

RUSTENBURG LOCAL MUNICIPALITY



FUNDS AND RESERVE POLICY

1. INTRODUCTION

The purpose of this policy is to ensure that municipality maintains cost effective and efficient cash funding

To ensure that provisions and reserves are maintained at the sufficient required level to avoid future unfunded liabilities.

The policy is in line with the requirements of Section 8 of the Local Government: Municipal Budget and Reporting Regulation of 2009 (Government Gazette 32141 in order to monitor and sustain the municipality's financial management.

1. PURPOSE OF THE POLICY

1.1 The policy outlines the assumptions and methodology to be followed on estimating the following:

- 1.1.1 Anticipated revenue to be collected based on trading services to be billed and other revenue,
- 1.1.2 Provision for debt impairment based on the previous payment levels and past trends
- 1.1.3 Setting of cost reflective tariffs in relation to the consumers affordability
- 1.1.4 In line with the municipality's borrowing requirements
- 1.1.5 To ensure that funds are set aside monthly to fund reserves

2. GUIDING PRINCIPLES

2.1 The funds and reserve policy is based on the following principles:

2.1.1 Credibility

- The SDBIP be informed by the budget that is consistent with the IDP
- Financial viability of the municipality not to be compromised
- To ensure capability to spend funds allocated

2.1.2 Sustainability

- Ensure financial viability of the municipality
- Anticipated revenue to be collected and anticipated spending to be realistic

2.1.3 Responsiveness

- The budget to be responsive to the needs of the community
- Alignment of budget, LED Strategy with IDP to give effect to the provincial and national priorities
- The budget to respond to the municipal economic growth objectives and socio economic needs of the community.

2.1.4 Affordability

- Tariff setting to take into account local economic conditions and ability of consumers to pay in relation to the cost of rendering the services.

3. BUDGET ASSUMPTIONS AND METHODOLOGY

3.1 Funding the Annual Budget

- An annual budget may be funded from realistically anticipated revenues to be collected
- From the cash-backed accumulated surpluses from previous years not committed for any other purpose
- Borrowed funds earmarked to only fund the capital budget.
- Anticipated grants allocated to the municipality as gazetted for in the Division of Revenue Act (DORA).

3.2 Capital Budget

Capital budget provides funding for the municipality's capital programmes based on the needs identified by the community and the municipal objectives as outlined in the Integrated Development Plan of the municipality.

3.2.1 Basis of calculation

- The Zero based method is used in preparing the annual capital budget, except in cases where a contractual commitment has been made that will span over more than one financial year.
- Provisions on the capital budget shall be limited to the available financial resources and affordability.
- The annual budget shall be based on realistically anticipated revenue.
- Funds to be available (liquid cash) prior to budgeting
- Loans/ borrowing to be taken prior or be available prior to budgeting and must be equal to the anticipated capital expenditure.
- The impact of the capital budget on current and future operating budgets in terms of financial charges to be incurred on external loans, depreciation of fixed assets, maintenance of fixed assets and any other operating expenditure to be incurred resulting directly from the capital expenditure, should be carefully analysed when the annual capital budget is being compiled.
- In addition, council shall consider the likely impact of such operational expenses-net of any revenues expected to be generated by such item-on future property rates and services tariffs.

3.2.2 Funding of the Capital Budget

The capital budget shall be funded from the following:

3.2.2.1 Own Funding Sources

- The Council shall establish a Cash Replacement Reserve (CRR) for capital renewal, replacement and acquisition.
- Such reserve shall be established from unappropriated cash-backed accumulated surpluses

3.2.2.2 Amounts appropriated as contributions in each annual or adjustment budget

3.2.2.3 Public contributions, donations or other grants

- 3.2.2.4 Grants and subsidies allocated in the annual Division of Revenue Act
- 3.2.2.5 Grants and subsidies allocated by provincial government
- 3.2.2.6 Net gains on sale of fixed assets in terms of the fixed assets management and accounting policy
- 3.2.2.7 External loans/borrowings
- 3.2.2.8 Any other financing source secured by the municipality

4.2.3 Guiding principles on capital budget funding

4.2.3.1 Government grants and subsidies:

- Only gazetted allocations or transfers as reflected in the Division of Revenue Act or allocations per provincial gazette may be used to fund projects
- Conditions of the specific grant as allocated per projects must be taken into consideration.

4.2.3.1 Public contributions or donations/grants

- Capital projects will only be included in the annual budget if funding is guaranteed by means of the following:
 - I. A signed service level agreement
 - II. A contract or written confirmation
 - III. Or any legally binding document

4.2.4 Borrowing requirements

4.2.4.1 The borrowing requirements are used as a basis for determining the affordability of external loans over the Medium term and expenditure Framework. The ratios to be considered when taking up new loans/borrowings include the following:

- I. Long term credit rating of at least BBB
- II. Interest cost to total expenditure not to exceed 9%
- III. Long –term debt to revenue (excluding grants) not to exceed 50%
- IV. Consumers payment rate of above 95%
- V. Percentage of capital charges to operating expenditure of less than 15%

4.2.5 Cash-backed accumulated Reserves (CRR)

- Capital projects of a smaller nature such as office equipment, furniture, plant and equipment etc, shall be funded from own operating revenue of the same financial year.
- Capital projects to replace upgrade existing assets will be funded from CRR
- Infrastructure projects to service new developments and revenue received from sale of erven must be allocated to capital reserve for services
- Capital projects to upgrade bulk services will be allocated to the Capital Bulk Contributions Reserve for each services (electricity, water, sewerage)

4.3 Operating Budget

4.3.1 Basis of calculation

The operating budget provides funding to directorates for their medium term planned expenditure.

- The incremental approach is used in preparing the annual operating budget, except in cases where a contractual commitment has been made that would span over more than one financial year. In these instances the zero based method will be followed.
- The annual operating budget shall be based on realistically anticipated revenue to be collected, which should cater for total anticipated spending in accordance with Section 18 of MFMA no 26 2003
- NB: Amounts for provision of depreciation and debt impairment, although non-cash items are not to be used to “balance’ the operating budget shortfalls.

4.3.2 Assumptions for various budget categories

The municipality categorizes services rendered to the community according to its revenue generating capabilities as follows:-

- 4.3.2.1 Trading services (services that should generate predetermined surpluses that can be used to fund other services rendered.
- 4.3.2.2 Economic services (services that should at least break-even, but do not necessarily generate any surplus to fund other services rendered by the municipality);
- 4.3.2.3 Rates and general (services that are funded by property rates, government grants or surpluses generated by the trading services).

4.3.3 Funding of the Operating Budget

The operating budget shall be financed from the following main sources of revenue:

4.3.3.1 Property rates

- Property rates levied according to the Municipal Property Rates Act and property rates policy based on the market values
- The budget is compiled using the latest approved Valuation Roll and any supplementary Valuation Roll, consistent with current and past trends
- Property rates tariffs are determined annually as part of the tariff setting process;
- Property rates rebates, exemptions and reductions are budgeted either as revenue foregone or as a grant as per the MFMA Budget circular 51 depending on the conditions thereof;
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4.3.3.2 Service charges (electricity, refuse, sanitation, water)

- Projected revenue from service charges must be realistic based on current and past trends with expected growth considering the current economic conditions.
- The following conditions must be considered for each service:-
 - I. **Metered services comprising of electricity and water:-**
 - The consumption trends for the previous financial years
 - Envisaged water restrictions or load shedding where applicable
 - Actual revenue collected in previous financial years
 - II. **Refuse removal services**
 - The actual number of erven receiving service per category
 - Actual revenue collected in previous financial years

III. **Sewerage service**

- The actual number of erven receiving the service per category
- The consumption trends per category
- The actual revenue collected in the previous financial years
- Rebates, exemptions or reduction for service charges are budgeted either as revenue foregone or as a grant as per MFMA Budget Circular 51 depending on the conditions thereof;

4.3.3.3 Government grants and subsidies

- Revenue from government grants and subsidies shall be in line with allocations gazetted in the Division of revenue act and provincial gazettes.

4.3.3.4 Interest on investments

- Interest received from actual long-term and short-term investments shall be based on the amount reasonably expected to be earned on cash amounts available during the year according to the expected interest rate trends

4.3.3.5 Rental fees

- Revenue from rental of property shall be charged based on the percentage growth rate as determined by Financial services for a particular budget year

4.3.3.6 Fines

- Projected revenue for fines shall be charged in terms of the approved tariffs, considering the past trends calculated on the basis of actual receipts extrapolated over 12 months and expected growth for a particular budget year.

4.3.3.7 Other sundry revenue

- Other projected revenue is charged in terms of the approved sundry tariffs considering the past trends and expected growth for each category

4.3.3.8 Cash –backed accumulated surpluses from previous years not committed for any other purpose.

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4.3.4 Guiding principles when compiling the operating budget

4.3.4.1 the annual budget must be cash backed

4.3.4.2 provision for bad debt must be the difference of the actual payment levels percentage

4.3.4.3 growth parameters must be realistic, taking into account current economic conditions

4.3.4.4 tariffs adjustments must be realistic, taking into consideration affordability, bulk purchases increases and future projected growth according to the approved Integrated Development Plan

4.3.4.5 the tariffs increases should be cost reflective and as far as possible be limited to inflation targeting per budget circulars

4.3.4.6 revenue from public contributions, donations or any other grants may only be included in the budget if the following documents are received:-

- I. a signed service level agreement
- II. a contract or written confirmation
- III. or any other legally binding document.

4.3.5 Expenditure Categories

The following assumptions are used when compiling the operating budget spending:-

4.3.5.1 Salaries, wages and allowances

- A detailed salary budget shall be compiled on an annual basis
- Salaries and allowances are calculated based on the percentage increase as per the collective agreement between organized labor and the employer for the particular period
- All funded positions are budgeted for in total
- An additional 2% shall be allocated for filling of new critical positions as per the approved structure
- The remuneration of political office bearers shall be based on the limitations and percentages as determined by the responsible National Minister
- As a guiding principle the salary budget should not exceed 35% of the annual operating budget.

4.3.5.2 Collection Costs

- Will include and not limited to costs attributed to the maintenance of the financial system used for the collection of outstanding amounts based on the service level agreement including commission.

4.3.5.3 Depreciation

- Depreciation shall be budgeted for according to the asset register and to limit the impact of the implementation of GRAP 17 a transfer shall be made from the accumulated surplus
- It shall be calculated at costs, using the straight line method, to allocate the depreciation cost to the residual values over the estimated useful lives of the assets

4.3.5.4 Interest on external borrowing

- It refers to interest and redemption that has to be repaid on external loans taken up by the municipality.
- The budget is determined by the repayments that the municipality is liable for, based on the loan agreement entered into with the other party.

4.3.5.5 Repairs and maintenance

- To ensure the health of the municipal asset base, sufficient provision must be made for the maintenance

of the existing infrastructure assets based on affordable levels.

- Infrastructure maintenance costs shall be informed by the maintenance plan for each trading service

4.3.5.6 Bulk purchases

The expenditure on bulk purchases shall be determined using tariffs as stipulated by the Water boards, NERSA and any service provider from time to time.

4.3.5.7 Contributions to funds

Refers to the contributions made to provisions (**e.g. leave reserve funds**) on annual basis and is determined based on the actual expenditure in the previous year and any other factor that could have an effect

4.3.5.8 Internal charges

- These refer to inter departmental charges within the municipality.
- The performance of each line item is analysed where after the budget is based on the previous years' performance

4.3.5.9 Other expenditure

- Individual line items are to be revised annually when compiling the budget to ensure proper control over the expenditure
 - Increase for these line items shall be linked to the average inflation rate and macro-economic indicators unless a signed service level agreement stipulates otherwise.
 - As a guiding principle repairs and maintenance budget should constitute at least between 5% and 10% of the total operating budget based on the affordability levels
 - The maintenance budget percentage should increase annually be increased incrementally until the required targets are achieved.

4.3.5.10 Appropriations

It refers to the transfers to and from the capital replacement reserve to offset depreciation charges. Appropriations are determined on an annual basis.

4. DEBT MANAGEMENT

- Debt is managed in terms of the Council Credit Control Policy
- Provision for revenue that will not be collected shall be budgeted adequately as an expense and must be based on the projected annual nonpayment for services.

5. BORROWING MANAGEMENT

The borrowing requirements are based on the backlogs of the infrastructure needs taken into consideration the operational impact of any loans

6. CASH MANAGEMENT

- Cash availability shall be closely monitored to ensure a minimum cash days on hand of ninety (90) days for daily operations.

- Surplus cash not immediately required for operation purposes shall be invested in terms of the council's Investment Policy so as to maximize returns on the investments
- Municipality shall implement the inclining block tariffs and time of use tariffs

7. RESERVES

- To ensure that funding is readily available for future development and timeous replacement of aging infrastructure
- Municipality shall create dedicated reserves that are cash-backed all the time
- All reserves to be 'rein-fenced as internal reserves within the accumulated surplus, except for provisions as allowed by the General Recognised Accounting Practice (GRAP).
- The following are the recommended reserves to be re-in fenced and cash backed over a period of time:-

7.1 Capital Replacement Reserve

- The municipality shall establish the capital replacement reserve through contributions from the operating budget
- Once fully established, it shall provide internal funding for municipal capital replacement and renewal programme.
- The reserve shall be cash-backed all the time.

7.2 Bulk Capital Contributions Reserves

- This reserve shall supplement capital expenditure for the necessary expansion and upgrading of bulk infrastructure due to new developments
- Revenue generated through bulk services contributions shall be allocated to this reserve for each applicable service
- The reserve shall be cash-backed all the time

8. PROVISIONS

A provision is recognized when the municipality has a present obligation as a result of a past event and is probable, more likely than not, that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

8.1 Provisions shall be revised annually and those settled within the next twelve months are treated as current liabilities.

8.1.1 Leave Provision

10% of the leave provision shall be cash backed-as not all leave balances are to be redeemed for cash at once.

8.1.2 Landfill site rehabilitation Provision

This provision shall be cash-backed to ensure availability of cash for rehabilitation at closure.

8.1.3 Long Services Awards

5% of the long service leave provision shall be cash backed-as not all leave balances are to be redeemed for cash at once.

8.1.4 Post-Retirements Benefits

The provision for medical care benefits to qualifying retired employees shall be cash backed to ensure the availability of cash for the payment of medical aid payments

9. IMPLEMENTATION AND REVIEW OF POLICY

- This policy shall be implemented once approved by Council
- To be implemented with effect from the 1st of July 2015
- Shall be reviewed on an annual basis and tabled with other budget related policies as part of the budget process when circumstances warrant that to ensure that it is in line with the municipality's strategic objectives and legislation