. This can include discussions with constituents, ward committees and ward representatives to encourage inputs and comments and to prepare for the full council meeting that considers the annual report and oversight report.

Questions raised with the administration by council or the committee may be taken on notice by the accounting officer and responses subsequently provided to the committee process. Ideally however, questions should be responded to immediately during the committee meetings to avoid delays. The top management team may assist the accounting officer if needed. If the executive or the accounting officer and administration are unable to respond immediately to questions raised at committee or council meetings, then the committee or council may rightfully conclude that the executive and administration have not performed satisfactorily and may not understand the report that they have tabled.

When enquiring on matters in the annual reports from municipal entities, issues of commercial confidence may arise. In such cases the council should make a judgement as to whether the information is essential to determine a conclusion on the annual report and whether it may be necessary to meet in private. Such a step must be taken with caution in order not to weaken the democratic and transparency objectives of the annual reporting process.

Municipalities should take into account all costs of the various mechanisms (oversight committee and other meetings) for reviewing the annual report and preparing an

oversight report. The cost needs to be balanced against the need for transparency, good governance practice and accountability, the capacity of the municipality and the need for an effective process within the time allowed.

### ***Timing considerations***

Note that no later than two months from the date of tabling, council must consider the annual report and adopt an oversight report. Also, the annual report must be made public immediately after it is tabled and the public invited to submit representations. To assist with this process a municipal finance management calendar will be published in the near future.

Councils are encouraged to effectively use the time permitted under the MFMA (two months from when the report is tabled) for consideration in order to achieve a quality and acceptable annual report and strive for approval of a report that meets the provisions of the MFMA and MSA. Municipalities are encouraged to review the report immediately after it has been tabled so that steps to obtain additional information and amendments can be taken to facilitate completion of the oversight report within the timetable provided. The process for consideration may involve an initial review and analysis that seeks inputs from the community, audit committee and the administration, to be followed by a further review of the report, additional information and representations received. When any additional information is required the administration should promptly provide this.

The MFMA provides that if all the components of the annual report are not completed on time, then those components that are available must be tabled and considered and a written explanation be submitted to council stating why components are delayed and when they will be tabled. In such cases, an oversight report may be completed and the report approved, but this should be with reservations or referred back for completion when the missing components are tabled, no more than two months later. In any case, the components that have been tabled must be published and open for public representations and, where required, the oversight report amended when the remaining components are tabled.

### ***Understanding the annual report and determining conclusions***

A mechanism that facilitates better understanding of the annual report by all councillors is essential, as the MFMA requires that council, and not the executive or administration, comment on the annual report and arrive at a decision.

To facilitate consideration of the annual report in its entirety, the council should obtain the views of the audit committee. The audit committee is charged with providing council with, among other matters as prescribed, an authoritative and credible view of

the financial position of the municipality or entity, its efficiency and effectiveness, performance management and the level of compliance with the MFMA, DoRA and other relevant legislation.

In order to approve the annual report without reservations, council should be able to agree that the information contained in the report is a fair and reasonable record of the performance of the municipality and properly accounts for the actions of the municipality in the financial year reported upon. Approval means that the executive and administration have discharged in full, their accountability for decisions and actions and that their performance meets the criteria set by performance objectives and measures and is also acceptable to the community.

If the council has reservations on any matter in the report then these reservations should be outlined in the oversight report and the executive and administration should address these as determined by council.

A conclusion that the report is approved without reservations is the preferred outcome from the process. However, this conclusion should not be an outcome of only cursory examination of the report but should be as a result of a rigorous analysis by councillors with inputs from the public and other stakeholders.

Although the accounting officer is required to attend all meetings where the report is discussed to respond to questions, it is incumbent on all councillors to fully understand the report in order to identify matters that may require further information from the accounting officer.

### ***Staff performance bonuses***

To promote continuous improvement in the performance of the municipality and entities, it is strongly recommended that council reward performance in a manner that is commensurate with achievement of policy outcomes. Therefore, the payment of performance bonuses should be measurable with the extent of outcomes achieved. In some instances, performance bonuses were paid even though performance could not be measured. If the level of acceptance cannot be achieved then it follows that the performance of the administration has not met the objectives approved in the IDP, budget and SDBIPs. Where there are reservations, the seriousness of these should be taken into account before considering any part-payment of bonuses.

### ***Municipal entities***

Where municipalities have one or more municipal entities, separate annual reports from the municipality and each of the entities will be tabled in council. Only the annual financial statements will be consolidated in the municipality report. Although each of

the annual reports is to be considered by council, it would be impractical to complete multiple oversight reports. It is recommended that council adopt one oversight report that provides comments on each of the annual reports. In this way, council is able to reinforce the important linkages between the municipality and its entities, their close interrelationship in the provision of services and that performance of the municipality is an outcome of performance by the municipal administration and all the entities.

### **Summary - Reporting to enable oversight by councillors**

Councillors will be required to use, understand and review financial statements, audit reports and annual reports in discharging their oversight role over municipalities and municipal entities. The new approach to municipal financial management places increased importance on oversight and accountability for the executive mayor or committee and all non-executive councillors.

These reforms, if properly implemented, will ensure timely in-year reports that provide up-to-date performance and financial information, and will assist councillors in policy making. Executive mayors or committees, non-executive councillors and other public office bearers and officials will be able to be accountable for municipal service delivery. With this new level of accountability, elected public officer bearers, residents, taxpayers and users of municipal services will be able to monitor whether public services are being delivered effectively and efficiently.

In order to be properly accountable and oversee municipal programmes and services, councillors must determine how well these programmes and services are being delivered to their constituents. Councillors, board members, public office bearers and officials will need to measure service delivery. This is accomplished by a framework of financial and non-financial reporting on the achievement of performance measures established in the budget and the SDBIP.



## **PART TWELVE**

### **The audit committee and internal audit unit**

#### **What is an audit committee and what are its functions?**

The MFMA requires each municipality and each municipal entity to have an audit committee.

A single audit committee may be established for a district municipality and the local municipalities within that district municipality, or for a municipality and any municipal entities under its sole control.

The audit committee must consist of at least three persons with appropriate knowledge and experience. The majority of the members of the audit committee may not be in the employ of the municipality or municipal entity, although some municipal staff may be assigned to provide administrative support to the committee. The members of the audit committee are appointed by the municipal council or by the council of the parent municipality in the case of a municipal entity. One of the members who is not in the employ of the municipality or municipal entity must be appointed as the chairperson of the committee. No councillor or member of the board of directors of a municipal entity may be appointed to the audit committee.

An audit committee is an independent advisory body, which must advise the municipal council or the board of directors of a municipal entity, on matters relating to:

- internal financial control and internal audits
- risk management
- accounting policies
- the adequacy, reliability and accuracy of financial reporting and information
- performance management
- effective governance
- compliance with the MFMA, DoRA and any other applicable legislation
- performance evaluation
- any other issues referred to it by the municipality or municipal entity.

The audit committee should meet as often as is required to perform its functions, but at least four times a year. In addition to the above, the audit committee has the following responsibilities every financial year:

- review the annual financial statements to provide an authoritative and credible view of the financial position of the municipality or municipal entity, its efficiency and effectiveness and its overall level of compliance with the MFMA, DoRA and other applicable legislation

## PART TWELVE: The audit committee and internal audit unit

- respond to the council on any issues raised by the Auditor-General in the audit report
- carry out investigations into the financial affairs of the municipality or municipal entity as the council of the municipality, or parent municipality or the board of directors of a municipal entity, may request
- perform any other functions as may be prescribed
- advise council during the consideration of the annual report and preparation of the oversight report.

In carrying out its responsibilities, an audit committee must have access to the financial records and other relevant information of the municipality or municipal entity. The audit committee must receive and review reports of the internal audit unit of the municipality. The audit committee must also liaise with the person designated by the Auditor-General to audit the financial statements of the municipality or municipal entity.

### **What is the role of the internal audit unit?**

The MFMA requires each municipality and each municipal entity to have an internal audit unit. The internal audit unit should be established as an independent section within the council that takes direction from and provides support to the audit committee and municipal manager/ accounting officer. It is generally established with the appointment of professional internal audit staff as employees of council, although small and medium-sized councils may choose to share the function with the district and other municipalities. The internal audit function may be outsourced if the municipality or municipal entity needs help with developing its internal capacity and the council of the municipality or the board of directors of the entity has determined that this is feasible or cost effective.

Internal audit functions can be divided into the following key areas:

- prepare a risk based audit plan and an internal audit programme for each financial year
- advise the accounting officer and report to the audit committee on the implementation of the internal audit plan and matters relating to:
  - the internal audit
  - internal controls
  - accounting procedures and practices
  - risk and risk management
  - performance management
  - loss control
  - compliance with the MFMA, DoRA and any other applicable legislation

## PART TWELVE: The audit committee and internal audit unit

- examine and review the reliability and integrity of financial and operating information and the means used to identify, measure, classify and report this information
- examine and review the systems established to ensure compliance with policies, plans, procedures, laws, regulations and contracts that could have an impact on the overall operations and reporting of the council
- examine and review the system of internal controls for safeguarding assets of the municipality
- periodically verify the existence of property and equipment assets of the municipality
- evaluate the economy and efficiency with which the municipality has utilised resources
- review the operations and programmes of the municipality to ascertain whether the results are consistent with established goals and objectives
- evaluate the extent of compliance and reliability of performance management systems as required by the MFMA, and ensure that annual performance agreements are evaluated at the end of each financial year
- perform investigations into financial problems of the municipality or municipal entity, based on circumstances encountered during internal audit reviews or as requested by the audit committee or management
- perform such other duties as may be assigned to it by the accounting officer.

In order to conduct its affairs, the head of the internal audit function should have sufficient authority that will allow:

- unrestricted access to all functions, records, property and council staff
- full and uninhibited access to the audit committee
- adequate resources to carry out its functions
- autonomous application of the internal audit function including the scope of work and application of techniques as required
- assistance from staff in areas where internal audits are being performed.

Generally, the internal audit function should not be allowed to:

- perform operational duties within the municipality
- initiate or approve any financial transaction external to the internal audit function.

The head of the internal audit function is accountable to the audit committee and municipal manager and should report regularly on the following:

- an assessment of the adequacy and effectiveness of internal control processes and risk management

- significant issues relating to such controls, including potential improvements to established structures
- the status of the annual internal audit plan in relation to other particular milestones.

### What is an internal control system?

An internal control system deals with the management of risk within a municipality, often grouped into managerial, financial, operational and strategic systems, and which use specific risk prevention strategies. Some of the key elements of internal control systems include:

- policies, procedures, plans and objectives
- legislation
- budgetary systems
- organisational structures
- management review
- personnel arrangements
- staff supervision and performance review
- segregation of duties
- authorisations and approvals
- physical safeguards
- accounting systems
- information systems.

Internal control systems are established to help management ensure that transactions are checked, verified, reviewed, monitored and recorded with accuracy to reduce exposure to risk, thus contributing to a reasonable assurance of internal control. Physical checks at council premises by the internal audit staff will ensure that well crafted policy is practically applied.

Some typical internal controls that are established include:

- the review and reconciliation of designated financial records
- monitoring of cash and inventory levels
- checking or validation procedures for the accuracy of arithmetical calculation
- access to and security over cash and other negotiable instruments
- access to and security over assets and other resources
- actual to budget comparisons
- the writing off of bad and doubtful debts
- raising of debts, payment of accounts, payroll procedures
- separation of certain duties, such as cashiering and payment of accounts
- procedures for the dispatch of mail, and mail opening

## PART TWELVE: The audit committee and internal audit unit

- changes to computer programmes
- access to and security over information technology systems.

The overall reliability of an internal control system depends on the municipality's ability to regularly maintain and monitor its ongoing operation. This is an important aspect of effective internal control, and it will involve management conducting a number of additional tasks that include:

- creating and maintaining a management culture that emphasises internal control systems as an important priority within council's operations
- creating, maintaining, monitoring, and publishing internal control policies and procedures
- ensuring that all staff are aware of their respective roles and responsibilities in undertaking their own tasks of internal control, including induction and training
- investigating anomalies and breaches of internal control systems looking to reinforce such control processes
- reviewing internal control systems on a regular basis to take account of changing circumstances
- modifying internal control systems on a regular basis for new municipal functions or changes in structure

Internal control systems should be regularly and systematically reviewed. While the internal audit unit will generally initiate a review, the onus should be on the relevant manager of a particular area to ensure that the internal controls are always appropriate.

The internal audit function should keep comprehensive documentation on the regular review of internal control systems. The audit committee may wish to examine the documentation on internal control systems from time to time or it may seek a report from the internal audit function, as it requires.

### **Summary - Councillors' role in relation to the audit committee and internal audit unit**

The MFMA requires that every municipality and each municipal entity have an audit committee, internal audit unit and a system of internal control.

An audit committee is an independent advisory body that advises the council and staff on matters such as internal financial control and internal audit, risk management, accounting policy, performance management, effective governance, financial reporting and legislative compliance among other matters. The audit committee must consist of at least three persons, the majority of whom must not be in the employ of the municipality – no councillor may serve on the audit committee.

An internal audit unit should also be established within the municipality as an independent section that provides support to the audit committee to establish a risk based plan and internal audit programme, and to provide advice to the senior officials and the audit committee on internal controls, accounting procedures and policies, risk and risk management, legislative compliance, asset management and performance management amongst a range of other duties.

Municipalities may wish to establish their own audit committee, or participate in a joint audit committee with other nearby municipalities. In addition, municipalities may wish to outsource their internal audit function if considered feasible and cost effective.

The audit committee and internal audit function are important tools to help councillors in the oversight function. Councillors should be aware of the role of both units and should be in a position to monitor audit committee reports when they are presented to council.

## **PART THIRTEEN**

### **Forbidden activities and financial misconduct**

#### **What are the implications of forbidden activities for councillors and officials?**

The MFMA prohibits municipalities or municipal entities from the following:

- conducting any commercial activities -
  - except in the exercise of the powers and functions assigned it in terms of the Constitution or national or provincial legislation; or
  - outside the borders of the Republic
- providing a municipal service in an area outside its jurisdiction, except with the approval of the council of the municipality having jurisdiction in that area; or
- making loans to –
  - councillors or officials of the municipality
  - directors or officials of the entity
  - members of the public.

The MFMA further states that if a municipality or municipal entity, on 1 July 2004, is engaged in any activity prohibited by this section and which is otherwise lawful, the municipality or municipal entity must take all reasonable steps to rectify its position and to comply with that subsection as soon as may be reasonable in the circumstances.

National Treasury MFMA circular number 8 of 2004, relates to forbidden loans. The circular addresses calls from a number of municipalities for greater clarification of this section and what constitutes forbidden loans. The circular presents comments on the following:

- the implication of the section
- how it applies to specified types of borrowers
- what constitutes a loan -
  - loans to members of the public - provision of infrastructure
  - deferred payments on purchase of immovable property.
- situations where granting or taking up a loan is part of a broader agreement
- various common employment arrangements -
  - allowances
  - study schemes
  - housing schemes
  - transport schemes
  - advances on salary.

The circular also discusses reporting requirements of the activities mentioned above in the notes to the annual financial statements and annual reports.

Penalties for deliberate or negligent breach of the MFMA would constitute an act of financial misconduct. A municipality or entity is required to investigate allegations of financial misconduct and, where warranted, institute disciplinary proceedings.

### **What are the misconduct provisions that councillors should be aware of?**

The MFMA contains provisions for financial misconduct by officials and councillors, including the degree of responsibilities assigned to the municipal manager, accounting officer, chief financial officer and other officials of the municipality and municipal entities. These address the question of non-compliance with the MFMA; failure to perform a duty under the act; providing incorrect and misleading information; and making unauthorised, irregular and wasteful expenditure. The provisions require council to investigate such behaviour and institute disciplinary action.

The MFMA deals with criminal proceedings and sanctions applicable to financial misconduct for officials and councillors on matters relating to misleading information and being negligent in performing the basic functions of accounting officers' fiduciary responsibilities.

For councillors, any deliberate acts of influence over the accounting officer, the chief finance officer and other officials, including non-disclosure contravening the MFMA, its regulations or interfering in the financial management of the municipality or its entities constitutes an offence, which may lead to criminal proceedings.

### **Summary - The implications of forbidden activities and financial misconduct**

Certain activities are forbidden under the MFMA and constitute financial misconduct which could, where warranted, result in disciplinary proceedings being taken.

Deliberate acts of undue influence, interference, non-disclosure and negligence in performing fiduciary responsibilities that constitute financial misconduct could result in criminal proceedings.

Councillors should be aware of matters that constitute an offence under the MFMA or other legislation.

## **PART FOURTEEN**

### **Resolving financial problems**

The MFMA places the primary responsibility of avoiding, identifying and resolving financial problems on the municipality itself.

This means that the executive mayor or committee, council, municipal manager and senior officials must ensure that the municipality meets its financial commitments and works as a team to avoid financial problems. If a municipality encounters a serious financial problem or anticipates problems in meeting its financial commitments it must immediately:

- seek solutions for the problem
- notify the MECs for local government and finance in the province
- notify National Treasury
- notify SALGA.

#### **What happens if council fails to fulfil an executive obligation?**

A provincial intervention may be justified if a financial problem has been caused by or resulted in a failure by the municipality to comply with an executive obligation in terms of legislation or the Constitution. The MFMA provides for the province on becoming aware that there is a serious financial problem in a municipality, to promptly do the following:

- consult the mayor of the municipality to determine the facts
- assess the seriousness of the situation and the municipality's response to the situation
- determine whether the situation justifies a discretionary intervention or requires a mandatory intervention in terms of section 139 of the Constitution.

If by the start of the budget year (1 July), a municipal council has not approved an annual budget, including revenue-raising measures necessary to give effect to the budget, the provincial executive must intervene. The provincial executive must take any appropriate steps to ensure that a budget and/or revenue-raising measures are approved. The steps available to the provincial executive include dissolving the council and appointing an administrator until a newly elected council has been declared elected.

If the provincial executive dissolves a municipal council, a written notice must be submitted to the Minister for Provincial and Local Government, the provincial legislature and the National Council of Provinces. The dissolution takes effect 14 days from the date of the notice.

## PART FOURTEEN: Resolving financial problems

The provincial executive may approve a temporary budget and/or revenue-raising measures to provide for the continued functioning of the municipality. The appointed administrator may, with the approval of the provincial MEC for finance, withdraw funds from the municipal bank accounts in order to defray current and capital expenditure, but during any month may not exceed eight percent of the total amount allowed in the approved budget for the previous financial year. The limit must be scaled down proportionally if revenue flows are not at least at the level as the previous year or exceed the amount available. The funds withdrawn under a temporary budget must be considered a part of the subsequent annual budget approved for the budget year.

A mandatory provincial intervention is also necessary if a municipality, as a result of a crisis in its financial affairs, is in serious or persistent material breach of its obligations to provide basic services or to meet its financial commitments, or admits that it is unable to meet its obligations or financial commitments.

Under either of the above conditions, the provincial executive must promptly act to intervene in the municipality. Once the provincial executive determines that conditions exist for an intervention, the province must:

- assess the seriousness of the financial problem in the municipality
- seek solutions to resolve the financial problem in a way that would be sustainable and would build the municipality's capacity to manage its own financial affairs
- determine whether the financial problem, singly or in combination with other problems, is sufficiently serious or sustained that the municipality would benefit from a financial recovery plan and, if so, request the preparation of a financial recovery plan by a qualified person
- submit the financial recovery plan and recommendations to the MEC for finance and National Treasury
- consult with the mayor of the municipality to obtain the municipality's co-operation in resolving the financial problem, and if applicable, implementing the financial recovery plan.

The MEC must submit an assessment of the seriousness of the municipality's financial problems, stating whether a financial recovery plan is justified, and a copy of any request for the preparation of a recovery plan to the Minister for Provincial and Local Government, the provincial legislature, the National Council of Provinces, the municipality and National Treasury. A financial recovery plan can recommend changes to the municipality's budget and revenue raising measures, or any other measure that would provide a sustainable remedy to the municipality's financial problems.

### What are the criteria for determining the seriousness of financial problems?

When determining the seriousness of a financial problem the following factors, singly or in combination, may indicate the severity of the problem:

- the municipality has failed to make payments to a lender or investor when due
- the municipality has failed to meet a contractual obligation which provides security for its debts or other obligations
- the municipality has failed to make any other payment when due, which individually or in the aggregate is more than an amount as may be prescribed or, if none is prescribed, more than two per cent of the municipality's budgeted operating expenditure
- the actual current expenditure of the municipality has exceeded the sum of its actual current revenue plus available surpluses for at least two consecutive financial years
- the municipality had an operating deficit in excess of five per cent of revenue in the most recent financial year for which financial information is available
- the municipality's failure to meet its financial commitments has impacted, or is likely to impact on the availability or price of credit to other municipalities
- the municipality is more than 60 days late in submitting its annual financial statements to the Auditor-General
- the Auditor-General has withheld an opinion or issued a disclaimer due to inadequacies in the financial statements or records of the municipality, or has issued an opinion which identifies a serious financial problem in the municipality
- Any of the above factors exists in a municipality for which the municipality has sole control or has a responsibility for its debt and the municipality has failed to intervene effectively.

Any recurring or continuous failure by a municipality to meet its financial commitments, which substantially weakens the municipality's ability to procure goods, services or credit on usual commercial terms, may indicate that the municipality is in persistent material breach of its obligations to meet its financial commitments.

### How are financial recovery plans prepared?

Any suitably qualified person, on request by the provincial executive, may prepare a financial recovery plan for a discretionary provincial intervention. Only the Municipal Financial Recovery Service, located in National Treasury, may prepare a financial recovery plan for a mandatory intervention.

When preparing a financial recovery plan for a discretionary provincial intervention, the person requested to prepare the plan or the Municipal Financial Recovery Service must:

## PART FOURTEEN: Resolving financial problems

- consult with the relevant municipality; the municipality's principal suppliers and creditors, to the extent they can reasonably be contacted; the MEC for finance and the MEC for local government in the province; and organised labour
- take into account any financial recovery plan that has previously been prepared for the municipality; and any proposals for a financial recovery plan, that may be advanced by the municipality or any creditor of the municipality
- at least 14 days before finalising the plan submit the plan for comment to the municipality; the MEC for finance and the MEC for local government; SALGA; organised labour; and on request, to any supplier or creditor of the municipality
- publish a notice in a newspaper of general circulation in the municipality stating the place, including any website address, where copies of the plan will be available to the public free of charge or at a reasonable price; and inviting the local community to submit written comments in respect of the plan.

The person charged with preparing the financial recovery plan or the Municipal Financial Recovery Service must after considering any comments received from consultations mentioned above, finalise the financial recovery plan and submit it to the MEC for finance in the province for approval.

### **What does a financial recovery plan include?**

A financial recovery plan must be aimed at securing the municipality's ability to meet its obligations to provide basic services or its financial commitments. Such a plan, whether for a mandatory or discretionary intervention:

- must identify the financial problems of the municipality
- must be designed to place the municipality in a sound and sustainable financial condition as soon as possible
- must state the principal strategic objectives of the plan, and ways and means for achieving those objectives
- must set out a specific strategy for addressing the municipality's financial problems, including a strategy for reducing unnecessary expenditure and increasing the collection of revenue, as may be necessary
- must identify the human and financial resources needed to assist in resolving financial problems, and where those resources are proposed to come from
- must describe the anticipated timeframe for financial recovery, and milestones to be achieved
- must identify what actions are necessary for implementing the plan, distinguishing between actions to be taken by the municipality and actions to be taken by other parties
- may provide for the liquidation of specific assets, excluding those needed for the

## PART FOURTEEN: Resolving financial problems

- provision of the minimum level of basic municipal services
- may provide for debt restructuring or debt relief
- may provide for special measures to prevent unauthorised, irregular and fruitless and wasteful expenditures and other losses
- may identify any actual and potential revenue sources.

### **What must a parent municipality do if there are financial problems in a municipal entity?**

If a municipal entity experiences serious or persistent financial problems and the board of directors fails to act effectively, the parent municipality must either:

- take appropriate steps in terms of its rights and powers over that entity
- impose a financial recovery plan, which must meet the same criteria set out for a municipality
- liquidate or disestablish the entity.

### **Summary - Councillors' role in resolving financial problems**

The primary responsibility rests with each municipality to avoid, identify and resolve its own financial problems. Only when this fails will the provincial executive intervene using certain discretionary powers or mandatory powers should the situation become a crisis.

The resolution of financial problems may require the preparation of a recovery plan and the assistance of the Municipal Financial Recovery Service. Such a plan is aimed at reversing the crisis and re-establishing sustainable financial management. At all times, the municipality plays a vital role in the steps taken to recover from any financial problem.



## Conclusion

This guide provides a comprehensive description of the new roles and responsibilities of councillors in relation to municipal financial management. It examines the provisions of the MFMA and related finance legislation and discusses the contemporary best practice concepts necessary to improve municipal service delivery and provide best value for money for all municipalities.

It provides the context for local government management, by examining the Constitution and the system of governance in South Africa and how it relates to municipalities. The guide then goes on to explain the overall objectives of the MFMA, which is to modernise local government financial management, describing the actual processes required to reform municipalities whilst maintaining political and administrative accountability. Specific provisions of the MFMA, and related legislation such as the MSA, are discussed in detail. This covers areas such as management of assets, liabilities, revenue and expenditure, budgeting and strategic planning, service delivery, supply chain, financial reporting, audit and internal control and the resolution of financial problems.

The guide is developed to help councillors come to terms with their responsibilities and help them to develop a good understanding of recent finance legislation. A good understanding of these issues is essential for councillors to act effectively and in the best interests of their communities. It is essential reading for new and experienced councillors alike, and should be made readily available to anyone working in a municipality.

National Treasury and provincial treasuries, in the spirit of co-operative government, are committed to providing municipalities and their councillors with the necessary information to enable them to carry out their responsibilities effectively. A number of other guides and circulars are also available on the National Treasury website to help in this regard, at [www.treasury.gov.za/mfma](http://www.treasury.gov.za/mfma). Further questions on the MFMA can be directed to the National Treasury feedback line: [mfma@treasury.gov.za](mailto:mfma@treasury.gov.za).



## Annexure 1- Publications related to the Municipal Finance Management Act

Available on the National Treasury website (30 March 2006) [www.treasury.gov.za/mfma](http://www.treasury.gov.za/mfma)

### Legislation

Division of Revenue Acts

Local Government: Municipal Finance Management Act (No. 56 of 2003)

Local Government: Municipal Systems Act (No. 32 of 2000)

Local Government: Municipal Systems Amendment Act (No. 44 of 2003)

Local Government: Municipal Structures Act (No. 117 of 1998)

Local Government: Municipal Structures Amendment Act (No.33 of 2000)

Local Government: Municipal Property Rates Act (No. 6 of 2004)

Local Government: Municipal Demarcation Act (No. 27 of 1998)

Local Government: Transition Act Second Amendment Act (No. 97 of 1996)

Water Services Act (No. 108 of 1997)

Electricity Act (No. 41 of 1987)

Intergovernmental Fiscal Relations Act (No. 97 of 1997)

Intergovernmental Relations Framework Act (No. 13 of 2005)

The Constitution of the Republic of South Africa (No. 108 of 1996)

\* Policy framework for Municipal Borrowing and Financial Emergencies

### Regulations

Municipal Supply Chain Management Regulations – Gazette No. 27636,  
30 May 2005

Municipal Investment and Municipal PPP Regulations - Gazette No. 27431,  
1 April 2005

### Gazette Notices

Supply chain management exemption from regulation 44 – Gazette No. 28411  
and Condonation Notice, 18 January 2006

Additional allocations to provincial and local government 2005/06 -  
Gazette No. 28306, 7 December 2005

Exemptions from sections 117, 16(2) and SCM Regulations;

Repeal of Municipal Accountants Act - Gazette No. 27748, 30 June 2005

Exemptions from supply chain management provisions – Gazette No. 27044,  
1 December 2004

MFMA Delays and Exemptions - Gazette No. 26511, 1 July 2004

MFMA Implementation dates (Excel version available on request)

MFMA Commencement Dates - Gazette No. 26510, 25 June 2004

**Media Releases**

New tender procedures for municipalities – 5 June 2005

2004/05 local government budgets and selected outcomes – 1 September 2005

MFMA Launch – 1 July 2004

**Frequently Asked Questions**

FAQ Version 1 - 31 January 2005

**Circulars**

MFMA Circular No. 32 – The Oversight Report – 15 March 2006

MFMA Circular No. 31 – Budget Tabling and Adoption – 10 March 2006

MFMA Circular No. 30 – 2006 Division of Revenue Bill – 15 February 2006

MFMA Circular No. 29 – Supply Chain Management Issues – 31 January 2006

MFMA Circular No. 28 – Budget Content and Format – 2006/07 MTREF –  
12 December 2005

MFMA Circular No. 27 - Medium Term Budget Policy Statement 2005 -  
18 November 2005

MFMA Circular No. 26 - Long Term Borrowing - 1 November 2005

- Long Term Debt checklist and certification - information to be provided

MFMA Circular No. 25 - Supply Chain Management Guide and Bid Documents -  
3 October 2005

MFMA Circular No. 24 - Training - 29 September 2005

MFMA Circular No. 23 - Bulk Resources for Municipal Services - 9 September 2005

MFMA Circular No. 22 - Model Policy Supply Chain Management - 25 August 2005

- Model Policy - Supply Chain Management
- Municipal Code of Conduct - Municipal Supply Chain Management  
Role Players

MFMA Circular No. 21 - Disputes Between Organs of State - 25 August 2005

MFMA Circular No. 20 - Delegations - 12 August 2005

- Municipalities delegated by National Treasury to provinces

MFMA Circular No. 19 - Budget Process 2006/07 - 15 August 2005

- Schedule of Key Deadlines - Election year
- Budget Evaluation Checklist (BEC)
- Guidelines for completing the Budget Evaluation Checklist

MFMA Circular No. 18 - New Accounting Standards - 23 June 2005

- Municipality Capacity Categorisation
- Specimen Annual Financial Statements - June 2005
- Accounting Standards Implementation Guide - June 2005

MFMA Circular No. 17 - Qualifications and Training - 25 April 2005

## ANNEXURE 1

- MFMA Circular No. 16 - Supply Chain Management Training - 20 April 2005
- Annexure A - Supply Chain Management Training
- MFMA Circular No. 15 - Budget Submission 2005/06
- MFMA Circular No. 14 - 2005 Division of Revenue Bill and Municipal Budgets
- Division of Revenue Bill 2005
  - LG Conditional Grant Framework Allocations – Gazette Notice
  - Annexure A - LG Conditional Grant Framework
  - Annexure B - LG Recurrent Grants - Schedule 6 - Part 1.
  - Annexure B - LG Recurrent Grants - Schedule 6 - Part 2.
  - Annexure B - LG Infrastructure Grants - Schedule 4B 6A.
  - Annexure B - LG Indirect Grants - Schedule 7
  - Annexure B - LG Equitable Share - Schedule 3
  - Annexure B - LG Appendix to MIG - Schedule 4B
  - Annexure E - Frameworks and Allocations
  - Provincial Budgets - 2005/06
- Circular No. 13 - Service Delivery & Budget Implementation Plan - 31 January 2005
- Circular No. 12 - Definition of Vote in MFMA - 31 January 2005
- GFS Functions – Descriptions
  - GFS Functions – Explanation
  - GFS Functions - Functional Mapping Matrix
- MFMA Circular No. 11 - Annual Report Guidelines - 14 January 2005
- Annual Report Guidelines – Chapter 5: Functional Service Delivery Report
- MFMA Circular No. 10 - Budget Process 2005/06 - 8 October 2004
- Schedule of Key Deadlines – 06 October 2004
  - Budget Evaluation Checklist
- MFMA Circular No. 9 - Training - 6 October 2004
- MFMA Circular No. 8 - Forbidden Loans - 1 October 2004
- MFMA Circular No. 7 - MFMA Implementation Plan Template - 23 September 2004
- MFMA Implementation Plan Template - 23 September 2004
- MFMA Circular No. 6 - Workshops, Supply Chain Management - 13 September 2004
- MFMA Circular No. 5 - Twelve (12) Urgent Implementation Priorities - 8 September 2004
- MFMA Twelve (12) Urgent Implementation Priorities Checklist – 8 September 2004
  - Quarterly Return Form s178(2)(a) - Municipalities with corporate entities
  - Quarterly Return Form s178(2)(b) - Municipalities with public-private partnerships
  - Quarterly Return Form s178(2)(c) - Municipalities with long-term contracts
- MFMA Circular No. 4 - Specimen Annual Financial Statements - 2 September 2004
- MFMA Circular No. 3 - Supporting Materials - 31 August 2004

MFMA Circular No. 2 - Supply Chain Management - 21 July 2004  
MFMA Circular No. 1 - Introduction to the MFMA - 20 April 2004

### **Guidelines**

A Guide to Municipal Finance Management for Councillors – March 2006  
Introductory Guide to the MFMA, Updated Edition - August 2004  
Guide to the New Accounting Standards - May 2004  
Municipal Finance Management Intern Programme Guidelines – May 2004  
Draft Specimen Financial Statements – June 2005  
Supply Chain Management: A Guide for Accounting Officers of Municipalities and Municipal Entities – October 2005  
Application for Later Date of Effect or Reclassification of Capacity

### **Local Government Restructuring Grant**

Guidelines for the Disbursement of the LG Restructuring Grant, July 2000  
Memorandum of Agreement with Johannesburg Metropolitan Council  
Assessment of the Application from Johannesburg Metropolitan Council

### **Intergovernmental Fiscal Reviews**

1999 to 2005 IGFR Reports

### **Urban Development Zones**

Municipal Gazette Notices  
Municipal Urban Development Zone Maps

## Annexure 2- Activities relating to the next budget year

Dates	Mayor and Council / Entity Board	Administration – Municipality and Entity
July	<ul style="list-style-type: none"> <li>• Mayor leads review of previous year's budget process</li> <li>• Mayor leads planning for next budget process</li> </ul>	<ul style="list-style-type: none"> <li>• Assists with review and planning</li> </ul>
August	<ul style="list-style-type: none"> <li>• Mayor tables in council a time schedule outlining key deadlines for budget process</li> <li>• Mayor establishes committees and consultation forums for the budget process</li> </ul>	<ul style="list-style-type: none"> <li>• Assists with preparing schedule of key deadlines and establishing committees and consultation forums</li> </ul>
September	<ul style="list-style-type: none"> <li>• Through the IDP and budget-related policy review process, council sets strategic objectives and policies for service delivery and development</li> </ul>	<ul style="list-style-type: none"> <li>• Based on the strategic direction set in the reviewed IDP and budget-related policies, determines revenue and expenditure projections including levels for rates and tariffs. The Medium Term Budget Policy Statement for the municipality is produced (MTBPS)</li> <li>• Engages with national and provincial sector departments for alignment with municipal strategy</li> </ul>
October		<ul style="list-style-type: none"> <li>• Initial review of potential price movements of bulk resources</li> </ul>
November		<ul style="list-style-type: none"> <li>• Changes to IDP and budget-related policies as per the review process are incorporated in budget documentation</li> </ul>

## ANNEXURE 2

<b>Dates</b>	<b>Mayor and Council / Entity Board</b>	<b>Administration – Municipality and Entity</b>
December	<ul style="list-style-type: none"> <li>• Council finalises policies for rates, tariffs and other service charges</li> </ul>	<ul style="list-style-type: none"> <li>• Proposed budget and departmental SDBIPs are prepared, taking into account strategic direction, the municipal MTBPS and previous year's performance as per audited financial statements</li> </ul>
January	<ul style="list-style-type: none"> <li>• Entity board approves proposed budget and plans and submits to accounting officer of municipality</li> </ul>	<ul style="list-style-type: none"> <li>• Proposed national and provincial allocations incorporated into budget documentation</li> </ul>
February	<ul style="list-style-type: none"> <li>• Council considers budgets and SDBIPs of entities and accepts or makes recommendations to entities</li> </ul>	<ul style="list-style-type: none"> <li>• Proposed budget and SDBIP submitted to mayor taking into account the mid-year review of the current year and any corrective measures proposed as part of an oversight report for the past year</li> <li>• District municipalities to notify local municipalities of projected allocations</li> </ul>
March	<ul style="list-style-type: none"> <li>• Entity board considers recommendations of municipal council and submits revised budget</li> <li>• Mayor tables to council for consultation purposes the budgets of the municipality and entities complete with all required documentation (resolutions etc)</li> </ul>	<ul style="list-style-type: none"> <li>• Tabled budget including all required documentation is published, submitted to organs of state as required and stakeholders invited to comment</li> <li>• Changes in prices for bulk resources reviewed subject to final date for communication by providers (March 15)</li> </ul>

## ANNEXURE 2

<b>Dates</b>	<b>Mayor and Council / Entity Board</b>	<b>Administration – Municipality and Entity</b>
April	<ul style="list-style-type: none"> <li>• Consultation with national and provincial treasuries and finalise sector plans</li> </ul>	<ul style="list-style-type: none"> <li>• Budget documentation revised taking into account consultation and results of the third quarterly review</li> </ul>
May	<ul style="list-style-type: none"> <li>• Public hearings on the budget and council debate</li> <li>• Mayor responds to submissions and tables amendments for consideration by council</li> <li>• Council considers approval of the budget at least 30 days prior to the start of the budget year</li> <li>• Entity board approves budget of entity at least 30 days prior to the start of the budget year taking into account any recommendations of the municipal council</li> </ul>	<ul style="list-style-type: none"> <li>• Final budget documentation prepared for consideration of approval by council</li> </ul>
June	<ul style="list-style-type: none"> <li>• Council approves annual budget before start of budget year</li> <li>• Mayor approves SDBIP and annual performance agreements of senior managers at the latest within 28 days of approval of the budget by council and preferably before the start of the budget year. These must be linked to each other and to measurable performance objectives approved in the budget</li> <li>• Mayor publishes SDBIP and annual performance agreements and provides to council and MEC for local government in the province</li> </ul>	<ul style="list-style-type: none"> <li>• Municipal and entity accounting officers publish approved budget and required supporting documentation immediately after approval</li> <li>• Municipal accounting officer submits to the mayor the SDBIP and annual performance agreements revised as per the approved budget no later than 14 days after approval of the budget</li> </ul>

### Annexure 3- Activities relating to the current budget year

Dates	Mayor and Council / Entity Board	Administration – Municipality and Entity
July	<ul style="list-style-type: none"> <li>• Mayor approves SDBIP and annual performance agreements if not already approved before the start of the budget year.</li> </ul>	<ul style="list-style-type: none"> <li>• Begins Implementing the budget</li> </ul>
August	<ul style="list-style-type: none"> <li>• Mayor reviews monthly reports for July and only reports to council if there are material deviations from the budget and SDBIP</li> </ul>	<ul style="list-style-type: none"> <li>• Entity accounting officers provide monthly reports for July to board and Accounting Officer of municipality no later than 7 working days after month end</li> <li>• Municipal accounting officer provides monthly reports (including reports of entities) for July to mayor and organs of state as required no later than 10 working days after month end</li> </ul>
September	<ul style="list-style-type: none"> <li>• Review of monthly reports for August</li> </ul>	<ul style="list-style-type: none"> <li>• Preparation of monthly reports for August</li> </ul>
October	<ul style="list-style-type: none"> <li>• Mayor reviews first quarter performance reports and tables to council</li> <li>• Council considers first quarter performance report and acts as necessary</li> </ul>	<ul style="list-style-type: none"> <li>• Entity accounting officers provide monthly reports for September to board and accounting officer of municipality no later than 7 working days after month end</li> <li>• Municipal accounting officer provides 1st quarter performance report (including reports of entities) to mayor and organs of state as required</li> </ul>

### ANNEXURE 3

<b>Dates</b>	<b>Mayor and Council / Entity Board</b>	<b>Administration – Municipality and Entity</b>
November	<ul style="list-style-type: none"> <li>• Review of monthly reports for October</li> </ul>	<ul style="list-style-type: none"> <li>• Preparation of monthly reports for October</li> </ul>
December	<ul style="list-style-type: none"> <li>• Review of monthly reports for November</li> </ul>	<ul style="list-style-type: none"> <li>• Preparation of monthly reports for November</li> </ul>
January	<ul style="list-style-type: none"> <li>• Mayor reviews mid year review reports and tables to council with recommendations regarding the need for an adjustments budget</li> <li>• Council considers mid year review and acts as necessary</li> </ul>	<ul style="list-style-type: none"> <li>• Entity accounting officers provide mid-year review reports to board and accounting officer of municipality</li> <li>• Municipal accounting officer provides mid-year review reports including reports of entities and recommendations regarding the need for an adjustment budget to mayor and organs of state as required</li> <li>• Results of mid-year review are fed into the next year budget process</li> </ul>
February	<ul style="list-style-type: none"> <li>• Review of monthly reports for January</li> </ul>	<ul style="list-style-type: none"> <li>• Preparation of monthly reports for January</li> </ul>
March	<ul style="list-style-type: none"> <li>• Review of monthly reports for February</li> </ul>	<ul style="list-style-type: none"> <li>• Preparation of monthly reports for February</li> </ul>
April	<ul style="list-style-type: none"> <li>• Review of quarterly reports for third quarter</li> </ul>	<ul style="list-style-type: none"> <li>• Preparation of quarterly reports for third quarter</li> <li>• Results of third quarter review fed into next year budget process</li> </ul>
May	<ul style="list-style-type: none"> <li>• Review of monthly reports for April</li> </ul>	<ul style="list-style-type: none"> <li>• Preparation of monthly reports for April</li> </ul>
June	<ul style="list-style-type: none"> <li>• Review of monthly reports for May</li> </ul>	<ul style="list-style-type: none"> <li>• Preparation of monthly reports for May</li> </ul>

### Annexure 4 - Activities relating to the past budget year

Dates	Mayor and Council / Entity Board	Administration – Municipality and Entity
July		<ul style="list-style-type: none"> <li>• Preparation of annual financial statements for municipality and entities commences</li> </ul>
August		<ul style="list-style-type: none"> <li>• Entity accounting officers submit annual financial statements to the municipal accounting officer and Auditor-General for audit</li> <li>• Municipal accounting officer submits annual financial statements to auditor general for audit</li> <li>• Municipal accounting officer leads preparation of consolidated annual financial statements</li> </ul>
September		<ul style="list-style-type: none"> <li>• Municipal accounting officer submits consolidated annual financial statements to Auditor-General for audit</li> </ul>
October		<ul style="list-style-type: none"> <li>• Unaudited figures fed into the first quarterly review for the current year.</li> </ul>
November		<ul style="list-style-type: none"> <li>• Audited annual financial statements and audit report of municipality and entities received from Auditor-General</li> </ul>

## ANNEXURE 4

<b>Dates</b>	<b>Mayor and Council / Entity Board</b>	<b>Administration – Municipality and Entity</b>
December		<ul style="list-style-type: none"> <li>• Audited consolidated annual financial statements and audit report received from Auditor-General</li> <li>• Municipal and entity accounting officers put plans in place to address issues raised in the audit reports</li> <li>• Entity accounting officers submit annual reports to municipal accounting officer</li> </ul>
January	<ul style="list-style-type: none"> <li>• Mayor tables in council the annual reports of the municipality and entities including the audited financial statements and audit report of each</li> </ul>	<ul style="list-style-type: none"> <li>• Immediately after tabling the municipal accounting officer publishes the annual reports and submits to Auditor-General, and organs of state as required</li> </ul>
February	<ul style="list-style-type: none"> <li>• Council conducts public hearings, debates issues and considers oversight report</li> </ul>	<ul style="list-style-type: none"> <li>• Municipal and entity accounting officers attend meetings to respond to questions and ensure copies of minutes of the meetings are submitted to the Auditor-General and organs of state as required</li> </ul>
March	<ul style="list-style-type: none"> <li>• Council adopts oversight report</li> </ul>	<ul style="list-style-type: none"> <li>• Municipal accounting officer publishes the oversight report within seven days of adoption</li> </ul>

