FUNDING AND RESERVES POLICY

MARCH 2022

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INTRODUCTION AND OBJECTIVE

The Council sets itself the objective of becoming a financially sustainable municipality with basic levels of service delivery to the entire community.

This policy aims to set standards and guide lines towards ensuring financial viability over both the short- and long term and includes funding as well as reserves requirements.

1. SECTION A: FUNDING POLICY

1.1. LEGISLATIVE REQUIREMENTS

In terms of Sections 18 and 19 of the Municipal Finance Management Act (Act No 56 of 2003) (MFMA), an annual budget may only be funded from:

a. realistically anticipated revenues to be collected;

b. Cash backed accumulated funds from previous years' surpluses not committed for other purposes and

c. Borrowed funds, but only for capital projects.

Furthermore, spending on a capital project may only be commenced once the funding sources have been considered, are available and have not been committed for other purposes. In determining whether the budget is funded and in addition ensuring long term financial sustainability, the municipality will use analytical processes, including those specified by National Treasury from time to time.

1.2. STATEMENT OF INTENT

The municipality will not pass a budget which is not funded or where any of the indicators as listed in this document are negative, unless acceptable reasons can be provided for non-compliance and provided that the requirements of the MFMA must at all times be adhered to.

1.3. CASH MANAGEMENT

Cash must be managed in terms of the municipality's Cash Management and Investment Policy.

1.4. LIABILITY MANAGEMENT

Debt must be managed in terms of the municipality's Borrowing Policy.

1.5. FUNDING THE OPERATING BUDGET

1.5.1. Introduction

The municipality's objective is that the user of municipal resources must pay for such usage in the period in which it will occur.

The municipality recognizes the plight of the poor, and in line with national and provincial objectives, commits itself to subsidizing services to the poor. This may necessitate cross-subsidization in some tariffs to be calculated in the budget process.

1.5.2. General Principle When Compiling the Operating Budget

The following specific principles apply when compiling the budget:

a. The Council is committed to stringent budgeting policies and parameters through a budget that seeks to strike a balance between the development challenges of the poor areas and the need to maintain the infrastructure in established areas

b. The council is committed to ensuring that consultation on the budget takes place as widely as possible

c. To achieve balanced budgets on an affordable basis now and in future

d. Tariffs need to remain or move towards being cost reflective, and should take into account the need to address infrastructure backlogs

e. There will be no budget allocated to national and provincial funded projects unless the necessary grants to the municipality are reflected in the national and provincial budget and have been gazette as required by the annual Division of Revenue Act

f. The cost containment measures must be implemented to eliminate waste, reprioritize spending and ensure savings on six focus areas namely, consultancy fees, no credit cards, travel and related costs, advertising, catering and event costs as well as costs for accommodation

g. Depreciation must be fully budgeted for in the MTREF budget

1.6. FUNDING THE CAPITAL BUDGET

1.6.1. INTRODUCTION

The municipality's objective is to maintain, through proper maintenance and replacement measures, existing levels of service and to improve and implement services which are neglected or non – existent.

In order to achieve this objective the municipality must annually, within financial means, budget for the replacement of redundant assets as well as acquiring new assets.

1.6.2. FUNDING SOURCES FOR CAPITAL EXPENDITURE

The capital budget can be funded by way of transfers and grants, public contributions and donations, borrowing and internally generated funds.

Proceeds from the sale of assets must mainly be used to fund the capital replacement reserve and infrastructure type projects.

a. Internally Generated Funds

The capital budget may be financed from internally generated funds such as the capital replacement reserve and surplus cash resources. The allocations of the funding sources from internally generated funds will be determined during the budget process.

b. Transfers and Grants (Including Public Contributions and Donations)

Grants for capital expenditure have become a common practice, especially in order to extend service delivery to previously disadvantaged areas. While such grants are welcomed, care should be taken that the acceptance of grant funding does not place an unreasonable burden on the residents for future operating and maintenance costs which may be higher than their ability to pay.

The Accounting Officer will annually evaluate the long term effect of capital grants on future tariffs, and if deemed necessary, report on such to Council.

c. Borrowings

The municipality may only raise long-term borrowings in accordance with its Borrowing Policy.

The Accounting Officer must put accounting measures in place to ensure that no unspent portions of loans are utilized for operating purposes.

For budgeting purposes any difference between proposed capital spending from loans and proposed loans raised must be included in the cash surplus for the year, i.e. any unspent borrowings at year end must be cash-backed in the 'Cash backed reserves reconciliation'.

Repaying long-term liabilities will impact directly on future tariffs that will be charged to consumers. For this reason, Council will give priority to borrowing for revenue-generating assets only. Provision for acquiring non-revenue generating assets will be made by way of utilising other funding sources.

1.7. FUNDING COMPLIANCE MEASUREMENT

1.7.1. INTRODUCTION

The municipality must ensure that the annual budget or any subsequent adjustments budget complies with the requirements of the MFMA and this policy.

For this purpose a set of indicators must be used as part of the budget process and be submitted with the budget. These indicators will include all indicators as recommended by National Treasury as well as any additional indicators detailed in this policy.

If any of the indicators are negative during the compilation or approval process of the budget, the budget may not be approved, unless those negative indicators can be reasonably explained and any future budget projections address the turnaround of these indictors to within acceptable levels2.

1.7.2. CASH AND CASH EQUIVALENTS

A positive cash/cash equivalents position should be maintained throughout the year.

1.7.3. CASH PLUS INVESTMENTS LESS APPLICATION OF FUNDS

The overall cash position (cash/cash equivalents and investments) of the municipality must be sufficient that it can:

Provide for the cash-backing of:

a. unspent conditional transfers and grants;
b. unspent conditional public contributions;
c. unspent borrowing;
d. VAT due to SARS;
e. secured investments (whether long- or short-term);
f. reserves as approved by the municipality
g. Take into account other working capital requirements.

1.7.4. INDICATORS

a. MONTHLY AVERAGE PAYMENT COVERED BY CASH AND CASH EQUIVALENT (“CASH COVERAGE”)

This indicator shows the level of risk should the municipality experience financial stress.

b. SURPLUS/DEFICIT EXCLUDING DEPRECIATION OFFSETS5

It is probable that the operating budget including depreciation charges on assets funded by grants and public contributions, as well as on revalued assets, could result in a deficit.

It is not the intention that residents be burdened with tariff increases to provide for such depreciation charges. In order to ensure a “balanced” budget but excluding such depreciation charges, the depreciation charges maybe offset against the net surplus / deficit.

c. PROPERTY RATES/SERVICE CHARGE REVENUE PERCENTAGE INCREASE

The intention of this indicator is to ensure that tariff increases are in line with macro-economic targets.

d. CASH COLLECTION PER CENTRATE

The object of the indicator is to establish whether the projected cash to be collected is realistic and complies with section 18 of the MFMA.

It is not permissible to project a collection rate higher than the current rate. Any improvement in collection rates during the budget year may be appropriated in an Adjustments Budget.

e. BORROWING AS A PERCENTAGE OF CAPITAL EXPENDITURE (EXCLUDING GRANTS AND CONTRIBUTIONS)

This indicator provides information as to compliance with the MFMA in determining borrowing needs. The Accounting Officer must ensure compliance with the municipality’s borrowing policy.

f. REPAIRS AND MAINTENANCE EXPENDITURE LEVEL

Property Plant and Equipment should be maintained properly at all times in order to ensure sustainable service delivery. The budget should allocate sufficient resources to maintain assets and care should be exercised not to allow a declining maintenance program in order to fund other less important expenditure requirements.

Similarly, if the maintenance requirements become excessive, it could indicate that a capital renewal strategy should be implemented or reviewed.

As a general benchmark the maintenance budget infrastructure assets should be 8 per cent of the asset values (write down values). Currently the ratio is below this and the benchmark should be achieved in the near future.

Where the budgeted amounts for repairs and maintenance reflected on Table A9 are less than 8 per cent of the asset value (write down value) of the municipality's Plant, Property and Equipment (PPE) as reflected in the municipality's annual financial statements, the municipality must provide a detailed explanation and assurance that the budgeted amount is adequate to secure the ongoing health of the municipality's infrastructure supported by reference to its Immovable Asset Management Policy.

g. ASSET RENEWAL/REHABILITATION EXPENDITURE LEVEL

This indicator supports further the indicator for repairs and maintenance.

The Accounting Officer must, as part of the capital budget, indicate whether each project is a new asset or a replacement/renewal asset in order to determine whether the renewal program is sufficient or needs revision.

2. SECTION B: RESERVES POLICY

2.1. INTRODUCTION

The municipality recognises the importance to itself, its creditors, financiers, staff and the general public of providing for a measure of protection for future losses, as well as providing the necessary cash resources for future capital replacements and other current and non-current liabilities.

This policy therefore aims to provide for a measure of protection by creating certain reserves.

2.2. LEGAL REQUIREMENTS

There are no specific legal requirements for the creation of reserves. The GRAP Standards themselves do not provide for reserves.

2.3. TYPES OF RESERVES

Reserves can be classified into two main categories being "cash funded reserves" and "non – cash funded reserves".

2.3.1. CASH FUNDED RESERVES

In order to provide for sufficient cash resources for future expenditure, the municipality hereby approves the establishment of the following reserves:

CORPORATE SOCIAL RESPONSIBILITY (CSR)

The CSR is to be utilised for future capital expenditure from own funds and may not be used for maintenance or other operating expenditure.

The CSR must be cash- backed and the Accounting officer is hereby delegated to determine the contribution to the CSR during the compilation of the annual financial statements.

2.3.2. NON – CASH FUNDED RESERVES

On occasion it is necessary to create non – cash funded reserves. The Accounting Officer must create any reserves prescribed by the accounting standards, such as the Revaluation Reserve and Valuation Reserve, if required.

2.4. ACCOUNTING FOR RESERVES

2.4.1. REVALUATION RESERVE

The accounting for the Revaluation Reserve must be done in accordance with the requirements of GRAP 17.

2.4.2. OTHER RESERVES

The accounting for all other reserves must be processed through the Statement of Financial Performance. The required transfer to or from the reserves must be processed in the Statement of Net Assets to or from the accumulated surplus.

It is a condition of GRAP and this policy that no transactions may be directly appropriated against these reserves.

3. SECTION C: COMMENCEMENT AND APPROVAL

This Policy requires Council approval and will be in effect, after the approval of the Municipal Council as of 1 July 2022.