



## Municipal Budget Circular for the 2010/11 MTREF

This circular provides further guidance to municipalities and municipal entities for the preparation of their 2010/11 Budgets and Medium Term Revenue and Expenditure Framework (MTREF).

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**Given that the 2010 FIFA Soccer World Cup starts on 11 June 2010, municipalities are advised to finalise and adopt their 2010/11 Budgets and MTREF before this date.**

## 1 National priorities – doing more with existing resources

In his 2010 State of the Nation Address, the President signalled that government intends to:

- Deliver more and better services in a caring and efficient manner;
- Hold political office bearers and public servants accountable;
- Shift resources to new priorities;
- Move from debate to effective implementation and decisive action; and
- Work in partnership with communities, labour and business to achieve our shared objectives.

These objectives are directly relevant to municipalities. The challenge for each municipality is to do more within its existing resource envelope.

### 1.1 Efficient and effective public services

The national *Budget Review 2010* notes:

Over the next few years, government must deliver more services – and deliver them more efficiently – within a tight resource envelope. Achieving this objective requires a new way of working:

- The budget has been reprioritised so that money is moved from low-priority programmes to high-priority programmes.
- A performance culture where people are held accountable for their actions, accompanied by clear, measurable outcomes related to key development priorities.
- Government will manage growth in its consumption expenditure (wages, and goods and services) and obtain better value for money.
- Corruption, particularly in the tender system, will be uprooted.

Municipalities are encouraged to adopt similar stances on these issues. This is particularly important in the run-up to the local government elections. Mayors and councils need to remain focused on the effective delivery of core municipal services, and steer away from seeking to buy political support through patronage, ad hoc public relations projects, events or donations or any other action that is not consistent with the *Code of Conduct for Councillors* – as set out in the Municipal Systems Act 32 of 2000.

### 1.2 Municipalities' role in employment creation

The national *Budget Review 2010* notes:

Employment is central to human dignity, sustainable economic development and social cohesion. Creating jobs and increasing employment is South Africa's most critical objective.

While there are many policy options to consider, emphasis should be placed on removing the structural impediments to faster job growth. This means aligning real wage growth with productivity, speeding up regulatory reform to ensure that young and less-skilled workers can access the job market, and ensuring that further education and training programmes provide the real-world skills needed by public-

and private-sector employers. Public employment to support service delivery, and public works projects that draw in lower-skilled workers, will continue to play an important role. The issue of youth unemployment is imperative and needs to be confronted directly.

Chapter 12 of the *Local Government Budget and Expenditure Review 2008* analysed the extent to which municipalities were supporting job creation. It is noted that:

Many activities performed by municipalities lend themselves to providing job opportunities for low and unskilled labour. As indicated, municipalities face critical choices in this regard, whether to adopt capital intensive approaches or labour intensive approaches.... Anecdotal information suggests that generally municipalities are inclined to adopt capital intensive approaches. The mechanisation of grass cutting, street sweeping, ditch digging, road maintenance and a host of other activities points in this direction. Of course there is a balance between job creation, efficiency and cost. This needs to be managed and in each instance the appropriate technology for the task needs to be decided upon, with a bias towards labour intensive approaches. The challenge is to mainstream the labour intensive approaches that are being used in the EPWP projects into the normal way municipalities go about their business of delivering services.

Each municipality must explore how it can contribute to job creation when revising their IDPs and preparing their 2010/11 budgets. However, municipalities should not just employ more people without any reference to the level of staffing required to deliver effective services, and what is financially sustainable over the medium term. The municipality ought to focus on maximizing its contribution to job creation by:

- Ensuring that service delivery and capital project use labour intensive methods wherever appropriate;
- Ensuring that services providers use labour intensive approaches;
- Supporting labour intensive LED projects;
- Participating fully in the Extended Public Works Programme; and
- Implementing interns programmes to provide young people with on-the-job training.

### **1.3 Procurement reforms and fighting corruption**

Government is taking active steps to uproot the problem of corruption in all three spheres of government, particularly in the tender system. In this regard the national *Budget Review 2010* notes:

If government is not able to curb corruption in procurement processes, confidence in our democratic government will rapidly erode. Corruption is part of a broader problem associated with a narrow view of empowerment that has become more widespread. Empowerment is about building capabilities so that people can contribute to economic development and improve their lives and livelihoods, not about extracting large economic rents from government.

To reduce corruption and to lower the costs of procuring certain goods and services, government intends to reform the procurement system. Greater transparency (including electronic procurement systems), arms-length competitive tendering processes and providing greater certainty to industry about procurement pipelines will contribute to achieving better value for money. More centralised procurement arrangements will be adopted where this contributes to greater efficiency and transparency.

In addition, a supply chain compliance unit has been established in the National Treasury. It will investigate compliance with tender rules and procedures, and work with the Special Investigating Unit to investigate specific tenders where there is suspicion of corruption. Closer cooperation between the Special Investigating Unit, the South African Revenue Service, the Financial Intelligence Centre and the South African Police Service will hasten effective prosecution of people found to be defrauding government through the tender system. An inter-ministerial task team has been established to coordinate anti-corruption initiatives.

Municipalities are advised that the supply chain compliance unit will also be focusing on municipal procurement processes. Consequently, municipalities can expect requests for information relating to their tender committees and processes, as well as specific tenders and contracts.

#### 1.4 Additional allocations to local government

Government has again sought to insulate local government from the full impact of the slow down in national revenues. Direct transfers to local government grow by R23 billion over the medium term, of which R10.5 billion is additional to baseline. National transfers to local government grow by 13.4 per cent annually between 2009/10 and 2012/13, which is significantly higher than the average annual growth in total government expenditure of 8.8 per cent. Details of national transfers to local government are discussed in Chapter 9 of the national *Budget Review 2010* and in Annexure W1 to the 2010 Division of Revenue Bill. These documents are also available on National Treasury's website at: <http://www.treasury.gov.za/documents/national%20budget/2010/default.aspx>

## 2 Headline inflation forecasts

Municipalities must take the following inflation forecasts into consideration when preparing their budgets for 2010/11 and MTREF.

Fiscal year	2008/09 Actual	2009/10 Estimate	2010/11	2011/12 Forecast	2012/13
Headline CPI Inflation	9.9%	6.7%	5.7%	6.2%	5.9%

Source: *Budget Review 2010*

However, municipalities must also take into account the wage agreement SALGA concluded with municipal workers unions on 31 July 2009, comprising of a 10.5 per cent increase from 01 July 2009 and a 2.5 per cent non-pensionable allowance, which is pensionable from July 2010.

## 3 Revising rates, tariffs and other charges

When municipalities and municipal entities revise their rates, tariffs and other charges for their 2010/11 budgets and MTREF, they need to take into account the labour (i.e. the wage agreements with unions) and other input costs of services provided by the municipality or entity, the need to ensure financial sustainability, local economic conditions and the affordability of services, taking into consideration the municipality's indigent policy.

Municipalities should also take account of relevant policy developments in the different sectors.

In considering changes in property rates, municipalities need to take cognisance of local economic conditions such as the down turn in the property market, trends in household incomes and unemployment. Excessive increases in property rates and other tariffs are likely to be counterproductive, resulting in higher levels of non-payment and increased bad debts.

Municipalities must also explore imaginative ways of structuring the tariffs for utility services to encourage more efficient use of these services and to generate the resources required to fund the maintenance, renewal and expansion of the infrastructure required to provide the services.

National Treasury continues to encourage municipalities to keep increases in rates, tariffs and other charges as low as practically possible. For this reason National Treasury continues to require that municipalities must justify in their budget documentation all increases in excess of the 6 per cent upper boundary of the South African Reserve Bank's inflation target.

Municipalities should note that section 20 of the MFMA specifically empowers the Minister of Finance to take appropriate steps to ensure that municipalities do not materially and unreasonably prejudice national economic policies, particularly those on inflation, administered prices and equity.

### **3.1 Eskom bulk tariff increases**

NERSA has indicated that it will announce the revised bulk electricity pricing structure on 24 February 2010. National Treasury will circulate the decision as soon as it is available.

### **3.2 Water tariffs must be cost-reflective**

The national *Budget Review 2009* noted that:

Over the long term environmental considerations will affect the sustainability of growth. Government will promote efficient use of energy and water resources by producers and households, alongside measures to mitigate the effects of climate change. Prices that reflect economic cost and well-structured environmental taxes should provide incentives for efficiency improvements and new investment.

And, after noting the challenges with regards to electricity, it is noted that:

South Africa faces similar challenges with regard to water supply as demand growth outstrips supply. Better maintenance of infrastructure, new dam construction and cost-reflective tariffs will ensure that the supply challenges are managed in future.

Municipalities are, therefore, encouraged to review the level and structure of their water tariffs carefully, with a view to ensuring:

- Water tariffs are fully cost-reflective – including the cost of maintenance and renewal of purification plants and water networks, and the cost of new infrastructure;
- Water tariffs are structured to protect basic levels of service; and
- Water tariffs are designed to encourage efficient and sustainable consumption (e.g. through increasing block tariffs).

If a municipality's water tariffs are not fully cost reflective, the municipality should develop a pricing strategy to phase-in the necessary tariff increases in a manner that spreads the impact on consumers over a period of time. However, all municipalities should aim to have appropriately structured, cost-reflective water tariffs in place by 2014.

To mitigate the need for water tariff increases, municipalities must put in place an appropriate strategy to limit water losses to acceptable levels. In this regard municipalities must ensure that water used by its own operations is charged to the relevant service, and not simply attributed to water 'losses'.

### 3.3 Implementation of the Municipal Property Rates Act

The original four-year transitional period given to municipalities to implement the Municipal Property Rates Act (up to 1 July 2009) was extended by two years (up to 1 July 2011) through a legislative amendment to the Act in 2009 to allow those municipalities that had failed to implement new valuation rolls to continue to use existing valuation rolls and supplementary valuation rolls until 30 June 2011. The Department of Cooperative Governance and Traditional Affairs intends to introduce further amendments to the act to improve its implementation.

Municipalities are reminded that particular attention needs to be given to ensuring that the property rates charged to key economic sectors, such as agriculture, remain affordable.

The Department of Cooperative Governance and Traditional Affairs issued regulations, effective from 1 July 2009, that prescribe the rate ratio for the non-residential categories public service infrastructure and agricultural properties relative to residential properties. Processes are underway to also prescribe a ratio with respect to public benefit organisations relative to residential properties from 1 July 2010 as follows:

Categories	Ratio in relation to residential property
Residential property	1:1
Agricultural property	1:0.25
Public service infrastructure property	1:0.25
Public benefit organisation property	1:0.25

Note that the definition of 'public benefit organisation property' is limited to property owned by public benefit organisations and used for any specified public benefit activity listed in item (1) (welfare and humanitarian), item 2 (health care), and item 4 (education and development) of part 1 of the Ninth Schedule to the Income Tax Act.

### 3.4 Verification of existing municipal taxes

National Treasury has been implementing section 12 of the Municipal Fiscal Powers and Functions Act that deals with the verification of existing municipal taxes. The deadline for applications for the approval of existing municipal taxes was 7 September 2009. A total of 155 applications were received. In accordance with the procedure prescribed in the Act, National Treasury has notified the affected municipalities of the provisional recommendations on which municipal taxes may be continued and which taxes are unlikely to be approved. The Minister of Finance is currently consulting the Financial and Fiscal Commission, the Minister of Cooperative Governance and Traditional Affairs and affected municipalities to obtain their views and inputs. This process will be concluded through the issuing of regulations by the Minister of Finance during the latter part of 2010. It is however unlikely that these processes will be concluded before the start of the 2010/11 municipal budget year.

***Affected municipalities should, in the interim, use the provisional recommendation by the Minister of Finance on the taxes that existed prior to the Act to inform their 2010***

**Budgets and MTREFs.** Please note that existing municipal taxes that have not been approved by the Minister will lapse six months after notification by the Minister of Finance, and could accordingly have an impact on a municipal revenue budgets should any tax that existed prior to the Act not be approved.

Municipalities are also reminded to follow the appropriate application process set out in sections 5 and 6 of the Act prior to introducing any new municipal tax(es) as such tax(es) will only become legally enforceable after the Minister of Finance has approved such tax(es).

## 4 Funding choices and management issues

The national *Budget Review 2010* notes that the South African economy is slowly recovering, with economic growth of 2.3 per cent projected for 2010. However, it will take some time for the economic upturn to flow through to increased municipal revenues and better cash flows. Consequently, municipal revenues and cash flows are expected to remain under pressure in 2010/11 and so municipalities should adopt a conservative approach when projecting their expected revenues and cash receipts. Municipalities should also pay particular attention to managing all revenue and cash streams effectively, especially debtors.

Given the constraints on the revenue side, municipalities will again need to make some very tough decisions on the expenditure side this year. Priority ought to be given to:

- Ensuring that drinking water meets the required quality standards at all times;
- Protecting the poor from the worst impacts of the economic downturn;
- Supporting meaningful local economic development (LED) initiatives that foster micro and small business opportunities and job creation;
- Securing the health of their asset base (especially the municipality's revenue generating assets) by increasing spending on repairs and maintenance; and
- Expediting spending on capital projects that are funded by conditional grants.

Municipalities must pay special attention to controlling unnecessary spending on nice-to-have items and non-essential activities, such as foreign travel, councillor and staff perks, advertising and public relations activities. Attention should also be given to ensuring value for money is obtained when using consultancy and other outsourced services.

Municipalities must also ensure that their capital budgets reflect consistent efforts to address the backlogs in basic services and the refurbishment of existing network services.

### 4.1 Providing clean water and managing waste water

There are concerns about the quality of municipal drinking water and failures in the management of waste water. Municipalities must therefore include a section on '**Drinking water quality and waste water management**' in their 2010/11 budget document supporting information (we recommend it forms part of the section on *Measurable performance objectives and indicators* – section 12 of Schedule A). The section must set out the following information:

- Name of the Water Service Authority in the area and name of the Water Service Provider, and who actually manages the provision of drinking water and waste water management (if outsourced);
- The *Blue Drop* and *Green Drop* performance ratings (as determined by the Department

of Water Affairs) applicable to all water and waste water services within the municipality, highlighting areas that require attention;

- The current status of the municipality's *Water Safety Plan* and measures to be taken in 2010/11 and over the MTREF to implement it;
- A brief outline of problems that the municipality is experiencing with regards to the management of drinking water and sewerage;
- An outline of the steps the municipality needs to take to address the problems noted; and
- The 2010/11 budget and MTREF allocations proposed/made to fund the above measures.

Note the focus of this section must be on the quality of the functioning of existing services, and not deal with the extension of water and waste water services to households, which must be dealt with separately elsewhere in the budget document.

#### **4.2 Mayor's discretionary funds and similar discretionary budget allocations**

It has been observed that many municipal budgets contain sub-votes or allocations to "Mayoral Discretionary Funds", "Special Projects", "Special Events" or similar discretionary type funds.

National Treasury regards these types of allocations as a bad practice because:

- It is not clear how they are aligned to the constitutional requirement that municipalities structure their budgeting and planning processes to give priority to the basic needs of the community, and to promote the social and economic development of the community (see section 153(a) of the Constitution);
- They do not provide for the appropriation of funds for the purposes of a department or functional area of the municipality (see the definition of 'vote' in section 1 of the MFMA);
- They undermine the budget consultation processes since the intended use of the funds is not transparently reflected in the tabled budget; and
- There is a risk that they may be abused for personal gain or to improperly benefit another person or organisation.

Therefore National Treasury discourages allocations of this nature. Good budget practice requires that a municipal budget should transparently indicate the purposes and areas where municipal funds (i.e. public funds) are to be allocated. These kinds of discretionary funds immediately raise public suspicions of impropriety and corruption. In terms of section 52(a) of the MFMA the Mayor "must provide general political guidance over the fiscal and financial affairs of the municipality". The Mayor, therefore, provides direct input into the budget. If this is the case, why does the Mayor require a 'discretionary / personal slush fund'?

Section 17(3)(b) of the MFMA requires that when an annual budget is tabled it must be accompanied by "measurable performance objectives ... for each vote in the budget". What measurable performance objectives can be set in relation to these funds given that their use is at the discretion of the Mayor? This means the transparent and effective use of these funds cannot be monitored and assessed by the council and the public.

National Treasury notes that section 17(3)(j) of the MFMA requires that when an annual budget is tabled it must be accompanied by "particulars of any proposed allocations or grants by the municipality to ... (iv) any organisations or bodies referred to in section 67(1)". The aim of this provision is to ensure that all proposed allocations or grants are presented

transparently in the budget documentation that is tabled for public consultation and council approval, as well as for budget management and monitoring purposes. *Any allocations or grants made to organisations or bodies that are not reflected in a municipality's budget or adjustments budget must be regarded as unauthorised expenditure because they are "(f) a grant by the municipality otherwise than in accordance with this Act"* (see definition of unauthorised expenditure in section 1 of the MFMA).

National Treasury further notes that section 67 of the MFMA only allows funds to be transferred to 'an organisation or body' and not to an individual. *Any allocations or grants to individuals, other than in terms of the municipality's indigent policy or bursary scheme, must be regarded as irregular expenditure because they are expenditures not in accordance with a requirement of the MFMA.*

National Treasury and provincial treasuries will exercise close oversight of all discretionary type allocations in municipal budgets. If there are any concerns about the use of these funds, section 74 of the MFMA will be used to interrogate their use.

#### **4.3 Unallocated ward allocations**

It has been observed that certain municipalities provide for a 'bulk' Ward Allocation in their budgets. Then during the financial year projects are identified and funds are moved to other votes within the budget – where the funds get spent.

National Treasury does not regard this to be a good practice, because it means that the tabled budget does not reflect which ward projects are planned for purposes of public consultation and council approval. Instead the necessary plans and allocation decisions are made during the financial year and only go through an adjustments budget process - which does not require public consultation.

National Treasury therefore urges municipalities to allocate all Ward Allocations in their tabled and approved budgets, and then use the main adjustments budget in January/February to make any incremental adjustments deemed necessary for management purposes. This approach would greatly enhance transparency, force better planning of these projects and reduce the scope for corrupt practices influencing the choice of projects.

#### **4.4 New office buildings**

National Treasury has noted that a number of municipalities are contemplating building new offices to accommodate the municipal council, the municipality's main administration or both. Given the current economic conditions and the pressure this has placed on national and municipal revenues, as well as ongoing service delivery pressures, municipalities are urged to prioritise service delivery infrastructure in their capital budgets. National Treasury is also concerned that such projects will place upward pressure on tariffs and rates.

If a municipality plans to allocate funds to new projects to build or upgrade new office buildings in its 2010/11 budget and MTREF, the municipal manager must in terms of section 74 of the MFMA submit to National Treasury the following information:

1. A motivation as to why the proposed new office building is necessary;
2. A detailed costing of the proposed new office building;
3. An outline of how the project is to be financed; and
4. An overview of the service delivery infrastructure backlogs in the municipality.

The above information must be sent to Jan Hattingh (e-mail: [jan.hattingh@treasury.gov.za](mailto:jan.hattingh@treasury.gov.za)).

#### 4.5 Pledging of conditional grant transfers

The 2010 Division of Revenue Bill contains the following provision dealing with the use of conditional grant transfers as security for borrowing:

8(5) A municipality may only, after obtaining the approval of the National Treasury, pledge, offer as security or commit to a person or institution future conditional allocation transfers due to the municipality for the next financial year and the 2012/13 financial year, for the purpose of securing a loan or any other form of financial or other support from that person or institution.

This section, read together with section 48 of the MFMA, means that:

- A municipality may use future equitable share transfers as security for borrowing;
- A municipality may use conditional grant transfers due in the current financial year as security for bridging finance for projects that fall within the conditions of the relevant conditional grant; and
- A municipality may only use conditional grant transfers that may become due in the following two financial years as security for borrowing with the prior approval of the National Treasury.

The intention of this provision is to facilitate the implementation of capital projects financed by conditional transfers by allowing municipalities to use their indicative conditional allocations set out in the 2010 MTREF as security for bridging finance. Note that all the relevant procedures set out in Chapter 6 of the MFMA must still be followed in relation to these borrowings.

***The provision does not allow a municipality to commit conditional transfers beyond 30 June 2013. This means conditional transfers cannot be pledged as security for long term borrowing.***

When a municipality makes an application for approval in terms of section 8(5) of the 2010 Division of Revenue Act (if approved), National Treasury, in terms of section 74 of the MFMA, requires the following to be submitted:

1. A description of the project for which the finance is being raised;
2. A detailed costing of the project;
3. A project implementation plan, and a related cash-flow plan;
4. A detailed description of how the project is to be financed, showing:
  - a. Funding from the relevant conditional transfer;
  - b. Funding from public contributions and donations;
  - c. Funding from internally generated funds (own revenues), and
  - d. Funding from borrowing.
5. Name of the conditional transfer that is being used as security for the loan;
6. The percentage of the conditional transfer revenue stream that is being pledged;
7. A statement from the municipal manager setting out the reasons for pledging the conditional transfer, as opposed to other revenue streams of the municipality;
8. A statement from the person or institution making the loan indicating:
  - a. All the costs related to the loan; including origination costs, contracting fees and financing costs;
  - b. The value and period of the loan for which the pledge is being sought;
  - c. The interest rate on the loan for which the pledge is being sought;
  - d. The interest discount given to the municipality as a result of the conditional transfer being pledged to secure the loan;

- e. The time period over which the conditional grant revenue stream is being pledged;
- f. The percentage of the loan costs that the pledge covers; and
- g. Whether the municipality has given any other form of security for the loan.

All applications must be directed to Jan Hattingh (e-mail: [jan.hattingh@treasury.gov.za](mailto:jan.hattingh@treasury.gov.za)).

National Treasury undertakes to give municipalities a definitive answer to applications within 10 working days after receipt of all the abovementioned information. Should National Treasury deem it prudent to request further information from either the municipality or the person or institution making the loan, the above timeline will be extended accordingly.

When considering any application in terms of section 8(5), National Treasury will, among other things, take the following into consideration:

1. The borrowing must finance a project that complies fully with all the conditions set out in the conditional grant framework of the conditional transfer that is being pledged to secure the loan;
2. The period of the pledge may not extend beyond 30 June 2013;
3. The borrowing should ideally only finance 40 per cent of the total project cost;
4. Under normal circumstances, not more than 75 per cent of the indicative conditional transfer in the next financial year and the 2012/13 financial year should be pledged;
5. The municipality must derive a demonstrable benefit from the pledging arrangement; and
6. The cash-flow position of the municipality – if the municipality is already experiencing serious cash-flow problems this will automatically disqualify it from pledging future conditional transfers as security for borrowing, as there is a risk of the facility being abused.

To ensure that the purposes of conditional grants are not undermined by these pledging arrangements, the National Treasury requires that the pledging contract between the municipality and the person or institution making the loan must include the following clause:

XX. If the monies borrowed by the municipality in terms of this contract are used for any other purpose other than to finance the project specified in this loan agreement, then the pledge of any future conditional transfer as security for the loan is null and void, and the municipality must repay the loan from its own revenues.

#### **4.6 Virement policies of municipalities**

The MFMA and the Municipal Budget and Reporting Regulations seek to move municipalities away from the traditional approach of appropriating/approving budgets by line item. The aim is to give the heads of municipal departments and programmes greater flexibility in managing their budgets. To further facilitate this, each municipality must put in place a council approved virements policy, which should provide clear guidance to managers of when they may shift funds between items, projects, programmes and votes.

The following principles must be incorporated into municipal virements policies:

1. Virements should not be permitted in relation to the revenue side of the budget;
2. Virements between votes should be permitted where the proposed shifts in funding facilitate sound risk and financial management (e.g. the management of central insurance funds and insurance claims from separate votes);
3. Virements from the capital budget to the operating budget should not be permitted;
4. Virements towards personnel expenditure should not be permitted;

5. Virements to or from the following items should not be permitted: bulk purchases; debt impairment, interest charges; depreciation, grants to individuals, revenue foregone, insurance and VAT;
6. Virements should not result in adding 'new' projects to the Capital Budget;
7. Virements of conditional grant funds to purposes outside of that specified in the relevant conditional grant framework must not be permitted; and
8. There should be prudent limits on the amount of funds that may be moved to and from votes and sub-votes (e.g. not more than 5 per cent of the budget may be moved to or from a vote, programme, project etc.).

The policy must also indicate how the virements process is to be managed within the municipality so as to enable the tracking and reporting of funding shifts.

## 5 Conditional transfers to municipalities

Section 216 of the Constitution provides for national government to transfer resources to municipalities in terms of the annual Division of Revenue Act (DoRA) to assist them in exercising their powers and performing their functions. These allocations are announced annually in the national budget. Transfers to municipalities from national government are supplemented with transfers from provincial government. Further, transfers are also made between district municipalities and local municipalities.

It is important that all these transfers are made transparently, and properly captured in municipalities' budgets. In this regard, regulation 10 of the Municipal Budget and Reporting Regulations provides guidance on when municipalities should reflect a transfer on their budgets.

In support of this regulation, the 2010 Division of Revenue Bill provides that –

- In terms of section 14, National Treasury is required to publish in the Government Gazette the allocations or indicative allocations for all national grants to municipalities;
- In terms of section 29, each provincial treasury is required to publish in the Government Gazette the indicative allocation per municipality for every allocation to be made by the province to municipalities from the province's own funds; and
- In terms of section 28, each category C municipality must indicate in its budget all allocations from its equitable share and conditional allocations to be transferred to each category B municipality within the category C municipality's area of jurisdiction.

The Government Gazette reflecting the allocations and indicative allocations for all national grants to municipalities is available at:

<http://www.treasury.gov.za/legislation/bills/2010/>

In addition, National Treasury publishes a payment schedule that sets out exactly when equitable share and national conditional grant funds are to be transferred to municipalities:

[http://www.treasury.gov.za/legislation/mfma/media\\_releases/Municipal%20Payment%20Schedule/](http://www.treasury.gov.za/legislation/mfma/media_releases/Municipal%20Payment%20Schedule/)

The payment schedules that provincial treasuries are required to submit to National Treasury in terms of section 29(6) of the Division of Revenue Bill 2010, will be published on National Treasury's website, along with the national payment schedule.

### 5.1 Responsibilities of transferring and receiving authorities

The legal obligations placed on transferring and receiving officers in terms of the 2010 Division of Revenue Bill are very similar to previous requirements. National Treasury intends ensuring strict compliance in order to improve spending levels, and the quality of information relating to the management of conditional grants.

Municipalities are again reminded that compliance with the annual Division of Revenue Act is the responsibility of the municipal manager as the “receiving officer. The municipal manager is responsible for, among other things, the tabling of monthly reports in council on whether or not the municipality is complying with the Division of Revenue Act. He/she is also responsible for reporting on any delays in the transfer or the withholding of funds. *Failure on the part of a municipal manager to comply with the Act will have financial implications for the municipality as it will lead to the municipality losing revenue when funds are stopped and reallocated.*

Where the municipality is unable to comply, or requires an extension, the municipal manager must apply to the National Treasury and provide comprehensive motivation for the non-compliance.

### 5.2 Unspent conditional grant funds for 2005/06 to 2008/09

MFMA Budget Circular 48 officially initiated the process of enforcing the provisions that have appeared in each annual Division of Revenue Act since 2005 that deal with conditional grants that remain unspent at the end of the financial year.

After an extensive verification process, and giving municipalities an opportunity to prove that their unspent allocations had been spent (in accordance with the relevant grant conditions) or were committed to identifiable projects, National Treasury sent letters on 29 June 2009 (in respect of unspent conditional grants for 2005/06 to 2007/08) and 28 October 2009 (in respect of unspent conditional grants for 2008/09) to each of the affected municipalities instructing them to repay the outstanding balance of unspent conditional grant funds to the National Revenue Fund, and indicating that if they failed to do so, the amount they owed would be offset against their next equitable share transfer due on 30 November 2009.

A number of municipalities did repay their unspent conditional funds to the National Revenue Fund. However, the majority chose to ignore the matter, and it was only when National Treasury gave effect to the offset that they began to take the matter seriously. This resulted in the leadership of numerous municipalities meeting with National Treasury with a view to making more favourable arrangements for the repayment of the funds they owed the National Revenue Fund. In nearly all instances these municipalities have been accommodated, and either a portion or the entire amount of the offset funds was paid out to the municipalities concerned. Processes are currently underway to conclude agreements with each of these municipalities in terms of which they will return their unspent conditional grant funds from the years 2005/06 to 2008/09 to the National Revenue Fund.

National Treasury is managing the process for the 2005/06 to 2008/09 financial years in terms of section 35(2) of the Division of Revenue Act, No 12 of 2009, as the failure of the municipalities to return unspent conditional grant funds to the National Revenue Fund in accordance with the law amounts to financial mismanagement.

### 5.3 Unspent conditional grant funds for 2009/10

To bring legal certainty to the process of managing unspent conditional grant funds, the 2010 Division of Revenue Bill contains the following provisions:

#### Unspent conditional allocations

20. (1) Despite the provisions of the Public Finance Management Act or the Municipal Finance Management Act relating to roll-overs, any conditional

allocation, excluding the Gautrain Rapid Rail Link Grant and the Expanded Public Works Programme Incentive Grant, that is, in the case of a province, not spent at the end of a financial year or, in the case of a municipality, at the end of a municipal financial year, reverts to the National Revenue Fund, unless the relevant receiving officer can prove to the satisfaction of the National Treasury that the unspent allocation is committed to identifiable projects.

(2) The National Treasury may, at the request of a transferring national officer, provincial treasury or municipality, approve—

(a) a roll-over from a conditional allocation to the next financial year; and

(b) spending of a portion of a conditional allocation on activities related to the purpose of that allocation, where the province or municipality projects significant unforeseeable and unavoidable over-spending on its budget.

(3) Any funds which must revert to the National Revenue Fund in terms of subsection (1), and which have not been approved by the National Treasury to be retained in terms of subsection (2), must be repaid to the National Revenue Fund.

(4) The National Treasury, in accordance with subsection (5), may set-off any funds which must be repaid to the National Revenue Fund in terms of subsections (1) and (3), but which have not been repaid—

(a) in the case of a province, against future conditional grant allocations to that province; and

(b) in the case of a municipality, against future equitable share or conditional grant allocations to that municipality.

(5) Prior to the National Treasury offsetting any amounts against allocations to provinces or municipalities in terms of subsection (4), the National Treasury must give the relevant transferring national officer, province or municipality—

(a) written notice of the intention to set-off amounts against upcoming allocations; and

(b) an opportunity, within 14 days of receipt of the notice referred to in paragraph (a), to—

(i) submit written representations that prove to the satisfaction of the National Treasury that the unspent allocation was either spent in accordance with the relevant framework, or is committed to identifiable projects;

(ii) propose alternative means acceptable to the National Treasury by which the unspent allocations can be repaid to the National Revenue Fund; and

(iii) propose an alternative payment schedule in terms of which the unspent allocations will be repaid to the National Revenue Fund.

(6) A notice contemplated in subsection (5) must include the intended amount to be set-off against allocations, and the reasons for offsetting the amounts.

(7) Despite anything else contained within this section, the retention of funds which should revert to the National Revenue Fund in terms of subsection (1) and (3), and which have not been approved by the National Treasury to be retained in terms of subsection (2), constitutes financial misconduct in terms of section 34.

The process to ensure the return of unspent conditional grants for the 2009/10 financial year will be managed in accordance with section 20 set out above. The following practical arrangements will apply –

- When preparing their annual financial statements a municipality must determine what portion of each national conditional allocation it received remained unspent as at 30 June 2010.
- National Treasury will initiate the process outlined in section 20(4) and (5) of the Division of Revenue Act on 2 August 2010 based on the June 2010 conditional grant

expenditure reports. If the receiving officer wants to motivate in terms of section 20(5)(b) that the funds have been spent or are committed to identifiable projects or wants to propose an alternative payment method or schedule the required information must be submitted to National Treasury by 16 August 2010.

- National Treasury will confirm in writing whether or not the municipality may retain as a rollover any of the unspent funds because they are committed to identifiable projects or whether it has agreed to any alternative payment methods or schedules by 30 September 2010.
- A municipality must return the remaining unspent conditional grant funds that are not subject of a specific repayment agreement with National Treasury to the National Revenue Fund by 15 October 2010. Failure to return these unspent funds by this date will constitute financial misconduct in terms of section 20(7) of the Division of Revenue Act.
- Any unspent conditional grant funds that should have been repaid to the National Revenue Fund by 15 October 2010 will be offset against the municipality's November equitable share allocation.

When applying to retain unspent conditional allocations committed to identifiable projects or requesting a rollover in terms of section 20(2) of the Division of Revenue Act, municipalities must supply National Treasury with the following information –

1. Details of each of the projects to which funds are committed;
2. A progress report on the state of implementation of each of the projects;
3. The amount of funds committed to each project, and the conditional allocation from which the funds come from; and
4. An indication of the time-period within which the funds are to be spent.

All the calculations of the amounts to be surrendered to the National Revenue Fund (NRF) will be subject to scrutiny by the Office of the Auditor-General and therefore will be audited.

#### **5.4 Appropriation of conditional grants that are rolled over**

Municipalities may not rollover unspent conditional grant spending in terms of section 28(2)(e) of the MFMA (read together with regulation 23(5) of the Municipal Budget and Reporting Regulations) because they are national/provincial funds. The applicable rollover process is that effected through the national/provincial adjustments budget in November each year.

This means that strictly speaking municipalities may not spend unspent conditional grants that have been rolled over in terms of the process described above, or that have been rolled over at the request of a transferring national officer until they are 're-appropriated' in a national adjustments budget passed by Parliament and then a municipal adjustments budget required in terms of section 28(2)(b) of the MFMA (read together with regulation 23(3) of the Municipal Budget and Reporting Regulations). However, this would imply delaying the spending of such funds until sometime after December each year.

Therefore National Treasury has determined the following:

- A municipality may proceed to spend any rollovers approved by the National Treasury in terms of section 20(2) and any unspent conditional grant funds that National Treasury approves as being committed to identifiable projects as soon as the municipality receives written approval in this regard from the National Treasury.
- A municipality that is allocated a rollover or given permission to retain unspent conditional grant funds must appropriate such funds in a municipal adjustments budget in terms of regulation 23(3) of the Municipal Budget and Reporting Regulations within

sixty days after the rollovers are gazetted in the annual Adjustments Estimate Government Gazette.

This process will minimize any delay in the spending of these funds, and provide formal approval for such funding to be spent.

### 5.5 Management and monitoring of conditional grants

To further improve the management and monitoring of conditional grants National Treasury will give special attention to the following matters:

- Municipalities must reflect all grants (from national, provincial and local) on both the revenue and the expenditure sides of their 2010/11 budgets, as well as for the MTREF;
- Monitoring that all funds transferred from national and provincial government are deposited in municipalities' primary bank accounts; and
- Monitoring that accounting officers (as receiving officers) fulfill their duties set out in sections 12 and 13 of the Division of Revenue Bill, particularly as they relate to the preparation and submission of information on conditional grants to the relevant national or provincial transferring officer, and to the relevant provincial treasury and National Treasury as part of their section 71 reporting obligations.

### 5.6 Other issues

Accounting treatment of conditional grants: Municipalities are reminded that in accordance with accrual accounting principles, conditional grants should only be treated as 'transfers recognized' revenue when the grant revenue has been 'earned' by incurring expenditure in accordance with the conditions of the grant.

VAT on conditional grants: SARS has issued a specific guide to assist municipalities meeting their VAT obligations – **VAT 419 Guide for Municipalities**. To assist municipalities accessing this guide it has been placed on the National Treasury website at:

<http://www.treasury.gov.za/legislation/mfma/guidelines/default.aspx>

Interest received and reclaimed VAT in respect of conditional grants: Municipalities are reminded that in MFMA Circular 48, National Treasury determined that:

- Interest received on conditional grant funds must be treated as 'own revenue' and its use by the municipality is not subject to any special conditions; and
- 'Reclaimed VAT' in respect of conditional grant expenditures must be treated as 'own revenue' and its use by the municipality is not subject to any special conditions.

## 6 The Municipal Budget and Reporting Regulations

The Municipal Budget and Reporting Regulations are designed to achieve a range of objectives, including improving the local government sphere's ability to deliver services by facilitating improved financial sustainability and better medium term planning. The regulations, formats and associated guides etc are available on National Treasury's website at:

[http://www.treasury.gov.za/legislation/mfma/reg\\_gaz/](http://www.treasury.gov.za/legislation/mfma/reg_gaz/)

Municipalities are reminded that the regulations applied to all municipalities and municipal entities as from 1 July 2009.

## 6.1 All municipalities must prepare budgets in accordance with the regulations

All municipalities must prepare budgets, adjustments budgets and in-year reports for the 2010/11 financial year in accordance with the Municipal Budget and Reporting Regulations. In this regard, municipalities must comply with both:

- The formats set out in Schedules A, B and C; and
- The relevant attachments to each of the Schedules (the Excel Formats).

The MFMA requires every municipality to table budget documents and budget tables before 1 April 2010 that comply with the regulations; and their budgets that are approved by council before 30 June 2010 must also comply with the regulations.

If a municipality fails to prepare its budget, adjustments budget and in-year reports in accordance with the relevant formats actions the National Treasury will take will include:

- The municipality will be required to resubmit their documentation in the regulated format by a date determined by the National Treasury;
- The municipality's non-compliance with the required formats will be reported to the Auditor-General; and
- A list of municipalities that fail to comply with the required formats will be tabled in Parliament and the provincial legislatures.

Note that all municipalities must use the Version 2.2 – 28 November 2009 – of the Excel Formats which is the latest and most advanced version of these formats. If a municipality does not submit its budget using this version, National Treasury will not accept it and the municipality will be deemed not to have submitted the budget information. The reason for insisting on a single version is to ensure comparability, to facilitate the process of aggregating the budgets and to expedite national and provincial consultation processes.

## 6.2 Application of regulations to municipal entities

All municipal entities that provide normal municipal type services (e.g. water, electricity, refuse removal, etc.) must comply with Chapter 3 of the Municipal Budget and Reporting Regulations.

Municipalities that have entities that must comply with Chapter 3 of the regulations must produce the **consolidated tables** prescribed in Schedule A of the regulations.

Municipalities that have entities that do not provide normal municipal services or where budgeted amounts are immaterial and only comprise of funds transferred from a municipality may apply to National Treasury for an exemption in respect of those entities. Applications must be sent to Jan Hattingh (e-mail: [jan.hattingh@treasury.gov.za](mailto:jan.hattingh@treasury.gov.za)) by 01 March 2010, and must include the following information:

- (a) the name of the entity;
- (b) a description of the ownership and governance arrangements of the entity;
- (c) details of the functions and services the entity delivers;
- (d) a copy of the entity's 2008/09 annual financial statements; and
- (e) a copy of the entity's 2009/10 annual budget.

National Treasury will inform municipalities in writing on the outcome of these applications by 15 March 2010.

### 6.3 Phasing in of formats and tables

National Treasury recognises that it will take time to achieve full compliance with both the letter and spirit of the new formats and tables for municipal budgets, adjustments budgets and in-year reports. To facilitate the phasing-in of the formats and tables the following guidance is given:

1. As a matter of principle, municipalities should seek to comply with the formats and tables as completely as practically possible. Where there are real technical difficulties these must be disclosed as footnotes to the relevant tables.
2. Where tables require 'current year' and 'audit outcome' all municipalities were required by Circular 48 to initiate projects to restate all historical information in line with the prescribed formats – ready for 2010/11 budget. Where this has not been done, it is important that the bottom line information is complete and reconciles to the audited results.
3. As regards completing Table A4, municipalities must place 'repairs and maintenance' under 'other expenditure' only if it cannot be allocated to component 'expenditure types' for the 2010/11 budget, but it must be allocated for the 2011/12 budget.
4. As regards completing Table A9, the 'Asset Register Summary' must be completed as far as information is available.
5. As regards Table A10, municipalities are advised to use the most recent data on demographic trends within the municipal area to determine the number of households to be serviced. This could include any comprehensive surveys undertaken by the municipality or other institutions such as StatsSA's 2007 Community Survey. The municipality should then project forward from there, based on what the municipality knows about on the extension of services that have taken place, or are planned. Municipalities should not underestimate the importance that government will place on this table in future as it provides key information on the roll-out of basic services, and whether targets are being achieved.
6. Municipalities should make an honest effort to fill out all the supporting tables as the information is critical to sound planning and budgeting.

### 6.4 Budgeting for revenue and 'revenue foregone'

The municipal budget must reflect all revenue anticipated to be received and recognised during the 2010/11 budget year and over the MTREF. All sources of revenue such as own revenue, grants, subsidies, agency receipts, donor funds, trust monies must be included.

The revenue amounts reflected in the financial performance budgets of the municipality must be net revenue (i.e. total revenue less revenue foregone).

#### Guidance on identifying revenue foregone:

While not entirely definitive, as each category should be assessed on a case-by case basis, it is suggested that municipalities apply the 'generally available to all' rule to determine whether an item is revenue foregone or expenditure (most often 'grant' expenditure). For example, if a rate rebate is available to all ratepayers of a particular category; e.g. residential land use, then the rebate should be treated as 'revenue foregone'. The broadly applied rebate is considered an adjustment to the tariff. However, if a rate rebate is provided to a particular ratepayer for charitable purposes this should be treated as expenditure and should be shown as a grant. Such a rebate to specific indigent households is an efficient way of collecting the property rates and then making an equivalent donation.

The new formats require that municipalities must disclose all revenue foregone on Supporting Table SA1. Note that revenue foregone must be distinguished from grant expenditures made in relation to the provision of, for instance, free basic services. These grant expenditures

must be detailed on Supporting Table SA21, and reflected as expenditure in the financial performance budget (Table A4) under 'transfers and grants'.

The key concept in the above explanation, is that a rates rebate that is 'generally available to all' is in practice *an adjustment to the rates tariff*, and so the revenue was never there to be collected (the revenue was foregone), and so should not be considered to be revenue in the first instance. This is why it is deducted on Table SA1 - and the net amount is reflected on Table A4. Note this net amount still includes rebates and exemptions of the type outlined in section 15(2) of the Municipal Property Rates Act (MPRA).

By contrast, a rebate or exemption provided to a ratepayer for any of the reasons set out in the section 15(2) of the MPRA would represent a grant for a charitable purpose and so should be treated as expenditure. In other words, the revenue was there to be collected, but the municipality chose not to collect it because it wanted to assist the ratepayer because they are poor, a pensioner or whatever other specific reason. The aim of this procedure is to obtain more reliable information on all benefits provided by local government to deserving groups of people.

The objective of this approach is also to ensure that the revenue reflected on Table A4 does not overstate the amount of revenue that is actually available to the municipality for collection - as a rebate generally available to all - was never realistically collectable.

### **6.5 Budgeting by GFS and 'internal charges'**

In all instances the definition of the GFS functions includes the costs incurred in the 'administration or support of ...' the specific function. This is consistent with the advice that National Treasury has given in respect of 'internal charges', namely when compiling the budgets by standard classification and by vote:

- Reflect the total cost of delivering the primary services before recharges to support functions are taken into account; and
- This may result in certain Votes or functions having very small budgets if their budgets are 'earned' by providing 'internal services' to other functions or Votes.

Note that the direction of recharges is from the primary function to the support function. This approach will facilitate the calculation of the full cost of services provided by the municipality.

### **6.6 Budgeting for Free Basic Services**

The equitable share is designed to compensate municipalities for providing free basic services to indigent households. Table A10 in the new formats requires the municipality to reflect the *cost of the free basic services* it is providing to households. Note that these costs are not equivalent to the expenditure on grants to individuals that are reflected on Supporting Table SA21 because certain of the services (such as the 6kl of water generally available to all) may be reflected as revenue foregone on Supporting Table SA1, while the amounts on Supporting Table SA 21 may reflect the revenue cost / expenditure and not the actual cost of providing the service. The focus here is on the actual cost to the municipality of providing the free basic service.

### **6.7 Prior year comparative information**

Section (1)(d)(ii) of the MFMA requires the presentation of the amounts of the 'preceding year' in the annual budget. The purpose is to provide historical trend information to assist the Council and the community to assess the proposed budget. These amounts should be aligned with the audited financial statements, or the latest corrected amounts if changes are made in the comparative amounts in the following years' audited financial statements.

## 6.8 2010/11 MTREF Funding Compliance Assessment

Municipalities are expected to prepare three-year budgets that are, among other things, sustainable in terms of being funded from realistically anticipated revenues to be collected. Consequently, municipalities must assess their revenue situation and financial health for purposes of determining whether or not they have sufficient revenue and adequate financial stability to fund and deliver on their proposed budgets. This is an explicit requirement of the MFMA.

In addition, municipalities are urged to objectively examine the credibility of their proposed budgets in terms of their spending and institutional capacity. For example, it makes no sense for a municipality to adopt an annual capital budget when it only has spending capacity to spend far less than the amount budgeted.

To enable municipalities to assess whether their budgets are funded in compliance with section 18 of the MFMA, National Treasury developed the Funding Compliance Assessment procedure, described in MFMA Circular 42 dated 30 March 2007. Further guidance is given in the *MFMA Funding Compliance Guideline*, which is available at:

<http://www.treasury.gov.za/legislation/mfma/guidelines/default.aspx>.

All municipalities must do a funding compliance assessment of their 2010/11 budgets in accordance with the guidance given in MFMA Circular 42 and the *MFMA Funding Compliance Guideline* before tabling their budget, and where necessary rework their budget to comply so that they table a properly funded budget.

In this regard, and acting in terms of section 74 of the MFMA, National Treasury requests all municipalities to submit the following information along with their 2010/11 budgets:

- Supporting Table SA10 of the new formats;
- A narrative assessment of each of the funding compliance variables noted in the *MFMA Funding Compliance Guideline*; and
- An indication of any steps the municipality took in preparing its 2009/10 budget in response to its funding compliance assessment in order to ensure better compliance with section 18 of the MFMA.

National Treasury and / or the relevant provincial treasury will independently assess the funding compliance of each municipality's budget and compare the results to the self assessments done by the municipality.

In terms of the Constitution and Section 5 of the MFMA, the National Treasury and provincial treasuries will exercise their oversight roles by referring back to municipalities those budgets that are not funded in accordance with the MFMA.

## 7 Budget process and submissions for the 2010/11 MTREF

Over the past number of years there have been significant improvements in municipal budget processes. Municipalities are encouraged to continue their efforts to improve their budget processes based on the guidance provided in MFMA Circulars 10, 19, 28 and 31 as well as the new regulations.

Once more, municipalities are reminded that the IDP review process and the budget process should be combined into a single process.

## 7.1 Submitting budget documentation and schedules for 2010/11

To facilitate oversight of compliance with this aspect of the Municipal Budget and Reporting Regulations, accounting officers are reminded that:

- Section 22(b)(i) of the MFMA requires that **immediately** after an annual budget is tabled in a municipal council it must be submitted to the National Treasury and the relevant provincial treasury in both printed and electronic formats. The deadline for such submissions is Friday, 9 April 2010.
- Section 24(3) of the MFMA, read together with regulation 20(1), requires that the approved annual budget must be submitted **within ten working days** after the council has approved the annual budget. So if the council only approves the annual budget on 30 June 2010, the final date for such a submission is Wednesday, 14 July 2010, otherwise an earlier date applies.

The municipal manager must submit:

- the budget documentation as set out in Schedule A of the Municipal Budget and Reporting Regulations, including the main tables (A1 - A10) and all the supporting tables (SA1 – SA37) in both printed and electronic format; and
- the draft service delivery and budget implementation plan in both printed and electronic format; and
- in the case of approved budgets, the council resolution.

Municipalities are required to send electronic versions to [lgdocuments@treasury.gov.za](mailto:lgdocuments@treasury.gov.za).

If the budget documents are too large to be sent via e-mail, arrangements for them to be downloaded from the municipality's website must be made with Elsabe Rossouw (e-mail: [Elsabe.Rossouw@treasury.gov.za](mailto:Elsabe.Rossouw@treasury.gov.za)).

Municipalities are required to send printed submissions of their budget documents and council resolution to:

For couriered documents

Ms Linda Kruger  
National Treasury  
40 Church Square  
Pretoria, 0002

For posted documents

Ms Linda Kruger  
National Treasury  
Private Bag X115  
Pretoria, 0001

## 7.2 Submissions to the National Treasury database for publication

For publication purposes, municipalities are still required to use the Budget Reform Returns to upload budget and monthly expenditure to the National Treasury Local Government Database. These returns are available in the original formats as well as in versions aligned to the Municipal Budget and Reporting Regulations. National Treasury is aware that it will take some time to align the current reporting formats with the new reporting formats and that system vendors need to make adjustments to their accounting software. National Treasury will therefore allow both the current returns as well as the aligned returns to be submitted to [lgdatabase@treasury.gov.za](mailto:lgdatabase@treasury.gov.za) for the next 2 years after which only the aligned version of the electronic returns will be accepted as the source for publications.

The new aligned electronic returns may be downloaded from National Treasury's website at the following link: [http://www.treasury.gov.za/legislation/mfma/return\\_forms/default.aspx](http://www.treasury.gov.za/legislation/mfma/return_forms/default.aspx).

### 7.3 Publication of budgets on municipal websites

In terms of section 75 of the MFMA all municipalities are required to publish their budgets, annual reports (containing audited annual financial statements) and other relevant information on the municipality's website. This will aid in promoting public accountability and good governance.

All relevant documents mentioned in this circular are available on the National Treasury website, [www.treasury.gov.za/legislation/mfma](http://www.treasury.gov.za/legislation/mfma). Municipalities are encouraged to visit it regularly as documents are regularly added / updated on the website.

## Contact



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**JH Hattingh**  
**Chief Director: Local Government Budget Analysis**  
**19 February 2010**

## Annexure

### Summary of key issues

**Given that the 2010 FIFA Soccer World Cup starts on 11 June 2010, municipalities are advised to finalise and adopt their 2010/11 Budgets and MTREF before this date.**

#### National priorities – doing more with existing resources

1. The challenge for each municipality is to do more within its existing resource envelope.
2. In the run-up to the local government elections, Mayors and councils need to remain focused on the effective delivery of core municipal services, and steer away from seeking to buy political support through patronage.
3. Each municipality must explore how it can contribute to job creation when revising their IDPs and preparing their 2010/11 budgets.
4. Government is taking active steps to uproot the problem of corruption in all three spheres of government, particularly in the tender system. Municipalities must play their part.
5. Municipalities are advised that National Treasury's supply chain compliance unit will also be focusing on municipal procurement processes.

#### Headline inflation forecasts

6. The headline inflation forecast for 2010/11 is 5.7 per cent. Municipalities must take this into consideration when preparing their budgets.
7. Municipalities should also take into account the wage agreement SALGA concluded with municipal workers unions on 31 July 2009.

#### Revising rates, tariffs and other charges

8. Municipalities must explore imaginative ways of structuring the tariffs for utility services to encourage more efficient use of these services and to generate the resources required to maintain, renew and expand infrastructure.
9. NERSA is expected to announce the electricity bulk tariff increase on 24 February 2010. In the interim, National Treasury advises municipalities to use 35 per cent.
10. All municipalities should aim to have appropriately structured, cost-reflective water tariffs in place by 2014.
11. Municipalities must note that COGTA is in the process of prescribing a ratio with respect to public benefit organisations relative to residential properties.
12. The verification of existing municipal taxes in terms of section 12 of the Municipal Fiscal Powers and Functions Act continues.

#### Funding choices and management issues

13. Municipal revenues and cash flows are expected to remain under pressure in 2010/11 and so municipalities should adopt a conservative approach when projecting their expected revenues and cash receipts
14. Municipalities must pay special attention to controlling unnecessary spending on nice-to-have items and non-essential activities, such as foreign travel, councillor and staff perks, advertising and public relations activities.
15. Municipalities must also ensure that their capital budgets reflect consistent efforts to address the backlogs in basic services and the refurbishment of existing network services.
16. Municipalities must include a section on 'Drinking water quality and waste water

- management' in their 2010/11 budget document supporting information
17. Allocations to "Mayoral Discretionary Funds", "Special Projects", "Special Events" or similar discretionary type funds are discouraged.
  18. Municipalities are urged to allocate all Ward Allocations in tabled and approved budgets.
  19. Municipalities are discouraged from starting projects to build or renovate office buildings, but rather to prioritise service delivery infrastructure.
  20. Municipalities are allowed to use future conditional transfers as security for bridging finance to facilitate the implementation of capital projects financed by conditional grants, but only after getting approval from National Treasury.
  21. Each municipality must put in place a council approved virements policy, which should provide clear guidance to managers of when they may shift funds between items, projects, programmes and votes.

#### **Conditional transfers to municipalities**

22. To bring legal certainty to the process of managing unspent conditional grant funds, section 20 of the 2010 Division of Revenue Bill regulates the process.
23. Municipalities may not rollover unspent conditional grant spending in terms of section 28(2)(e) of the MFMA. Written permission to spend these rolled over funds will be given by National Treasury.

#### **The Municipal Budget and Reporting Regulations**

24. All municipalities must prepare budgets, adjustments budgets and in-year reports for the 2010/11 financial year in accordance with the Municipal Budget and Reporting Regulations. In this regard, municipalities must comply with both:
  - The formats set out in Schedules A, B and C; and
  - The relevant attachments to each of the Schedules (the Excel Formats).
25. All municipalities must do a funding compliance assessment of their 2010/11 budgets in accordance with the guidance given in MFMA Circular 42 and the MFMA Funding Compliance Guideline before tabling their budget, and where necessary rework their budget to comply so that they table a properly funded budget.

#### **Budget process and submissions for the 2010/11 MTREF**

26. The deadline for the submission of tabled budgets is Friday, 9 April 2010.
27. The deadline for the submission of approved budgets is ten working days after the council approves the annual budget.