



SELECT COMMITTEE OF FINANCE
BRIEFING SESSION: FINANCIAL VIABILITY

19 SEPTEMBER 2007



PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA

TABLE OF CONTENTS

CONTENTS	PAGE
1. 2007-08 Budget Summary.....	3
1.1 Operating Budget.....	3
1.2 Capital Budget.....	7
1.3 Credibility of the budgets.....	10
1.4 Summary of key budget issues.....	12
2. 2006-07 Financial Status.....	13
2.1 Executive Summary.....	13
2.2 Financial systems.....	15
2.3 Audit outcomes and risks.....	15
2.4 Loans and investments.....	17
3. Conditional Grants/ MIG - Spending and Performance of the Municipality	19
4. Inter-governmental Relations.....	22
5. Financial Management Grant – National Treasury.....	23
6. Municipal Finance Management Act – Compliance and Assistance.....	24
7. Capacity Constraints.....	28
8. Alignment of municipality's IDP with Free State Growth and Development Strategy.....	29



PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA



1. 2007-08 BUDGET SUMMARY

1.1 2007-08 Operating Budget

Total **Operating expenditure budget** for **2007-08** is estimated at **R211 million**, excluding a surplus of **R15 million** which will be utilized to finance capital projects.

Operating Expenditure

➤ Salaries and allowances	:	R80 million (R75 million in 2006-07), an increase of 8%.
➤ Electricity purchases	:	R36 million (R33,1 million in 2006-07), an increase of 10%
➤ Water purchases	:	R9 million (R7 million in 2006-07), an increase of 21%
➤ Chemicals	:	R2,5 million (R2,3 million in 2006-07)
➤ Indigent Subsidies	:	R18,2 million (R13,6 million in 2006-07), an increase of 25%
➤ Repairs and Maintenance	:	R17,2 million (R14,8 million in 2006-07), an increase of 14%
➤ Interest on loans	:	R4,3 million
➤ Fuel & Oil	:	R3,4 million
➤ Poverty Alleviation	:	R2 million



PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA



Chart 1: Operating Expenditure by Vote

Bulk purchases of electricity and water are the major cost drivers in the relevant votes. The following charts illustrate operational expenditure budget in terms of functions and type of expenditure.

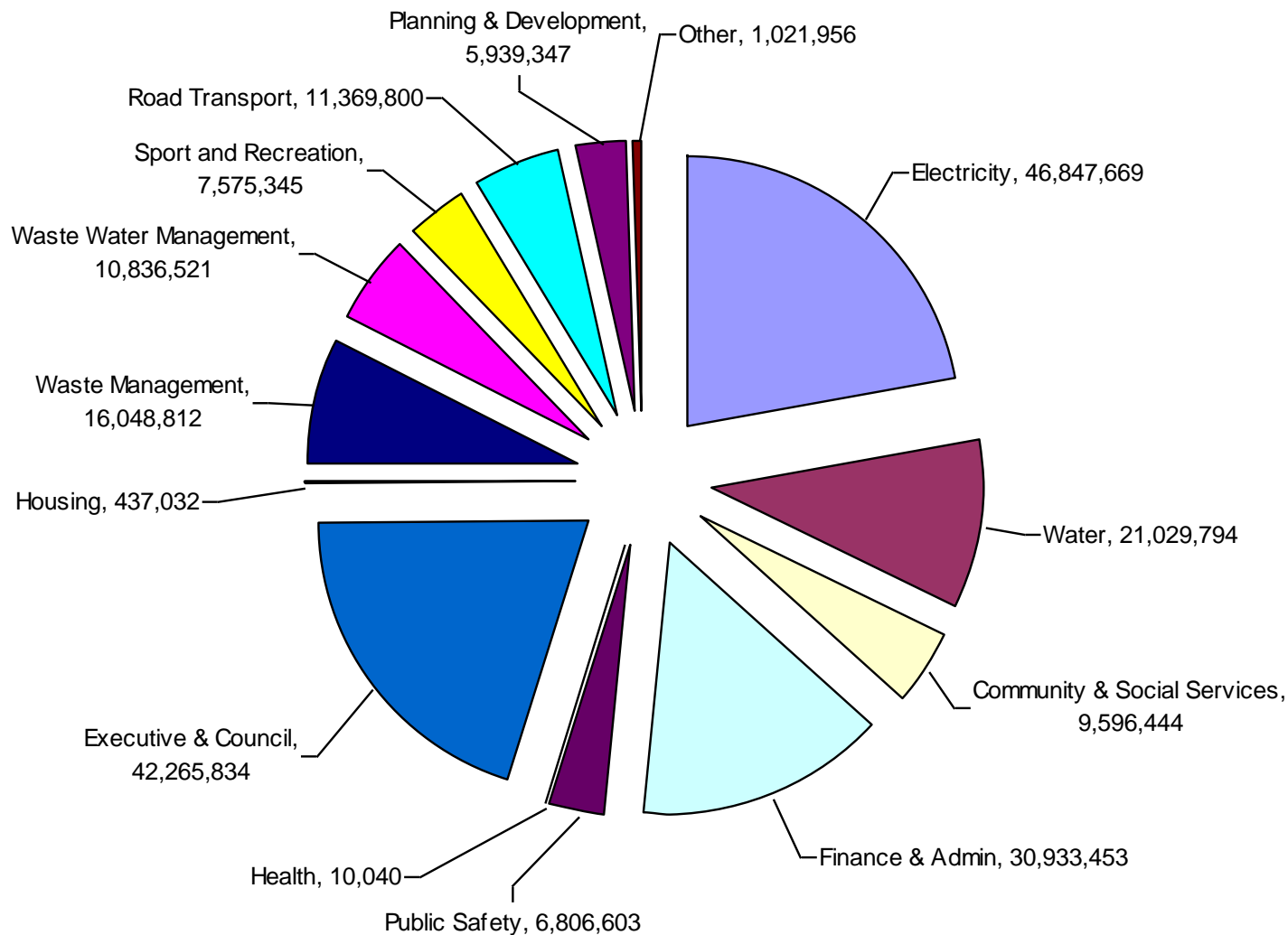
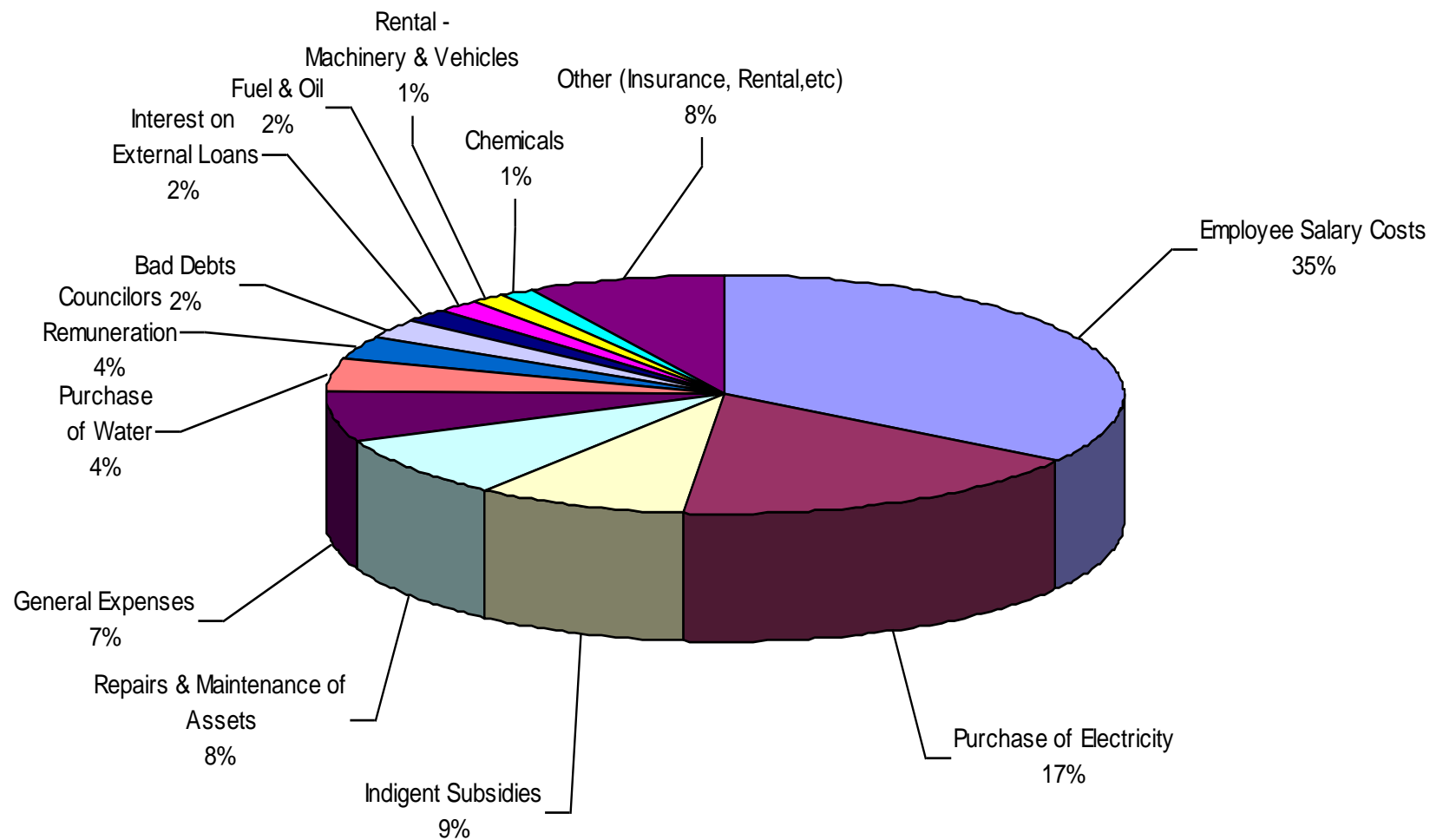


Chart 2: Operating Expenditure by Type

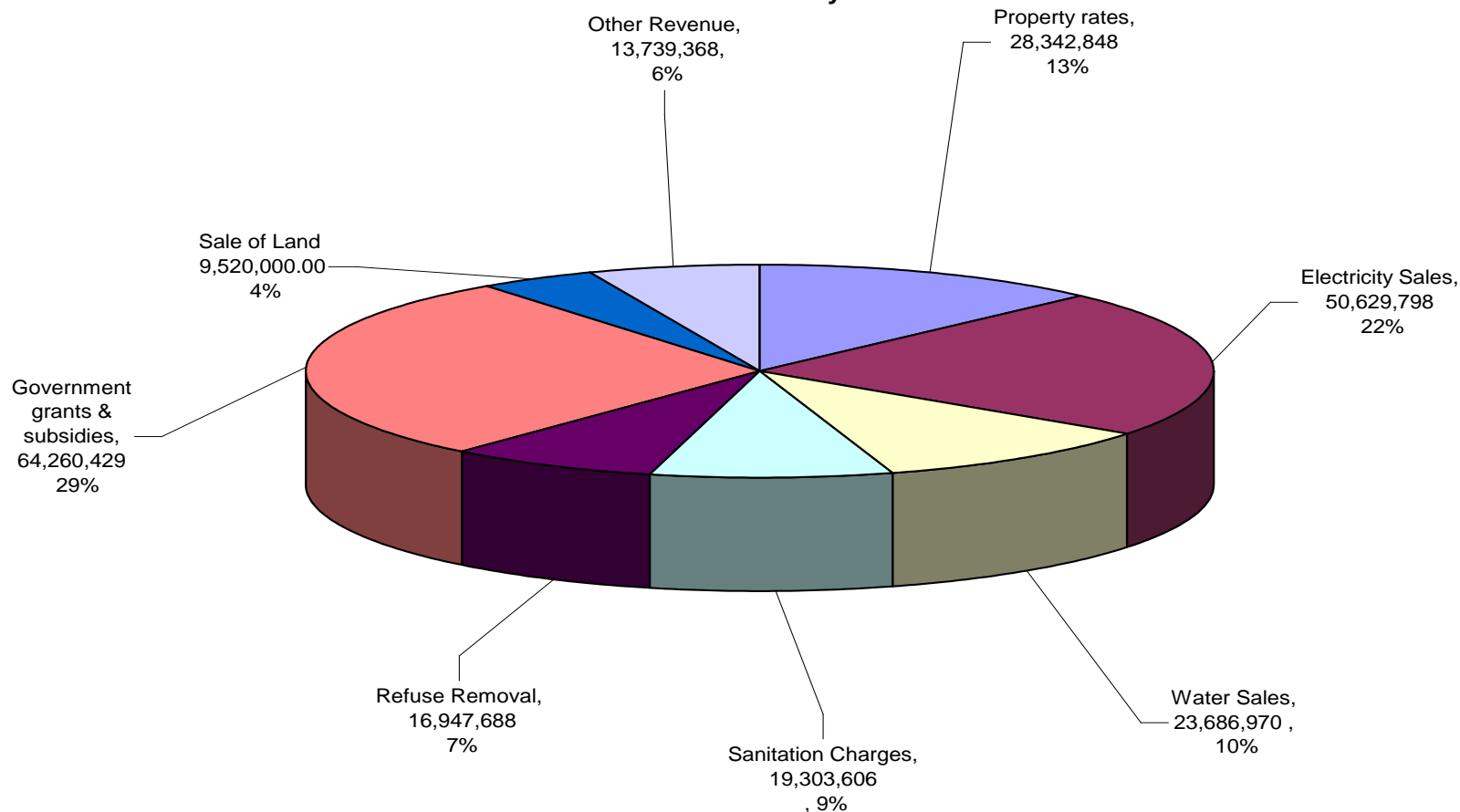


Operating Revenue

Operational budget is funded by operating revenue proposed for **2007-08** is estimated at **R226** million (**R211** million in 2006-07), an increase of 7%. **R9,5** million is expected from selling of land.

Operating revenue source can be illustrated as follows;

Chart 3 : Revenue by Source



1.2 Capital Budget

Total **Capital Budget** for **2007-08** amounts to **R76 million (R61,6 million in 2006-07)** and is made up as follows;

- Sanitation : R 51 million (R 7,6 million in 2006-07)
- Roads : R 2,7 million
- Water : R 6,2 million
- Electricity : R 3,8 million
- Cemeteries : R 3 million
- Vehicles and machinery : R 1,6 million
- Institutional development : R 5,5 million

All the projects funded in the capital budget are aligned to Ngwathe Municipality's integrated development plan.

Capital Budget is mainly funded from National Government (Municipal Infrastructure Grant), and surplus cash.

The municipality has considered securing a loan to finance bucket eradication projects of Tumahole and Phiritona.

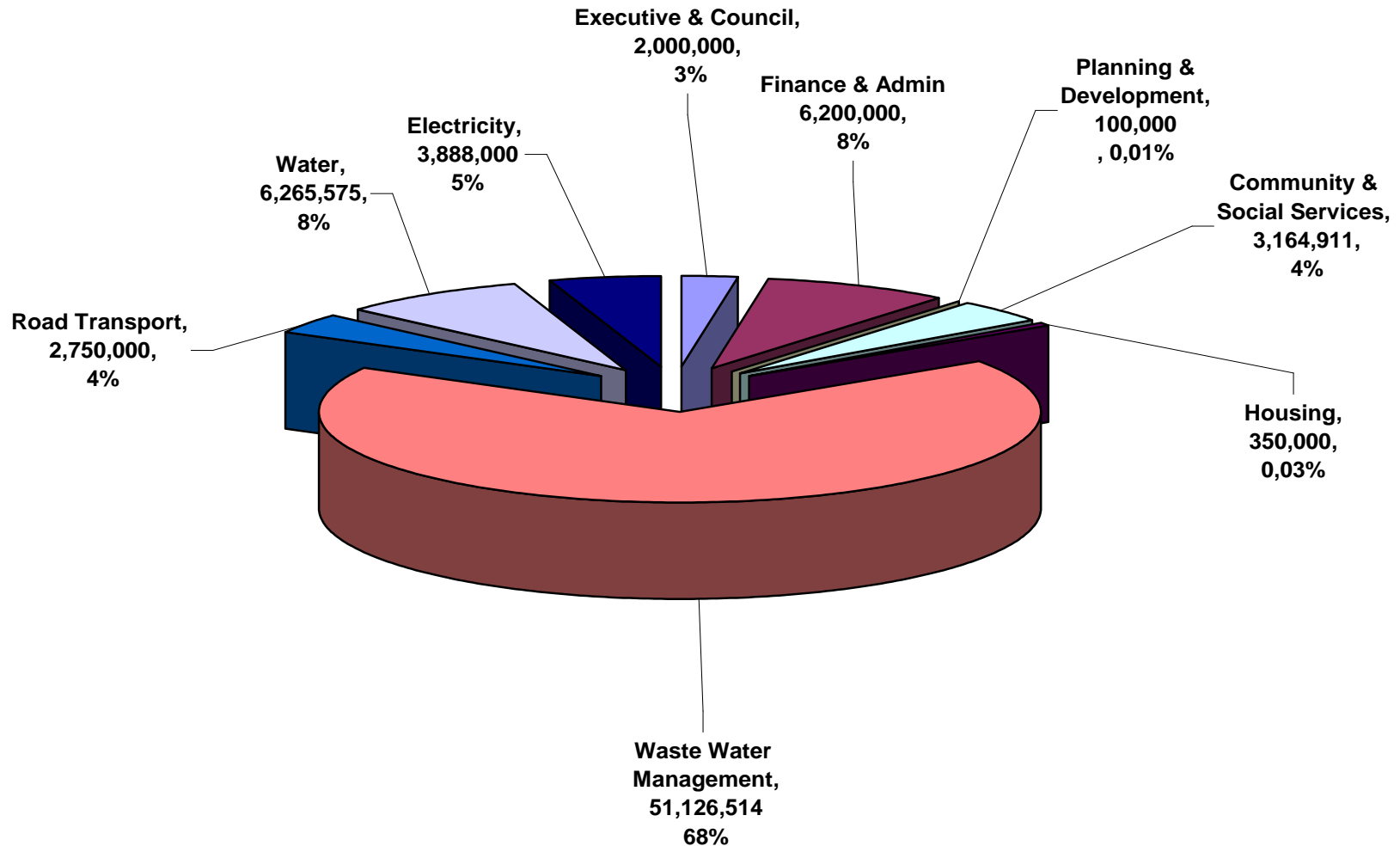


PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA



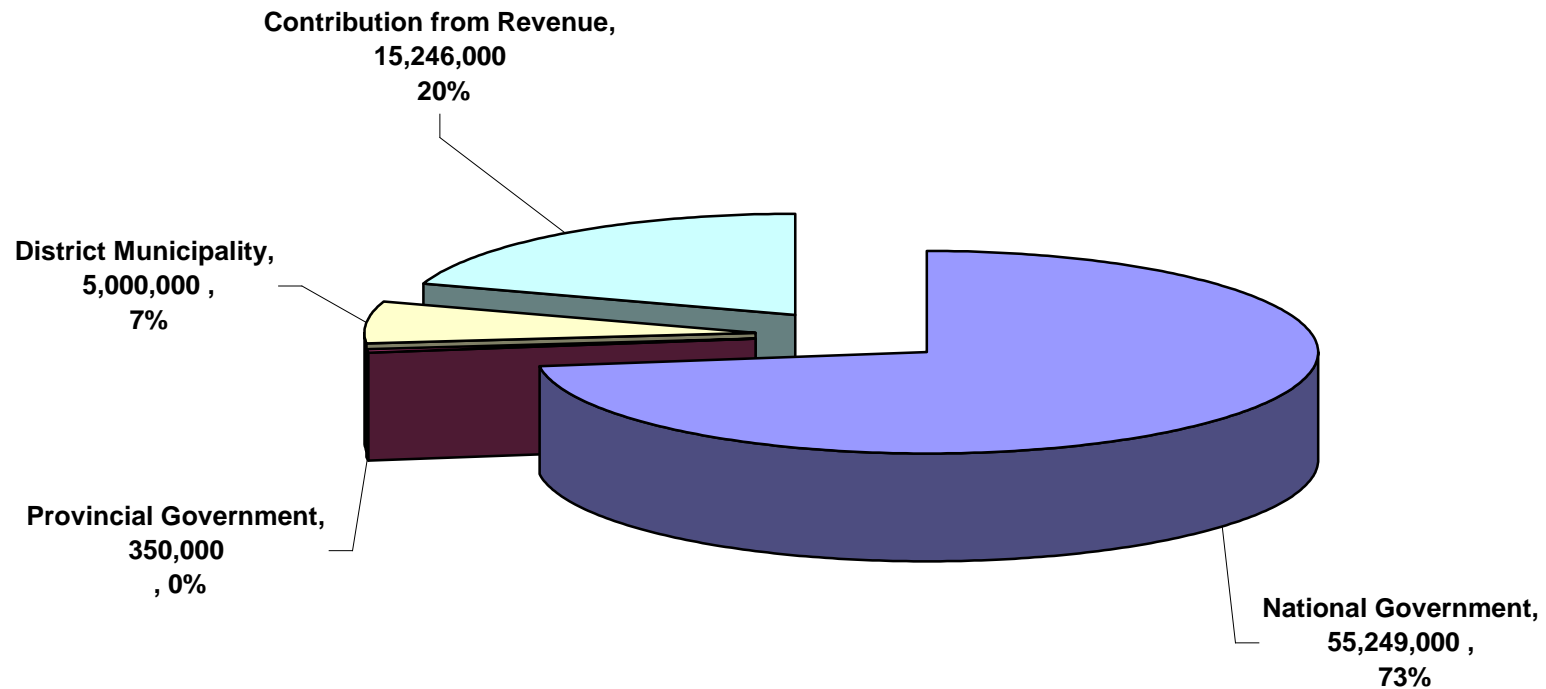
Chart 4 illustrates capital allocations made to various votes;

Chart 4: Capital Expenditure by Function



Details regarding sources of financing are illustrated on the following chart;

Chart 5: Capital Budget - Sources of Finance



1.3. Credibility of the budget

- Tariffs on water, sewerage, refuse, rates & taxes and minor services were increased based on National Treasury guidelines (MFMA Circular 41) as follows;
 - 2007/2008 – 5.1%
 - 2008/2009 – 4.3%
 - 2009/2010 – 4.5%
- Electricity tariffs will be completely restructured due alignment to REDs (E.g **Residential tariffs on conventional meters** will be increased by **6.95%**, and **residential tariffs on pre-paid meters** will be increased by **4,76%** however, basic charge will be removed on both instances.
- National growth parameters of 3% to 6% were considered in determination of tariffs for 2007/2008 budget year.
- The Increase was applied on all services and rates & taxes and will be implemented from 01 July 2007.
- First 50kw/h and 15kw/h of electricity will be provided free to indigent consumers and non- indigent households respectively.
- The current valuation roll will be utilized and property rates and taxes will be levied in accordance with the Local Government Ordinance. Property Rates Act will be implemented in the 2008/09 budget year.



PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA



Institutional arrangements

- IDP process plan and budget time table was prepared and table before Council.
- IDP and Budget Steering Committee was established.

Procedures and processes

- Budget inputs from different departments and units were submitted to Budget and Treasury Office in prescribed format according to the budget policy and guidelines from the National Treasury. Current financial year's budget and actual figures were also used as baseline information submitted to managers for preparing budgets.
- Capital expenditure is budget according to community and National priorities identified in the IDP.
- The Division of Revenue Bill for 2007/2008 was utilized to determine the Equitable Share, Councilors remuneration subsidy, Financial Management Grant, Municipal Systems Improvement Grant, and Municipal Infrastructure Grant.
- SALGBC collective agreement on remuneration of employees stipulate that salaries for 2007-08 financial year will be increased by CPIX (5,1%) plus 1,75%. Thus salaries, allowances and employee benefits were increased by 6,8%.
- Bulk water purchases were raised by 5.1%
- Bulk electricity purchases were increased by 5,7% according to Eskom guidelines

1.4 Summary of key budget issues

The budget was prepared in terms of GAMAP and GRAP standards. The following were excluded or included;

- Depreciation was introduced to account properly for municipal assets.
- Capital expenditure from own revenue is funded only by expected surplus cash.
- Redemption and interest on internal loans were removed.
- Audit fees were classified as normal expenditure not a contribution.
- The 2007/08 budget was balanced instead of just been funded.

Strategic service delivery focus areas are summarized as follows'

- **Spatial Development Framework**
 - a. Development and implementation of Spatial development framework
 - b. Development and implementation of the Land use management scheme
- **Service Delivery**
 - a. Sanitation
 - b. Roads
 - c. Water
 - d. Electricity
 - e. Refuse removal

2. 2006-07 FINANCIAL STATUS

2.1 EXECUTIVE SUMMARY

- Ngwathe Municipality bank overdraft facility decreased from R3,7 million in 2006 to R3,2 million in 2007.
- A total debt owed by consumers amounting to R40 million was written by Council during the 2006/2007 financial year and total debtors outstanding as at 30 June 2007 amounted to R92 million as compared to R122 million in 2006.
- Total value of fixed assets increased from R350 million in 2006 to R404 million in 2007.
- **Current ratio i.e. assets in relation to liabilities;**
Indicates extent to which claims of creditors are covered by assets,
2006 – Current ratio = 3.20 means for every R1 liability the municipality has R3.20 assets and this has deteriorated in 2007 whereby the ratio was 2.2 for every R1 liability.
- **Debt ratio** i.e the percentage of assets in relation debt; The percentage was 59% in 2006 and increased to 75% in 2007, and this shows that the municipality is highly indebted and the asset market value has decreased and this will make it difficult for the municipality to replace fixed assets and to obtain funding.
- **Salaries as percentage of total expenditure** amounted to 33,5% in 2006 and this improved to 32,5% in 2007.

See Table 1 below, for more information.



PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA



TABLE 1:

	2007	2006
Current assets	52,150,560	62,923,468
Non-current or fixed assets	17,573,463	19,312,784
Total assets	69,724,023	82,236,252
Current liabilities	23,722,017	19,647,207
Non-current liabilities	28,268,091	29,136,447
Total liabilities	51,990,108	48,783,654
Equity, funds and reserves	17,733,915.00	33,452,598
Operating Income	181,141,174	163,837,421
Total income	181,141,174	163,837,421
Payroll Expenses	63,357,797	55,209,681
	131,501,446	109,199,858
Total Expenditure	194,859,243	164,409,539
Net profit/(loss)	(13,718,069)	(572,118)



2.2 FINANCIAL SYSTEMS

- The municipality has implemented GAMAP/ GRAP compliant financial system (E-VENUS).
- Billing systems have been upgraded and were controls enhanced. The main challenge relating to billing is completeness and cleansing of data and meter readings. However, the municipality has implemented measures to address these shortcomings
- Cash and Debt Management systems were improved on the E-Venus computer system, however, internal control procedures are currently been improved and on job-training will be conducted to build capacity.

2.3 AUDIT OUTCOMES AND RISKS

- **Fixed assets**

The fixed asset register supplied by the municipality was incomplete, as, inter alia, all assets were not included and details provided were inadequate to trace the assets to appropriate supporting documentation

- **Long-term debtors**

Long-term debtors could not be verified due to a lack of supporting documentation.

- **Expenditure management**

Due to weaknesses in the control framework for expenditure and payments, it was identified that some payments made without original invoices and were not cancelled after payments were made.

- **Debtor management**

The municipal manager did not enforce the municipality's credit control and debt collection policies as required by section 100(a) of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2003), as no debtors were handed over for legal action. This resulted in a debtors' collection period of 267 days which is considered to be very high.



Steps taken to address under-collection of revenue

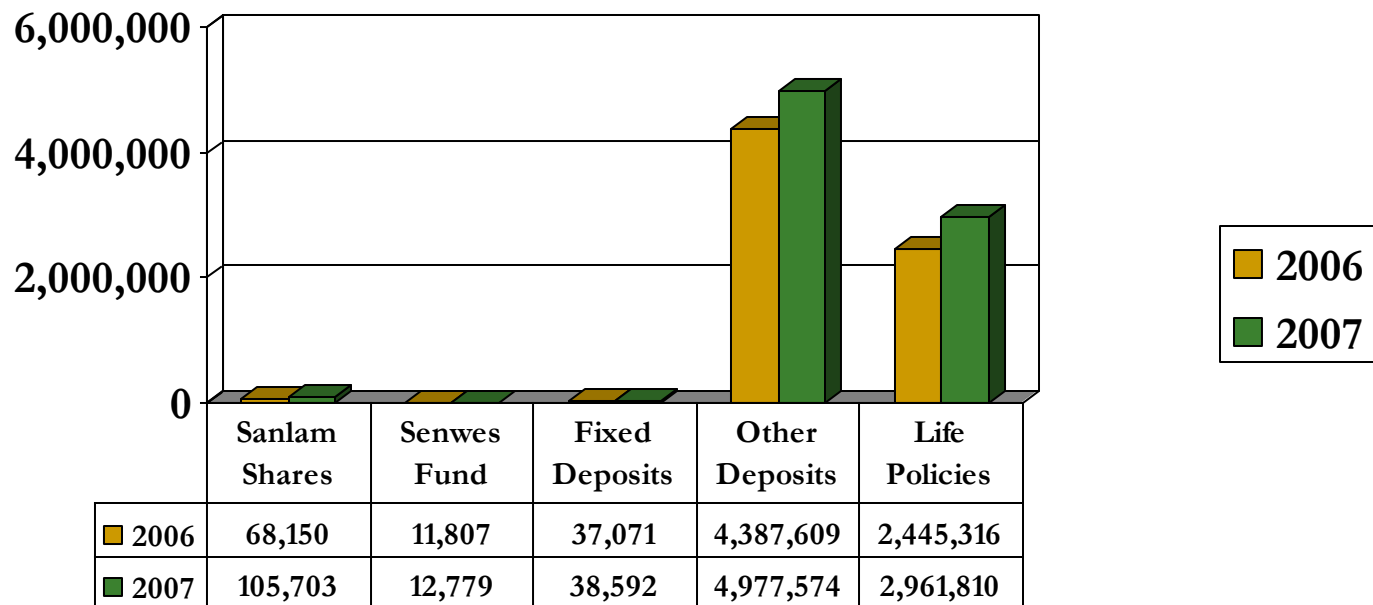
- Debt Collection unit consisting of 9 officials was established to strictly implement credit control and debt collection policy.
- Councilors and ward committees will assist in encouraging consumers to pay for services.
- One debt collection official will deal with collection of revenue and outstanding monies from National and Provincial Departments.

Revenue related policies

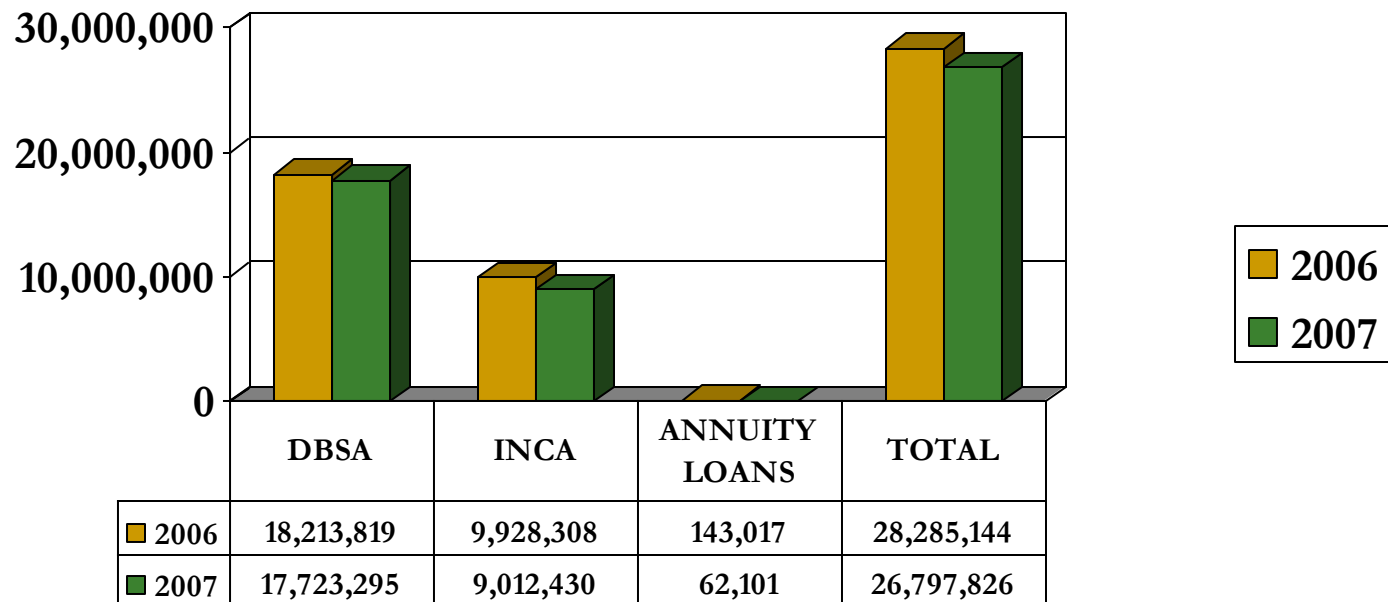
- All the revenue related by-laws are currently being compiled in conjunction with service provider and will be finalized in the 2007/2008 financial year.
- The following policies were compiled and a workshop was held with Councilors where they were discussed and reviewed;
 - Credit control and debt collection policy
 - Indigent Policy
 - Tariff Policy
 - Budget Policy



NGWATHE MUNICIPALITY INVESTMENTS



NGWATHE MUNICIPALITY LOANS



3. CONDITIONAL GRANTS - SPENDING

- The following projects were completed (2005-2007) within Ngwathe Municipality to enhance and upgrade service delivery infrastructure assets; These projects were funded by National Electrification Grant and Municipal Infrastructure Grant (MIG);

PROJECT DESCRIPTION	AMOUNT
PARYS	
Highmast lights	1 755 153
Water purification - Parys	5 700 000
Cemeteries	460 773
Roads	5 000 000
HEILBRON	
Highmast lights	2 918 418
Electrification of houses	1 000 000
Bulkwater	2 081 269
Waterborne sewer	2 453 000
Cemeteries	1 005 790

<u>PROJECT DESCRIPTION</u>	<u>AMOUNT</u>
<u>EDENVILLE</u>	
Electrification of houses	1 116 000
Highmast lights	1 755 153
<u>VREDEFORT</u>	
Roads	435 000
Waterborne sewer	2 094 000
Bulkwater	1 427 901
Cemeteries	596 943
<u>KOPPIES</u>	
Highmast lights	3 242 465
Roads	625 000
Cemeteries	261 788

Final outcomes of conditional grants and trends for 2006-07

Description	Allocation/ Budget	Actual transfers made	Actual Expenditure 30 June 2007
Municipal Financial Management Grant	500,000	500,000	500,000
Municipal Infrastructure Grant (MIG)	34,966,570	33,443,850	25,459,593
National Electrification Programme	1,176,727	1,000,000	1,000,000
Water Services - Disaster Relief	0	0	0
Provincial Government - Health	162,000	0	0.00
Provincial Government - Spatial Planning	514,000	310,000.00	310,000.00
Provincial Government - Town Planning	70,000	70,000.00	70,000.00
	37,389,297	35,323,850	27,339,593

4.

INTER- GOVERNMENTAL RELATIONS

NATIONAL (TREASURY AND DPLG)

- Relations with the National treasury and DPLG are satisfactory in terms of obtaining information for decision making, and where the municipality has queries and concerns these are addressed.
- Main challenges are with regard to communication whereby the municipality send reports and relevant departments do not provide feedback.

PROVINCIAL (TREASURY, LOCAL GOVERNMENT AND HOUSING, PUBLIC WORKS, OTHER)

- Communication and relations between Provincial Treasury, Department of Local Government & Housing and the municipality are exceptionally handled well in terms of capacity building and information sharing.
- Department of Roads and Public Works normally have meeting where issues of common interest are discussed and payment towards the municipal rates and taxes is made timeously.



PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA



5. FINANCIAL MANAGEMENT GRANT

- The municipality appointed 5 interns in 2004 for 2 years using the Financial Management Grant for their remuneration and workshops.
- Training on implementation of GRAP/ GAMAP and development of internal control procedures manuals was funded from 2006/2007 grant.



PARLIAMENT
OF THE REPUBLIC OF SOUTH AFRICA



6. PROGRESS ON IMPLEMENTATION OF MFMA

6.1 Implementation Plan and progress

- MFMA implementation plan was compiled in November 2004, and the following were included in the action plan;

ACTION TO BE TAKEN	OUTSTANDING MATTERS	TARGET DATE
Management Arrangements	<ul style="list-style-type: none">➤ Review of structure➤ Audit Committee➤ Risk Management➤ Delegations➤ Competency levels➤ Review of section 57 managers contracts in line with MFMA	<ul style="list-style-type: none">➤ 27 Sept 07➤ 30 Nov 07➤ 31 March 08➤ 27 Sept 07➤ 01 Oct 07➤ 30 Sept 07
Financial Planning and Reporting	<ul style="list-style-type: none">➤ SDBIP and performance agreements submitted to Mayor and MEC	<ul style="list-style-type: none">➤ 28 June 07
Income and Expenditure Management	<ul style="list-style-type: none">➤ Monthly reconciliation of all financial accounts	<ul style="list-style-type: none">➤ 31 Oct 07
Cash Management and Banking	<ul style="list-style-type: none">➤ Consolidated report on withdrawals to AG➤ New bank accounts to AG and Provincial Treasury	<ul style="list-style-type: none">➤ 31 Oct 07

ACTION TO BE TAKEN	OUTSTANDING MATTERS	TARGET DATE
Supply Chain Management Reform	<ul style="list-style-type: none"> ➤ Contract management in terms of s116 ➤ Capacity building ➤ PPP's 	01 November 2007
Municipal Investments and Borrowings	None	
Asset and Liability Management	<ul style="list-style-type: none"> ➤ Assets valued in terms of GRAP ➤ Delegation of power in terms of disposal of movable assets 	➤ 30 June 2008
In-Year and Annual Reporting	<ul style="list-style-type: none"> ➤ Development of website ➤ Implementation of issues raised by AG ➤ Annual report ➤ Oversight report 	<ul style="list-style-type: none"> ➤ 31 Dec 2007 ➤ 30 Nov 2007 ➤ 31 October 2007 ➤ 30 Nov 2007

6.2 Internal audit and audit committees

- ❖ The municipality has the **internal audit** unit and it comprises of Senior Internal Auditor, and three Audit Clerks.
- ❖ Audit committee was appointed by Council and resolution was taken on 30 May 2006, subsequent to the appointment of the audit committee, it was established that the chairperson of the committee is the manager of a company appointed to assist the municipality with compilation of Integrated Development Plan. Ethically and in terms of MFMA, it will not be professional for the abovementioned person to serve as a chairperson as it will constitute a conflict of interest. Management has however advertised for the appointment of the chairperson of the Audit Committee.

6.3 Risk Plans

- ❖ The municipality has compiled a draft fraud prevention plan and will be sent to Council for approval.
- ❖ Council approved risk management policy in 2004/2005 financial year, and risk management unit will be included in the structure to implement and review the policy.

6.4 Reduction of short-term debt by 25%

- ❖ Municipality's overdraft facility amounts to R 3 000 000, this amount was reduced by 100% in 2004/2005 financial year.
- ❖ The municipality's financial position deteriorated in 2005/2006 and the overdraft amounted to R2,7 million, an increase of more than 100%, the municipality's credit control and debt collection policy are currently being implemented to enhance revenue and reduce overdraft.

6.5 Tabling of Section 71 Reports in Council

- ❖ Monthly 71 reports are tabled before Finance and Budget Committee, Executive Committee and ultimately to Council.
- ❖ These reports are submitted to Provincial Treasury every month.
- ❖ There were challenges relating to timeous completion of section 71 reports due to replacement of financial management systems (March and April 2007). This will be improved as soon as all conversion processes are finalized.

6.6. Assistance by Provincial Treasury and DPLG

- ❖ Chief Financial Officer's forum was established in November 2006, whereby Free State Provincial Treasury, Free State Department of Local Government and Housing, SALGA and CFO from all Free State municipalities will be able to share ideas, best practices and raise concerns. Other sector departments and relevant stakeholders are also invited where expertise is needed.

7. CAPACITY CONSTRAINTS

- Several positions will be filled to build capacity within Finance Department of Ngwathe Municipality.
- The municipality has inherited number of unskilled officials after amalgamation, and this result in capacity constraints in terms of training these employees on changing accounting standards, legislation and computer systems.
- Training on Municipal Finance Management Act, GRAP/ GAMAP and the New Computer system is required.
- The municipality is currently developing revenue collection strategy and funding is required for this purpose.

8. Alignment of municipality's IDP with Free State Growth and Development Strategy

- The IDP of Ngwathe Municipality has been aligned to the Free State Growth and Development Strategy to a greater extent, however, the non core functions of local government are truly dependent on the strategic plans of Provincial Departments which are expected to be aligned to the FSGDS.
- The Strategic Planning Phase of the IDP, acknowledges the following with the FSGDS:
 - Plays a leading role in ensuring economic planning, infrastructure investment, and development spending in accordance with the principles set out in the NSDP in the Province
 - Guide IDP's in fulfilling the national agenda of development, in order to achieve sustainable development outcomes.
 - Has set out development priorities in accordance to the set guidelines provided by the Presidency, whereby the growth potential, capacity and constraints of the province are outlined according to Municipalities.



THANK YOU