

DR PIXLEY KA ISAKA SEME LOCAL MUNICIPALITY



FUNDING AND RESERVES POLICY 2024-2025

TABLE OF CONTENTS

DEFINITIONS3

1. PURPOSE5

2. OBJECTIVE5

3. FUNDING OF THE ANNUAL BUDGET5

4. CASH MANAGEMENT6

5. DEBT MANAGEMENT6

6. OPERATING BUDGET7

7. CAPITAL BUDGET8

8. RESERVES10

9. PROVISIONS11

10. OTHER ITEMS TO BE CASHED BACK12

11. APPROVAL OF POLICY AND DATE OF EFFECT12

DEFINITIONS

“Accounting Officer” – means a person appointment in terms of section 82(l)(a) or (b) of the Municipal Structures Act.

“allocation” means:

(i) a municipality's share of the local government's equitable share referred to in section 214(l)(a) of the Constitution;

(ii) an allocation of money to a municipality in terms of section 214(1)(c) of the Constitution;

(iii) an allocation of money to a municipality in terms of a provincial budget; or

(iv) any other allocation of money to a municipality by any other or another municipality, otherwise than in compliance with a commercial or other business transaction.

“Act” – means the Local Government: Municipal Finance Management Act, 2003 (Act 56 of 2003);

“Approved Budget” – means an annual budget

- a. Approved by municipal council; or
- b. Approved by a provincial or the national executive following an intervention in terms of section 139 of the constitution.

“Budget year” – means the financial year for which an annual budget is to be approved in terms of section 16 (1)

“Chief Financial Officer” – means an officer of the Municipality, designated by the Municipal Manager to be administratively in charge of the financial affairs of the municipality;

“Council” or “Municipality” – means the Municipal Council of Lekwa Local Municipality as referred to in Section 18 of the Municipal Structures Act;

“Creditor” – in relation to a municipality, means any person or service provider to whom money is owed by the Municipality;

“Debt” – means – (a) a monetary liability of obligation created by a financing agreement, note, debenture, bond, overdraft, or the issuance of municipal

securities; or (b) a contingent liability such as that created by guaranteeing a monetary liability or obligation of another.

“Delegate” – means an official / person delegated to perform tasks on behalf of another person; **“Financial Statement”** – means statements consisting of at least –

- (a) a statement of financial position;
- (b) a statement of financial performance;
- (c) a statement of changes in net assets;
- (d) any other statements that may be prescribed; and
- (e) any notes to these statements.

“Financial year” – means a year commencing on 1 July and ending on 30 June of the following year;

“Financing Agreement” means any long-term agreement, lease, instalment purchase contract or hire purchase agreement under which the Municipality undertakes to pay the capital cost of property, plant, or equipment over a period of time;

“Investment” – in relation to funds of a municipality, means –

- a) the placing on deposits of funds of a municipality with a financial institution;
- or
- b) the acquisition of assets with funds of a municipality not immediately required, with the primary aim of preserving those funds.

“Lender” – in relation to a municipality means a person or service provider who provides debt finance to a municipality;

1. PURPOSE

The funding and reserves policy is aimed to ensure that the municipality has sufficient and cost-effective funding in order to achieve its objectives through the implementation of its operating and capital budgets. This policy aims to set guidelines towards ensuring financial viability over both the short- and long-term which includes reserves requirements.

2. OBJECTIVE

The objectives of the policy are to:

- 2.1 Ensure that the MTREF framework (annual budget) of the municipality is appropriately funded.
- 2.2 Ensure that cash resources and reserves are maintained at the required levels to avoid future year unfunded liabilities.
- 2.3 To achieve financial sustainability with acceptable levels of service delivery to the community.

3. FUNDING OF THE ANNUAL BUDGET

- 3.1 An annual budget may only be funded from:
 - (a) Cash backed accumulated funds from previous years surpluses and reserves not committed for any other purpose; and/or
 - (b) Borrowed funds but only for capital expenditure.
- 3.2 Realistic anticipated revenue projections must take into account:
 - (a) Projected revenue for the current year based on collection levels to date.
 - (b) Actual revenue collected in previous financial years.
- 3.3 Capital expediting may only incur on a capital project if:
 - (a) The money for the project, excluding the cost of feasibility studies conducted by or on behalf of municipality, has been appropriated in the capital budget.
 - (b) The total cost for the project has been approved by council.

- (c) The future budgetary implications and projected cost covering all financial years until the project is operational has been considered.
- (d) The implications of the capital budget on municipal tax and tariff increases.
- (e) The sources of funding are available and have not been committed for other purposes.

4. CASH MANAGEMENT

- 4.1 The availability of cash is one of the most important requirements for financial sustainability and must be closely monitored to ensure minimum days cash on hand of forty-five (45) days for its daily operations.
- 4.2 Changes in the municipal environment that may have an impact on the municipal cash position include:
 - (a) Changes in revenue levels as a result of consumption patterns (water restrictions, load shedding etc.);
 - (b) Reduced growth as a result of economic conditions;
 - (c) Decrease in collection rate as a result of economic conditions;
 - (d) Implementation of electricity industry pricing policy (inclining block tariffs); and
 - (e) High distribution losses on electricity and water
 - (f) Increased debt levels.
- 4.3 Surplus cash not immediately required for operational purposes to be invested in terms of the municipality's investment policy to maximize the return on cash.
- 4.4 Ringfence capital grants in an interest-bearing account to lower the risk of utilisation grant for daily operations and maximize return on cash.

5. DEBT MANAGEMENT

- 5.1 Debt is managed in terms of the municipal credit control and debt collection policy and the writing off of bad debts and impairments of debtors' policy.

- 5.2 The provision for revenue that will not be collected are budgeted as an expense and is based on the projected annual non-payment rate for each service.
- 5.3 Clearly apportion all expenses incurred to provide services to the indigent customers i.e. Water services (Hiring of water tankers, Maintenance of boreholes and windmills)

6. OPERATING BUDGET

- 6.1 The operating budget provides funding to departments for their medium-term expenditure as planned.

The municipality categorizes services rendered to the community according to its revenue generating capabilities;

- (a) Trading services – services that generate surpluses that can be used for cross subsidization to fund other services.
 - (b) Economic services – services that break even with no surpluses.
 - (c) Rates and general services – services that are funded by rates, surpluses generated by trading services, and/or other revenues generated such as fines, interest received, grants and subsidies etc.
- 6.2 The operating budget is funded from the following main sources of revenue:
 - (a) Property rates.
 - (b) Surpluses generated from service charges.
 - (c) Government grants and subsidies.
 - (d) Other revenue, fines, interest received etc.
 - 6.3 The following guiding principles apply when compiling the operating budget:
 - (a) The annual budget must be balanced.

- (b) Growth parameters must be realistic taking into account the current economic conditions.
- (c) Tariff adjustments must be realistic, taking into consideration the general inflation, affordability, bulk increases and the demand according to the approved integrated development plan (IDP).

7. CAPITAL BUDGET

- 7.1 The capital budget provides funding for the municipality's capital programme based on the needs and objectives as identified by the community through the integrated development plan and provides for the eradication of infrastructural backlogs, renewal and upgrading of existing infrastructure, new developments and enlargement of bulk infrastructure.
- 7.2 Provisions on the capital budget will be limited to availability of sources of funding and affordability. The main sources of funding for capital expenditure are:
 - (a) Accumulated cash back internal reserves;
 - (b) Borrowings;
 - (c) Government grants and subsidies; and
 - (d) Public donations and contributions,
- 7.3 The following guiding principles applies when considering sources of funding for the capital budget:
 - a) Government grants and subsidies:
 - (i) only gazette allocations or transfers as reflected in the Division of Revenue Act or allocations as per provincial gazettes may be used to fund projects;
 - (ii) the conditions of the specific grant must be taken into consideration when allocated to a specific project; and
 - (iii) government grants and subsidies allocated to specific capital projects are provided for on the relevant department's operating budget to the extent the conditions will be met during the financial year.

- (b) In the case of public contributions, donations and/or other grants, such capital projects may only be included in the annual budget if the funding is guaranteed by means of:
 - (i) signed service level agreement;
 - (ii) contract or written confirmation; and/or
 - (iii) any other legally binding document.
- (c) Public donations, contributions and other grants are provided for on the relevant department's operating budget to the extent the conditions will be met during the financial year.
- (d) The borrowing requirements as contained in the borrowing policy are used as a basis to determine the affordability of external loans over the medium-term income and expenditure framework. The ratios to be considered to take up additional borrowings:
 - (i) long-term credit rating of BBB;
 - (ii) interest cost to total expenditure to not exceed 8%;
 - (iii) long-term debt to revenue (excluding grants) not to exceed 45%;
 - (iv) payment rate of above 95%;
- (e) Allocations to capital projects from cash back internal reserves will be based on the available funding for each ring-fenced reserve according to the conditions of each reserve as follows:
 - i) infrastructure projects to service new developments and the revenue is received through the sale of erven must be allocated to the capital reserve for services;
 - (ii) capital projects of a smaller nature such as office equipment, furniture, plant and equipment etc. must be allocated to the capital reserve from revenue which is funded from the revenue budget for that specific year. A general principle is that these types of capital expenditure should not exceed more than 1% of total operating expenditure;
 - (iii) capital projects to replace and/or upgrade existing assets will be allocated to the capital replacement reserve; and/or

(iv) capital projects to upgrade bulk services will be allocated to the capital bulk contributions reserve for each service.

7.4 All capital projects have an effect on future operating budget therefore the following cost factors should be considered before approval:

(a) Additional personnel cost to staff new facilities once operational;

(b) Additional contracted services, that is, security, cleaning etc.;

(c) Additional general expenditure, that is, services cost, stationery, telephones, material etc.;

(d) Additional other capital requirements to the operate facility, that is, vehicles, plant and equipment, furniture and office equipment etc.;

(e) Additional costs to maintain the assets;

(f) Additional interest and redemption in the case of borrowings;

(g) Additional depreciation charges; and

(h) Additional revenue generation. The impact of expenditure items must be offset by additional revenue generated to determine the real impact on tariffs.

8. RESERVES

8.1 All reserves are “ring fenced” as internal reserves within the accumulated surplus, except for provisions as allowed by the general recognized accounting practices (GRAP). 9.2 The following ring-fenced reserves exist:

(a) Capital reserve for new developments This reserve is used to fund capital expenditure to service new developments. Each development is ring fenced within this reserve. The valuer determines the price for the erven to be sold and the revenue generated through the sale of erven is then allocated to the specific development. This reserve must be cash backed to ensure the availability of cash to fund the capital expenditure required to service the erven.

(b) Capital replacement reserve Funding for capital budgets of future financial years is generated through a combination of methods. Once a municipality has reached its maximum gearing ability no further borrowings can be

taken up. This necessitates that the municipality also invests in a capital replacement reserve, however, it must be cash backed.

This reserve once fully established will enable the municipality to provide internal funding for its capital replacement and renewal programme.

Other contributions to the capital replacement reserve through the operating budget are:

- (i) interest received on investments;
- (ii) surface rentals from mines as identified from time to time; and This reserve must be cash backed to ensure the availability of cash to fund the municipal capital programme.

(c) Bulk capital contribution reserves;

This reserve is to supplement capital expenditure for the necessary expansions and upgrading of bulk infrastructure due to new developments. Revenue generated through bulk services contributions are allocated to this reserve for each applicable service. This reserve must also be cash backed.

9. PROVISIONS

A provision is recognized when the municipality has a present obligation as a result of a past event and it 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.

Provisions are revised annually and those estimates to be settled within the next twelve (12) months are treated as current liabilities.

The municipality has the following provisions:

- (a) Leave provision Liabilities for annual leave are recognized as they accrue to employees. An annual provision is made from the operating budget to the leave provision. Due to the fact that not all leave balances are redeemed for cash, only 75% of the leave provision is cash backed.
- (b) Landfill rehabilitation provision; landfill site rehabilitation provision is created for the current operational site at the future estimated time of

closure. The value of the provision is based on the expected future cost to rehabilitate the landfill site. This provision must be cash backed to ensure availability of cash for rehabilitation on closure.

- (c) Long services award: Municipal employees are awarded leave days according to years in service at year end. Due to the fact that not all long service leave balances are redeemed for cash, only 75% of the long service leave provision is cash backed.
- (d) Post employment medical care benefits: The municipality provides post-retirement medical care benefits by subsidizing the medical aid contributions to retired employees and their legitimate spouses. The entitlement to post-retirement medical benefits is based on employees remaining in service up to retirement age and the completion of a minimum service period. The expected cost of these benefits is accrued over a period of employment. This provision must be cash backed to ensure the availability of cash for the payment of medical aid payments.

10. OTHER ITEMS TO BE CASHED BACK

10.1 Donations, public contributions, unspent grant funding

Revenue received from conditional grants, donations and funding is recognized as revenue to the extent that the municipality has complied with any of the criteria, conditions or obligations embodied in the agreement. Unspent amounts in relation to donations, public contributions and unspent grant funding are therefore retained in cash and are not available to fund any other items on the operating or capital budget other than that for which it was intended for.

11. APPROVAL OF POLICY AND DATE OF EFFECT

The Funding and Reserves Policy of Dr Pixley Ka Isaka Seme Local Municipality shall come into effect on 1 July 2025.

**MA NGCOBO
MUNICIPAL MANAGER**

DATE