Modernising Financial Governance

Implementing the Municipal Finance Management Act, 2003

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Foreword

The Municipal Finance Management Act (*MFMA*) aims to modernise budget and financial management practices in municipalities in order to maximise the capacity of municipalities to deliver services to all their residents, customers and users. It also aims to put in place a sound financial governance framework, by clarifying and separating the roles and responsibilities of the executive mayor or committee, non-executive councillors and officials.

The Act empowers the mayor (or executive committee) to provide political leadership by taking responsibility for policy and outcomes, and holds the municipal manager and other senior managers responsible for implementation and outputs. Non-executive councillors are empowered to play a key policy-approval and monitoring role through the municipal council. The Act aims to enable managers to manage, but to make them more accountable.

All these various roles are possible because of the stringent reporting requirements of the Act – the challenge facing all stakeholders is their capacity to use the management information produced in terms of the Act to improve the efficiency and effectiveness of the municipality.

The Act is required by the Constitution, which obligates all three spheres of government to be transparent about their budgets and financial affairs. It also forms an integral part of the broader reform package for local government outlined in the White Paper on Local Government in 1998. The Act must be read together with other local government legislation, particularly the Municipal Systems Act, to ensure alignment of IDPs, budgets, performance systems and governance across municipal entities.

The Act takes effect on 1 July 2004, and replaces all other legislation that governs municipal financial management; details of the legislation to be replaced will be outlined in future *Government Gazettes*. Given the fundamental transformation of current practices required, the Act will be phased in over the next three years, taking into account the capacity of municipalities. The implementation of the Act is a unique opportunity for each municipality to reap great benefits for all stakeholders if it is done properly. To ensure this, I want to urge municipalities not to rush to implement the Act as a once-off event and to comply nominally with rules rather than the underlying principles. It would be better to phase in the Act in a way that leads to sustainable and continuous improvement each year. There are no easy answers to how best to implement the Act, and the solutions cannot be found in the National Treasury or even in the private sector – it is the practitioners in every municipality who can and must find ways to do so, and I would therefore like to encourage innovative municipalities or officials to provide information on their best practices. The National Treasury (not being a municipal practitioner) will facilitate these collective or peer-learning approaches by promoting such best practices. Such transformation is necessary even for the many private sector and teaching institutions that want to provide management, budgeting, financial or accounting services for municipalities.

This Guide is the first in a series of publications developed by the National Treasury to help municipalities and other important stakeholders implement the changes brought about by the introduction of the Act, not only the letter of the law but also its spirit. Its title, "Modernising Financial Governance…" represents the core thinking behind the legislation.

I wish you well in your reform programme.

Trevor Manuel
Minister of Finance

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The purpose of the Guide

The purpose of this Guide is to provide practitioners, and others interested in local government, with an initial understanding of the context and content of the *MFMA*.

It provides mayors, councillors, municipal officials, communities and other stakeholders with a first point of reference in familiarising themselves with their new responsibilities in municipal financial management.

The Guide provides readers with a thorough understanding of the intent of the legislation and its implications for local government and for the elected members and officials that serve within it.

How to use this Guide

The Guide is not a legal document, nor does it provide legal opinion or interpretation on any matter contained in the legislation. It should therefore be used only to obtain general advice and assistance to help practitioners develop their broader understanding. It should not be read in isolation of the Act or acted upon without legal advice.

Disclaimer

This Guide is compiled using the latest information available from departmental and other sources. Some of this information may be subject to further amendment.

PART ONE

VISION AND UNDERLYING PRINCIPLES

Chapter 1: Vision

Background

The Municipal Finance Management Act (*MFMA*) aims to modernise budget and financial management practices in municipalities in order to maximise the capacity of the municipalities to deliver services to all their residents, customers and users. It also gives effect to the principle of transparency as required by sections 215 and 216 of the Constitution.

The *MFMA* must be read together with three other critical pieces of legislation: the Municipal Structures Act, the Municipal Systems Act and the Property Rates Act. All four of these Acts have been designed to give effect to the 1998 White Paper on Local Government, which aims to transform municipalities to become more participatory, transparent and accountable.

Past practices

The Act replaces the current antiquated system of local government finance inherited from the previous rules-bound dispensation in 1994, which focused on rules and procedures rather than on sound outcomes. These practices included one-year, detailed line-item budgets, which did not allow for forward-planning or long-term strategic planning. Previous practices were one-dimensional, financial processes that were generally centrally controlled by prescribed bureaucratic rules and regulations that stifled managerial efficiency, inhibiting innovation and information and often resulting in poor decision-making and a passive approach to financial management generally.

Financial planning within municipalities tended toward short-term outputs that were not necessarily integrated into long-term outcomes. Budgets typically catered for immediate demands with little or no view to future needs or the future consequences of particular decisions. This often resulted in councils allocating resources based on historical commitments rather than looking at current priorities and future community needs.

Municipal practices were not rooted in a culture of performance and regular reporting. Reports were often irregular or inaccurate, or contained too much or too little information, with a lack of proper analysis to guide the council. Executive mayors/committees did not receive monthly budget reports from the municipal manager. Municipalities did not publish annual reports with non-financial performance information and did not submit their financial statements for audit on time or in some cases at all. The lack of effective monitoring and reporting systems often resulted in councils finding out too late about any financial problems that had arisen. Councillors could not play a leadership or oversight role, and neither could the community participate due to an opaque and non-strategic budget process.

New approach in modernising financial management

The Act therefore supplements conventional procedural rules with a performance-based system focusing on outputs and measurable objectives, to enable municipalities to maximise their capacity for service delivery.

The principles behind the reforms aim to improve financial affairs in local government and develop a more strategic approach to local service delivery. The Act establishes requirements for municipalities to consult effectively with their local communities, to work with other spheres of government and to focus on more sustainable means to deliver services.

The Act empowers councillors to play their constitutional role as politically elected representatives of the community and residents by approving policies and budgets proposed by the executive mayor or committee and then overseeing the performance of the municipality in implementing these policies and budgets. For this reason, the Act assumes a separation between councillors serving on the executive (i.e. mayor or executive committee) and non-executive councillors. The executive mayor or executive committee are expected to provide the municipality with political leadership, by proposing policies, budgets and performance targets for the municipality and its officials.

The Act also differentiates between the role of executive councillors and their officials by making the executive mayor or committee responsible for *policy* and *outcomes* and the municipal manager and other senior managers for *implementation* and *outputs*. The executive mayor or committee is expected to oversee the performance of its officials, using the service delivery and budget implementation plan and monitoring performance through monthly progress reports. Non-executive councillors are expected to hold both the executive mayor or committee and the officials accountable for performance, on the basis of monthly, quarterly and annual reports.

This separation of responsibilities between executive councillors, non-executive councillors and officials is important for good governance and is in line with modern practices of effective public management. The aim of the Act is to allow managers to manage, but to make them more accountable.

All these various roles are possible only because of the reporting requirements of the Act, as the Act recognises that effective service delivery is possible only with good-quality and timely management information. Such information allows management to be proactive, identifying and solving problems as they arise. The challenge facing all stakeholders is their capacity to use the information produced in terms of the Act to improve the efficiency and effectiveness of the service delivery of the municipality.

Maximising service delivery and continuous improvement

The Act aims to assist municipalities to maximise their capacity to deliver services. It will be a powerful tool to assist the executive mayor or committee, municipal manager and senior managers to achieve this objective. However, the benefits will materialise only if the municipality genuinely transforms itself, commits itself to making a fundamental break from past practices and focuses its efforts on a performance-driven approach to service delivery.

The transformation is quite fundamental, requiring some sections of the Act to be phased in over the medium term, commencing on 1 July 2004. Certain key sections will have to take effect immediately, owing to the importance of the provisions and their underlying principles for good financial management practices. The key point is that all municipalities must start to implement the Act in a sequenced and prioritised manner, recognising the need to reform internal processes, practices, policies and documentation. This will assist the municipality to prepare for full and qualitative implementation over the next three years. For this reason, municipalities need to adopt an approach of CONTINUOUS IMPROVEMENT over the next few years. This means that municipalities should strive to improve the content and quality of their financial management each year, measuring their progress in this regard after the end of each financial year.

The changed practices will affect all stakeholders, but particularly the municipal manager, other senior managers and finance officials. The municipal manager, senior managers and finance officials will require further training to ensure that the quality of management improves with the implementation of the Act. The mayor and councillors will benefit from attending workshops designed to assist them to reap the benefits of this Act read in association with the Municipal Systems Act. Most affected, however, will be the chief financial officer and all other finance officials, who will need more intensive training than other officials.

Improvement in skills and qualifications

Most current finance officials lack the broader skills to fully implement the *MFMA*, as do current municipal treasuries, since they have largely been accustomed to operating within a rules-driven environment, often steeped in a bean-counting culture out of step with modern management practices. The establishment of a Budget and Treasury Office provides a once-off opportunity to break with these past practices by setting up a ***new*** structure comprising highly qualified and competent professionals and a ***new*** culture that provides the municipality with fiscal and financial leadership. For this reason, the Minister of Finance has encouraged treasury and finance officials to form a new professional body to support and develop such officials – in this respect, given the similar approach of the Public Finance Management Act (PFMA) and the need for mobility between different spheres of government, the Minister has urged the merging of current bodies into a single new professional body. This call will require the promotion of a new corps of public sector finance and budget professionals – going beyond current narrow qualifications, which are not adequate in modern organisations or in the public sector. It will, however, also require a specific public sector approach, embracing the principles of "Batho Pele" and selfless service delivery to the public, which differ from current public sector practices and private sector professional associations.

Implementation of the Act will be an exercise of collective learning, and the National Treasury will promote peer-learning approaches developed by innovative municipalities to provide an opportunity to learn from current best practices. The National Treasury will recommend different courses for training both senior managers and treasury/finance officials. Mandatory courses will be phased in over the next three years and municipalities must ensure that relevant officials successfully complete these courses. The National Treasury strongly advises municipalities NOT to send their officials on courses that are not approved by the Treasury – many such unapproved courses lack a proper understanding of the reforms and they often train officials incorrectly.

Summary

This guide aims to assist municipal councillors and officials to implement the Act by planning a comprehensive programme for implementing the more demanding provisions and processes envisaged in the Act. Given that the Act is to be phased in over the next three years, municipalities are encouraged to develop their own capacity to implement the Act over this period and to refrain from resorting to the use of external consultants in order simply to comply NOMINALLY.

The key policy theme is to enable managers to manage, but to make them more accountable.

The long-term vision is to create a sector that has –

- sound financial systems and processes, producing the necessary information for managers;
- transparent budgeting processes;
- effective management of revenue, expenditure, assets and liabilities;
- unqualified financial statements, prepared on the accrual basis and on time.

In the short term, progress towards this vision will require each municipal manager to address immediate steps set out in the following chapters.

Chapter 2: Five underlying principles

The five underlying principles in the *MFMA*, which form the basis of the key reforms envisaged in the Act, are consistent with the other legislation on local government. It is anticipated that these principles and the specific reforms that flow from them will encourage a **stronger, better managed and more accountable local government** sphere, one that is better placed to meet the emerging demands and new challenges of the different communities that it serves in a more consistent and sustainable manner. The following principles are discussed:

- ***Promoting sound financial governance by clarifying roles***
- ***A more strategic approach to budgeting and financial management***
- ***Modernisation of financial management***
- ***Promoting co-operative government***
- ***Promoting sustainability***

The Act also gives effect to the constitutional principle that recognises that the local sphere of government is "distinctive" and "independent", with the power to determine its own budget and policies. It also recognises the approval and oversight role of the municipal council, as a legislature in its own right.

Being a distinctive government, each municipality has the right to determine its own budget with its own priorities and to collect property taxes, municipal levies and user charges. Given that the three spheres of government are also "interrelated", the provincial or national sphere can, in terms of section 139 of the Constitution, intervene in a municipality only when there is an executive failure or a budget or financial crisis. The *MFMA* brings greater responsibility, as it requires greater accountability to the municipal council and local community.

Promoting sound financial governance by clarifying roles

> *The MFMA and the Municipal Systems Act are central to developing the governance framework within a municipality, clarifying and separating the roles of mayors, councillors and officials, and the system of accountability and oversight.*

Empowerment, accountability and oversight

One of the most important objectives underpinning the *MFMA* is that of developing sound financial governance within every municipality. This means developing a comprehensive system clarifying (and separating) the responsibilities of mayors, councillors and officials. This framework is built around the responsibilities of **accountability** and **oversight**, which are in turn possible only if there is a culture of transparency and regular reporting in that municipality.

Confusing or duplicating responsibility tends to weaken accountability and oversight mechanisms, hence the need for separating responsibilities. The executive mayor or committee is responsible for providing the municipality with political leadership, proposing policy and overseeing its implementation. The council retains responsibility for approving policy and exercising oversight over its mayor, and the administration is accountable to the council via the mayor. Officials are responsible for implementation and for providing the executive mayor or committee with professional advice.

The council holds the mayor responsible for promised *outcomes* and the municipal manager for specific *outputs*. The mayor is expected to oversee and manage the municipal manager to ensure delivery on the agreed outputs, and the council must exercise oversight over the executive mayor or committee to ensure they fulfil this responsibility of oversight. The mayor must ensure that such outputs form part of the municipal manager's performance agreement, which must be revised at the start of the financial year so as to be consistent with the budget and service delivery and budget implementation plan (SDBIP).

For these reasons, the Act stipulates certain procedures and assigns specific responsibilities to the council, the mayor, councillors and municipal officials, in particular the municipal manager and chief financial officer.

The financial governance framework is summarised in Table 1 below:

Table 1: The Financial Governance Framework

	Responsible for	Oversight over	Accountable to
Council	Approving policy and budget	Mayor	Community
Mayor	Policy, budgets, outcomes, management of/oversight over municipal manager	Municipal manager	Council; public
Municipal manager	Outputs and implementation	Administration	Mayor; council; public
Chief financial officer	Outputs	Financial management	Municipal manager

A more strategic approach to budgeting

*By adopting three-year budgets linked to longer-term IDPs, municipalities can adopt more **forward-looking** and **better-informed** approaches and make **better judgements** about the future priorities for capital development and service delivery in their communities.*

Forward-looking and long-term planning

In the past, budgets were incremental (one-year) and backward looking, as they were based on the previous year's budget. The budgeting and planning processes were not integrated, often operating completely separately (with an iron wall between them). Budgets were presented in considerable detail, hampering effective policy and planning processes and making consultation unwieldy; revenue and capital estimates were unrealistic, resulting in poor service-delivery performance and disappointing community expectations; and there appeared to be little or no linkage to a comprehensive long-term fiscal or financial strategy.

The reforms of the Municipal Systems Act could not be properly implemented with such antiquated budgeting practices. After 2000, municipalities therefore adopted long-term integrated development plans (IDP) that were not linked to budgetary resources based on unrealistically high revenue projections. Municipalities were unable to implement such IDPs, as there were not sufficient funds in their budgets.

The *MFMA* addresses these deficiencies by requiring all councils to adopt new approaches to budget preparation, monitoring and implementation. These approaches must be considered in conjunction with the provisions of the Municipal Systems Act and the Property Rates Act, as the budget and the IDP must be aligned every year and all taxes and revenues must be adopted with the budget.

Though not legislated as a requirement, municipalities should strive to prepare a long-term ten to twenty-year vision and prepare an IDP covering at least five years. Such a long-term vision and IDP must be based on realistically projected revenue, and the IDP must be revised every year so that both are consistent with each other. In developing a long-term vision and future priorities, municipalities must not neglect or under-estimate the cost of current services and priorities, unless specific services or priorities are explicitly terminated.

Three-year budgets by vote (function) and programme (sub-function)

As with the national and provincial governments, municipalities will have the opportunity to table three-year budgets, by vote or function, i.e. electricity, water, etc., subdivided into programmes, and to manage their finances across a three-year timeframe, through a continuous cycle of forecasting, implementation and review. This approach will promote a performance management culture. Together with the Service Delivery and Budget Implementation Plan, these are important reforms and when implemented will ensure that an accountable and performance-driven service delivery culture is introduced. This key reform initiative will be a subject of a comprehensive budget guide to be issued shortly.

Like all governments, municipalities often focus on three different budgets covering five years. This is because the municipality prepares the budget for the next three years, it is still implementing the current year's budget and it is also closing off and preparing financial statements and annual reports for the previous financial year.

By taking a more strategic approach to budgeting and financial management, municipalities are required to consider the impact of their decisions into the longer term.

Modernisation of financial management

The MFMA recognises that financial management systems, processes and policies in local government must be modernised to help strengthen the municipality's ability to function effectively.

Financial management system improvements

Rather than nationally prescribed rules and procedures, the Act sets local government national norms and standards. This approach is similar to the King II corporate governance practices (the second King Committee on Corporate Governance, released in March 2002, updated the original and adds a specific reference to local government), which recognise that such best practices can be implemented only through an ethical and performance-based culture, and *not* by a purely rules-based culture. Hence mayors and managers are expected to take the national norms and standards into account when setting internal procedures, processes and mechanisms. These standards help to facilitate better performance, measurable outcomes, reformed accounting practices, improved disclosure and reporting, and best practice management techniques and prescribe certain actions for the prudent management of a municipality's assets and liabilities and other initiatives.

The legislation advocates a separation of roles and clearly describes the fiduciary and other responsibilities of the various stakeholders in order to develop reasonable operational accountability. It demands more accurate and timely financial reporting to better inform councils and communities of decisions and progress toward planned objectives. The Act also promotes a more strategic approach to financial management, linking the municipal budget, IDP and finances, and calls for in-year reporting on performance and implementation.

The reforms aim at building the institutional structure of an organisation by placing emphasis on the following three key objectives:

- To encourage a **disciplined approach** to financial management and service delivery (this includes having realistic revenue expectations when passing a budget to ensure that outcomes are achieved)
- To assign **resources** in line with strategic priorities, linking plans and budgets to long-term goals and providing a process that allows resources to be reallocated as policy objectives change
- To encourage operational **efficiency** where managers are given the authority to run their operations, subject to clear statements of procedure and strategy and clarity of roles, and are held accountable for the results produced

Promoting co-operative government

In addition to the Constitution, the Municipal Structures Act, the Municipal Systems Act (MSA) and the annual Division of Revenue Act, other legislation – the Property Rates Act (when promulgated), the National Land Transportation Act, the Housing Act, the Electricity Act and the Water Services Act – also has an impact on the *MFMA*. Section 10 of the Water Act allows the Minister of Water Affairs to cap municipal water tariffs; section 94(c) of the MSA similarly allows the Minister for Provincial and Local Government to cap the tariff for property rates.

In order to provide investors with comfort regarding guaranteed revenue streams, the *MFMA* allows exemption from the relevant provisions of these Acts if the municipality consults with the relevant national government departments before entering into long-term contracts and pledging their revenue streams.

The chapter of the *MFMA* on co-operative government seeks to promote co-operative approaches to fiscal and financial management within sectors as well as forging links with other spheres of government and organs of state. For example, it requires bulk providers of services to consult on pricing policies that impact on municipal services and sets a procedural framework for resolving financial disputes between organs of state.

Working together (working with other governments in the three spheres)

> *The MFMA fosters a greater level of co-operation across (and within) the different spheres of government, based on systems of mutual support, information sharing and communication and co-ordination of activities – each aiming to add value to the others' constitutional responsibilities with a view to improving outcomes for all.*

National, provincial and local government

Municipalities and other organs of state must promote **co-operative government**; municipalities must meet their financial commitments and provide other municipalities and provincial and national government with budget and financial information as required. They must inform neighbouring municipalities and provincial or national organs of state about any material financial and budget matters that may impact on them directly or indirectly (e.g. on their planning processes for related services).

The district municipality has a role in the overall planning and co-ordination of all local municipal budgets. It will also help facilitate the strategic planning process across municipalities within the district by receiving all IDPs with three-year budgets and annual performance reports for consolidation and forwarding to the relevant province. The provincial treasury can, in turn, co-ordinate such plans with provincial and national infrastructure and service plans.

National and provincial treasuries will assist and support a municipality's compliance with the *MFMA*, notwithstanding the municipality's own responsibilities in this regard, and will help to build a municipality's capacity and help identify and resolve its financial problems where necessary. National and provincial governments have to publish three-year local government grant allocations per municipality with their budgets, to allow municipalities to devise strategic plans for their activities. The Act also establishes a timeframe for national departments to advise municipalities of any tax and tariff capping policies and provides for national or provincial departments that supply bulk resources, like electricity and water, to municipalities to consult those municipalities about their price-setting policies.

The Act also requires the mayor to report to national and provincial government any instance in which the municipality does not comply with the Act. It describes the consultative process required by municipalities on various financial matters and lays out the process for provincial interventions to resolve financial problems.

Co-operative government

A summary of the framework for co-operative government is provided in Table 2 below:

Table 2: Co-operative Government

<> NATIONAL GOVERNMENT <>

Assists and supports municipalities with compliance where appropriate, assists in building capacity by providing financial or technical assistance, issues guides, manuals and regulations and provides three-year grant allocation details

<> PROVINCIAL GOVERNMENT <>

Plays a co-ordinating role in rollout of the *MFMA*, assists and supports municipalities where appropriate, intervenes when financial problems become evident in municipalities

<> LOCAL GOVERNMENT <>

Provides the other spheres of government with appropriate financial and service-delivery information, liaises with other municipalities and districts on strategic budget issues, provides provincial and national government with budget and financial information

Promoting sustainability

Sustainable local government is built on the basis of balanced budgets, as unfunded deficits are not allowed. Municipalities will have to take full responsibility for their actions and should not expect national or provincial government to bail out badly managed municipalities. Prioritising the level of service delivery and ensuring costs that are affordable to ratepayers as well as the continuation of routine maintenance will guarantee the sustainability of the service offered by the municipality.

Sustainability and the MFMA

The purpose of the *MFMA* is not to introduce a regime of control over local government, but rather to establish the basis for improved financial management, which is essential to improve service delivery and sustain municipal services into the future. Only badly run municipalities that fail to fulfil their executive obligations or are in a financial crisis will face intervention from provincial or national government.

Once municipalities receive their national and provincial grants, they must not expect additional resources to bail them out. Each municipality must act responsibly, and national and provincial government will not provide any guarantees on behalf of a municipality, nor reward badly managed municipalities with more funds every time they spend beyond a balanced budget.

Without compromising or impeding a municipality's right to exercise its powers or perform its constitutional functions, the *MFMA* regulates matters in a manner that creates a **more sustainable local government** sphere. Municipalities will have to pass budgets that are fully funded and borrow only for current and capital expenditure. Municipalities will therefore be allowed to spend only from money they have collected, as no borrowing for current expenditure may be carried over to the next financial year.

The issues of further strengthening accountability, oversight, transparency, clarity regarding roles and responsibilities and communication and empowerment remain central to the legislation.

An early warning system

The *MFMA* requires more regular and accurate financial reporting to the council in order to facilitate an environment in which potential or real financial problems are reported in a timely and appropriate manner that will allow council to remedy the situation.

The municipal manager must now submit monthly budget progress reports to the mayor and provincial treasury and a mid-year budget report and performance assessment to the mayor, the provincial treasury and the National Treasury by 31 January each year. The mayor must table the quarterly report to Council.

The municipal manager must also report to council on prescribed withdrawals from bank accounts each quarter and on unforeseen or unavoidable expenditure or expenditure that is deemed to be unauthorised or irregular or fruitless and wasteful.

Analysing the financial implications of decisions

Councils must adopt credible budgets with realistic revenue and expenditure estimates. Deficit budgets are no longer permitted and budgets must accommodate all operational and maintenance costs anticipated by the municipality.

Capital projects must be budgeted for and must be evaluated with due consideration of their projected and future operational costs. Long-term borrowing or debt must be more closely examined, together with contracts that exceed three years in duration and proposals to participate in a municipal entity or public-private partnership.

Municipalities must put in place robust systems of internal control and actively review their financial management systems to improve the efficiency and effectiveness of their processes. More regular and current financial reporting is required and must be made available to the community and other spheres of government.

Financial accountability

Councillors now have a greater responsibility of oversight over municipal finances and are therefore required to exercise greater diligence in the financial affairs of the municipality through quarterly monitoring and annual reports. There is a more disciplined role for all councillors to account to their communities for service delivery and financial performance.

Summary

The five underlying principles of the *MFMA* set the strategic focus of the reform agenda, which, when completed over the next three to five years, will usher in a new era in municipal financial management.

Chapter 3: The MFMA, the MSA and other national legislation

The Municipal Finance Management Act must be read with other national legislation, particularly close linkages and alignment between the Municipal Finance Management Act and the Municipal Systems Act. This should be recognised early on for a better understanding, correct interpretation and application of the two pieces of legislation. These two Acts are complementary to each other in many areas, and should therefore be read together. For example, chapter 5 of the MSA deals with IDPs and the preparatory process, whilst chapter 4 of the MFMA deals with budgets and their preparatory process. These two processes are however ONE process, and not two separate processes, as the IDP and budget must be fully aligned and consistent with each other.

The earlier chapter draws attention to these linkages with other legislation that sets foundation of the system and structure of local government but also important is the sector specific focus in other different legislation. These include, the Constitution of the Republic, Intergovernmental Fiscal Relations Act, Structures Act, Demarcation Act, Property Rates Act, Water Services Act, Electricity Act, Transport Act, annual Division of Revenue Act and their supporting regulations. Below we discuss only some of the main areas of linkages and alignment that must be considered.

Constitutional amendments

Areas of significance include recent amendments to the Constitution. The first relates to section 230A on borrowing, providing that loans may be raised for capital or current expenditure, with loans for current expenditure limited to use for bridging purposes during the fiscal year, and binding current and future councils to honour this decision. The other significant amendment relates to section 139 and deals with provincial interventions in a municipality. This allows the provincial executive to take appropriate steps in the event of a municipality's failure to fulfil an executive or legislative obligation, including the power to dissolve a council. The legislative obligation relates to the approval of a budget or other revenue-raising measures. This includes the imposition of a recovery plan in the case of an emergency when there is a persistent material breach of its obligations to provide basic services or to meet financial commitments.

The above matters will be dealt with in detail in a supporting guide to be issued later this year.

The MFMA and the Municipal Systems Act

Both the Municipal Systems Act and the *MFMA* deal with the internal processes, consultative processes, performance systems and reporting and accountability mechanisms. Parliament devoted a great deal of effort to ensure that the two Acts are totally consistent with each other, leading to amendments to the MSA. It is important to ensure that the MSA is read with the two sets of amendments, as per the Local Government Laws Amendment Act (Act 51 of 2002) and the MSA Amendment Act (Act 44 of 2003). An amended version of the MSA will be made available on the Department of Provincial and Local Government website.

Definitions
The first point to note is that the definitions in both the MSA and *MFMA* are similar, and there is much cross-referencing in the *MFMA* to definitions in the Municipal Systems Act. This applies to key definitions on municipal services, service delivery agreements, local community etc.

IDP and budgets
Mention has already been made about the need to see the process of annual revision of the IDP as the same process as that for preparing the next budget. This will ensure that the planning and budgeting processes are integrated as ONE process. For the same reason, the process leading to the adoption of the budget and IDP should be incorporated into one process, together with the process for approving or revising taxes, levies and user charges, and property rates and taxes ("budget-related policies"). This will ensure credible plans and budgets that can be implemented.

Further to the above, the *MFMA* and the Municipal Systems Act also contain more practical synergies that relate to good governance, consultation and accountability issues. A direct interrelationship exists when a municipality contemplates its processes with regards planning and budgeting. The amendment to the Municipal Systems Act and the *MFMA* chapter on budgeting require that a revised IDP be adopted at the time of adopting the budget. It follows that, in practice, the planning and budgeting processes will commence together at least 10 months before the start of the municipal financial year, when the mayor announces the process for revising the IDP and preparation of budget. Also, the alignment of policies through the adoption of the budget and other related policies such as the levying of fees for municipal services is made more explicit at the time of drafting and adopting the budget.

Performance systems and annual reports
Both the *MFMA* and MSA are built on the adoption by the municipality of a performance system. The budget of the municipality must contain performance targets and measurable objectives, which are set out at the beginning of the financial year (section 17 of the *MFMA*). Linked to these performance targets are the adoption of the annual service delivery and budget implementation plan (SDBIP) and annual performance agreement between the mayor (or executive committee) and municipal manager (refer to section 57 of the MSA as amended, and sections 53 and 69 of the *MFMA*).

At the end of the financial year, the municipality must publish an annual report, reporting on both its financial and non-financial performance. Whilst the *MFMA* focuses on financial performance (chapter 12), the MSA focuses on non-financial performance (section 46 of MSA as amended). The annual report will be considered by the municipal council using the process outlined in chapter 12 of the *MFMA*.

Procurement, supply change management and external providers
Whilst it is the *MFMA* that deals with the procurement of goods and services (procurement), the MSA is relevant when such procurement involves outsourcing of a municipal service to an external service provider. The first point to note is that the *MFMA* modernises procurement practices within the framework of the broader concept of supply chain management. Note that chapter 11 on supply chain management applies to all goods and services, including municipal services, but does not apply to recruitment or employment of staff.

The MSA only applies to municipal services, and it is important to note the definition of municipal services (MSA as revised by the LGLAA Act 51of 2002). Thus whilst the provision of services like electricity, water, sanitation and refuse removal are clearly municipal services, out-sourcing functions like collecting revenue or the provision of IT services are not municipal services. Hence chapter 8 of the MSA only applies to municipal services, and not to goods or services that are not municipal services. Note that chapter of the *MFMA* also applies to the procurement of municipal services. In addition, if an external provider is to be contracted to provide a municipal service on behalf of the municipality, both the MSA and *MFMA* apply.

All long-term contracts (i.e. longer than three years) have to comply with sections 33 and 116 of the *MFMA*, and in addition, the following sections will also apply:

a) If it is a PPP, section 120 of the *MFMA*
b) If it is a capital project, section 19 of the *MFMA*
c) If it is a contract with an external service provider, section 80 and 81 of the MSA (as amended)

Note that since new supply chain management system will be phased in over the next three years, an interim procurement system and regulations will apply for the first two to three years of implementing the MFMA.

It should be noted that procurement practices also have to comply with other national legislation like the Preferential Procurement Policy Framework Act and Broad-Based Economic Empowerment Act, etc.

In addition to the above, the linkages in section 46 of the Municipal Systems Act with the *MFMA* continue with regards annual performance reports and the need to ensure that these form part of the reports in terms of chapter 12 of the *MFMA*. In an effort to improve performance accountability and to reward excellence, section 57 of the Municipal Systems Act, which deals with performance contracts of the municipal manager, has been referenced to the *MFMA* provisions on the responsibilities of the accounting officer and further only awards bonuses at the end of the financial year after a performance assessment has been concluded and approved by the municipal council.

Municipal entities

Both the MSA and *MFMA* deal with the process to set up municipal entities, the type of entities and the governance arrangements for such entities. It is therefore important that municipalities not only comply with both Acts when setting up or governing municipal entities, but that the both Acts are seen to refer to one process for their establishment, and to one system of governance.

A whole new chapter 8A on municipal entities has been added to the MSA. The new chapter limits the type of entities a municipality may establish to only three types (private company, service utility or multi-jurisdictional service utility), and imposes a stricter establishment process for the establishment and acquisition of private companies, conditions for co-ownership etc. Before an entity is established a feasibility study should be conducted (section 84 of the *MFMA*), and if an entity is jointly owned with another organ of state, that organ of state should also conduct a feasibility study to determine impacts on budgets and staff placement and to assess commitments and liabilities.

In order to allow for proper governance arrangements, the Act prohibits councillor representation on the boards of municipal entities, and allows for appointment of non-executive directors in line with the King governance principles. In future, the performance of the entity against its service delivery agreement and specific performance objectives and indicators need to be determined for annual performance review. If the entity does not perform satisfactorily, or if it experiences serious or persistent financial problems, the municipality may disestablish the entity.

The MSA also sets out the responsibilities of the parent municipalities who have an ownership share in a municipal entity. Chapter 10 of the *MFMA* sets out strict rules of financial governance for the CEO of the municipal entity, and the financial management arrangements with regard to banking accounts, monthly reporting and fiscal powers of entities.

The financial management of all entities will in future be regulated by the *MFMA*, unless the majority share in an entity is held by a national or provincial organ of state, in which case the Public Finance Management Act (PFMA) applies.

Municipalities should take all steps necessary to convert non-compliance structures like section 21 companies, trusts and other forms. The implementation of provisions relating to entities will take effect from 1 July 2004 and all municipalities are required to report within three months on the name and address of a corporate entity, the extent, participation and particulars of the municipality's interest and whether the municipality has sole ownership and control over the entity. The chief executive officer of the entity is the accounting officer for the assignment of all *MFMA* duties and the board of directors is responsible for the governance over municipal entities.

Consultative processes

Both the MSA and *MFMA* require extensive consultations with the local community for important decisions like budgets, borrowing, IDPs, performance systems, annual reports, etc. The process of consultation is set out in the MSA, in chapter 4. To facilitate such consultations, municipalities are encouraged to set up websites, and to post all key documents on their websites.

There is a close link between the provisions of the *MFMA* and section 21 of the Municipal Systems Act with regard to the publishing of documentation. Publications must be displayed in the municipal head office and satellite offices and libraries. With technological advances, the information is also required to be published on an official municipal website.

Roles of mayor, councillors and officials

Both the MSA and *MFMA* make common assumptions about the role of various stakeholders in the municipality. Such roles also inform the code of conduct for councillors and officials as set out in Schedules 1 and 2 of the MSA. In addition, if there are financial transgressions, financial misconduct provisions and criminal sanctions apply in terms of chapter 15 of the *MFMA*. Where councillors or officials transgress their role or code of conduct, strict provisions apply.

Assignment of functions

Cooperation between governments is strengthened through these Acts, and when there is an assignment of a function or power to a municipality there must be comment by the Financial and Fiscal Commission and consultation with the Minister of Finance on the assignment, including possible liabilities. This aspect strengthens co-operative government and links with chapter 5 of the *MFMA* and directly impacts on the Division of Revenue Act. The other area of cooperation relates to the provision of services through service delivery agreements and the use of external mechanisms. An important area of alignment relates to the process of establishing an external mechanism to provide municipal services. The community consultation, assessments, capacity, feasibility studies, value for money, measurement of risk, projected borrowing and fiscal implications are all linked to the IDP and budget process.

National Treasury will issue a comprehensive guide on municipal entities.

Other legislation and the *MFMA*

The earlier sections draw attention to those linkages with other legislation that set the foundations of the system and structure of local government, but also important is the sector-specific focus. Apart from the Constitution and Municipal Systems Act and other national local government legislation like the Local Government: Municipal Structures Act, Property Rates Act and Municipal Demarcation, there are a number of national Acts of Parliament that impact on the *MFMA*. These include the following:

- Financial legislation like the Constitution of the Republic, Intergovernmental Fiscal Relations Act, Financial and Fiscal Relations Act, Preferential Procurement Policy Framework Act and the annual Division of Revenue Act
- Other local government legislation like the Municipal Structures Act, Demarcation Act and Property Rates Act
- Sectoral legislation like the Water Services Act, Electricity Act, Transport and Environment Acts

- The Remuneration of Political Office-bearers Act
- Planning legislation like the Land Development Objectives Act
- Labour legislation, including the Labour Relations Act, Skills Development Act, as well as pension and medical aid legislation

The Intergovernmental Fiscal Relations Act establishes the process of consultation for budget allocations, including the role of the Budget Forum. The annual Division of Revenue Act is one of the important pieces of budget legislation for local government, as it provides national allocations for the local government sphere by municipality, for each of the coming three years.

The Financial and Fiscal Commission Act (FFC) is also important for the local sphere. Not only does it spell out the process for filling vacancies to the FFC, but also includes rigorous provisions in the revised section 5 on the role of the FFC before any new function is shifted to any municipality. This assignment clause should also be read with section 10 of the amended MSA.

Some of the other pieces of legislation that impact on and should be read with the *MFMA* are the sectoral legislation relating to water and electricity and transport.

The Water Services Act, Act 108 of 1997, contains provisions relating to norms of standards, the development of plans and tariff mechanisms. Whilst the Electricity Act, Act 41 of 1987 (as amended), also contains provisions relating to the electricity regulator, it deals with aspects of licensing, the sale and supply of electricity within municipalities and tariffs. Note that where there is any conflict between such national legislation and the *MFMA* or MSA, it is the latter two Acts that take precedence, depending on the issue.

Particular note should be made of sections 42 and 43 of the *MFMA*, which take precedence over section 94(1)(c) and section 10 of the Water Services Act if a municipality properly consults (in terms of sections 33 and 46) with the relevant national departments when setting tariffs for long-term contracts. The applicability of these provisions and those in the *MFMA* especially that relating to budget preparation and consultation in chapter 4, co-operative government and pricing of bulk services in chapter 5 will assist in better management of processes whilst offering a mechanism for dispute resolution between organs of state. The *MFMA* requires that a structured process be followed to ensure that consultation is appropriately addressed. The improvement in the content and quality of municipal budgets will also assist. These provisions promote co-operative government between the national and local spheres in the tariff setting process. Sector departments will have to monitor the achievement of sector priorities.

The Property Rates Act contains further related provisions that deal with the adoption and contents of a rates policy, increases and their timing and documentation that must accompany the budget as outlined in the *MFMA*. It also requires alignment with community participatory processes and specifically publication of information with the budget. The period for which rates are levied is the same as the budget, unless imposed as part of a recovery plan. The limitation on increases in rates is directly aligned with the *MFMA*. There are also linkages with the supply chain management framework when securing the services of private providers in the execution of the municipal valuation exercise.

Summary

The above brief explanation should not be considered as exhaustive, but it highlights the linkages and synergies with the *MFMA* and other legislation. It also attempts to clarify the policies of government. It should serve as an illustration of the extent to which other pieces of legislation impact on the applicability of the *MFMA* and vice versa.

PART TWO

IMPLEMENTATION

Chapter 4: IMPLEMENTATION

Phased implementation

The *MFMA* will be phased in to allow municipalities adequate time to fully implement the reforms envisaged in the Act. Whilst some clauses will be delayed or exempted (in terms of sections 177 and 180), most sections of the Act will take effect on 1 July 2004. This is because *nominal* compliance with these sections will not be very difficult – the real challenge will be to implement the qualitative improvements envisaged by such sections, which will take longer to implement. An implementation document of the effective dates of all sections of the Act has been placed on the National Treasury website.

Implementing the *MFMA* is a collective learning exercise for all municipalities, and municipalities are encouraged NOT to rush implementation by contracting consulting companies. The National Treasury does not want municipalities to spend more funds on consultants for immediate compliance – rather the National Treasury is more concerned that municipalities prepare to build their own internal capacity, and do so on a more sustainable basis, without incurring unnecessary costs. Municipalities will therefore be given a reasonable period to fully comply with the Act, taking into account their current capacity, and the need to improve such capacity over the medium-term.

In implementing the *MFMA*, municipalities should also regard implementation of the 2004 Division of Revenue Act as part of the same process. This is because the 2004 Division of Revenue Act contains many transitional arrangements to assist municipalities to fully comply with the *MFMA* thereafter.

The National Treasury has conducted a survey amongst all municipalities, and classified them into three categories (i.e. high-, medium- or low-capacity) for the purpose of implementation. Due regard has also been given to capacity developed through participation in programmes supported by the Financial Management Grant and Municipal Infrastructure Grant. There will be three different dates of implementation for some reforms, with the shortest times for highly capacitated municipalities, and longer times for low-capacity municipalities. Note that the high-capacity municipalities will benefit by receiving all national grants directly in future, whilst many grants (eg MIG grants) to low-capacity municipalities may be provided indirectly, via a district municipality or even a province. A list of the three capacity-type municipalities is provided as an annexure to this document – note that as the *MFMA* is implemented, the capacity-type of a municipality will be reviewed every year, so that non-performing municipalities will be downgraded, whilst well-performing municipalities will be upgraded. The next review will take place in February 2005, as all municipalities will be expected to report by 31 January 2005 on their implementation progress as at 31 December 2004.

The first task for all municipalities is to prepare a three- to five-year implementation plan, with deadlines set by the municipality for itself. The deadlines must be realistic for the plan to be implemented. This chapter outlines the urgent and short-term steps that a municipality should prioritise when preparing its implementation plan.

The twelve URGENT steps are generally those that have to be implemented immediately, between now and 31 October 2004. These steps need to be implemented by ALL municipalities, irrespective of their capacity. Note that the only exception is compliance with section 8 of the 2004 Division of Revenue Act, where medium- and low-capacity municipalities are given more time to comply than high-capacity municipalities. It is also important that the implementation of the *MFMA* be done with the recent Municipal Systems Act amendments, particularly those related to the new chapter 8A on entities.

Given the need to assist municipalities, the more stringent financial misconduct and criminal sanction sections of the Act will not be applied in the first two years of implementation, except where there is deliberate or negligent non-compliance.

Twelve urgent steps for implementation

All municipalities, irrespective of their capacity, will need to comply with the following priorities:

- Preparing an implementation plan
- The municipal manager must be the accounting officer responsible for all funds managed by the municipality (implementation of chapter 8)
- Establishing a top management team with a person responsible for the duties of the chief financial officer (CFO) and appropriate delegations
- Implementing chapter 3 to ensure effective cash management and the control of all banking accounts by the CFO, including the primary bank account
- Meeting of financial commitments to other parties
- Monthly reporting revenue and spending for the 2004/05 budget
- Revising supply chain management policies
- Implementing the MSA amendments and *MFMA* for all corporate or municipal entities, PPPs, long-term contracts and borrowing
- Completing past financial statements and advising National Treasury (for 2003/04 financial year and before)
- Submitting 2003/04 financial statements to Auditor-General by 30 September 2004 and tabling an annual report by 31 January 2005.
- Complying with the membership provisions for tender committees and boards of entities by 1 July 2004
- Comply fully with the 2004 Division of Revenue Act, including section 8 on completing negotiations with Eskom or Water Boards as external mechanisms

Step 1: Preparing an implementation plan

The municipality must prepare a basic *MFMA* implementation plan, focusing on what the municipality intends to implement and achieve over the next three to five years. Targets should be set for each of the next five financial years. The implementation plan should be submitted to the National Treasury and relevant provincial treasury by 1 October 2004. The National Treasury is preparing a draft format for the preparation of an implementation plan. Municipalities are free to utilise this format to guide implementation. Drafts will be available on the Treasury website.

Step 2: The municipal manager must be the accounting officer responsible for all funds managed by the municipality (implementation of chapter 8)

The responsibility of the municipal manager as accounting officer will take effect from 1 July 2004 for ALL municipalities. It follows that no mayor or councillor or official can be responsible for any funds, or authorise the spending of funds. This is the most important role reserved only for the municipal manager, and any official delegated by the municipal manager to act on his or her behalf. Most of the provisions of chapter 8 will apply from 1 July 2004, though some may be delayed, and sanctions under chapter 15 will not be enforced for initial transgressions due to capacity weaknesses. However, such sanctions will be applied for any deliberate or negligent omissions or actions on the part of the municipal manager or any other official.

Step 3: Establishing a top management team with a person responsible for the duties of the CFO and delegations

Municipal managers are encouraged to formally establish a top management team if they have not done so already. This should be completed by 1 July 2004, and should include all those senior managers who are responsible for a department (or vote) or the budget of a department (or vote) or major activity. One of the critical steps is to appoint a CFO – however, given that such skills are not easily available, municipalities are encouraged to appoint their current head of treasury or another senior manager in an acting capacity of CFO, before attempting to appoint a permanent CFO. Note that given the management responsibilities of the CFO envisaged in the Act, municipalities should not assume that their current head of treasury should be appointed the CFO – the municipality should open up the process for appointing a CFO, to ensure that the municipality attracts the best skills possible for this post. Refer to the later chapter that spells out more detail on the CFO post, and the setting up of the Budget and Treasury Office.

The municipal manager should therefore complete delegations for specific responsibilities to the senior management of the municipality, to ensure effective implementation and accountability mechanisms are in place. The annexure supporting this document provides a list of delegations and describes the provisions that may be delegated.

Step 4: Implementing chapter 3 to ensure effective cash management and the control of all banking accounts by the CFO, including the primary bank account

This is one of the most urgent reforms that must be implemented by a municipality. This is to end the practice whereby any department or official of a municipality can set up a bank account, without the knowledge of the municipal manager or council. All bank accounts must be put under the responsibility of the chief financial officer (even if such person is the acting CFO), following a delegation to this effect by the municipal manager. Priority should therefore be given to implementing chapter 3 of the Act, on the management of banking accounts, and cash management and investments. Note that the primary bank account is also a requirement in terms of the 2004 Division of Revenue Act and that all grants from national and provincial government can only be paid into the primary bank account, in accordance with both the *MFMA* and the 2004 Division of Revenue Act. Non-compliance with this provision will transgress section 5 of the 2004 Division of Revenue Act, and may result in the withholding of the equitable share grant.

Step 5: Implement systems to ensure that all financial commitments are met

Municipalities must ensure that they take the appropriate steps to implement effective systems of expenditure control, and meet their financial commitments to other parties promptly and in accordance with the Act.

It is up to the accounting officer to take these steps, and ensure that all monies owing by the municipality are paid within 30 days of receiving an invoice or statement. Steps must be taken to resolve formal disputes between the municipality (or municipal entity) and another organ of state.

Step 6: Monthly reporting revenue and spending for the 2004/05 budget

Though the monthly reporting sections in the Act will be delayed to 1 July 2005 for high capacity and 2006 for low capacity municipalities, all municipal managers must take immediate steps to ensure that they report on the implementation of their 2004/05 budget, by submitting monthly reports to the mayor and on revenue collected and total spending, shortly after the end of each month. These reports should also be submitted to the council on a quarterly basis. Such reporting practice will ensure that the municipality is in a position to fully comply with section 71 once it takes effect on 1 July 2005.

These reporting practices will allow both the mayor and council to exercise an oversight role over implementation. Reports should be debated, published and used to continuously ensure performance improvement.

Step 7: Revising supply chain management policies

The National Treasury will be issuing procurement regulations along the lines of the current procurement system in municipalities, to take effect from 1 December 2004 for high capacity municipalities. Full implementation is delayed for medium capacity municipalities until 30 June 2006 and until 30 June 2007 for low capacity municipalities. In the interim, councils should commence a process of review of its existing supply chain management policies and report at least monthly to the council and at least quarterly to the mayor on progress toward implementation of the new policy.

Step 8: Implementing the MSA amendments and MFMA for all corporate or municipal entities, PPPs, long-term contracts and borrowing

All municipalities need to comply with section 178(2), by providing the National Treasury by 30 September 2004 with a list of:

a) all corporate entities under the municipality's sole control, or in which it has a share;
b) all public-private partnerships with a value of more than R1 million in total;
c) all other existing long-term contracts going beyond 1 January 2007 and over a value of R1 million.

All borrowing, PPPs, long-term contracts and new entities must be in terms of the *MFMA* and chapter 8A of the Systems Act after 1 July 2004. Note that these provisions will generally apply mainly to high- and medium-capacity municipalities who utilise these mechanisms, but will also apply to those low-capacity municipalities who want to use these mechanisms. Municipalities forming new entities, borrowing or signing long-term contracts after 1 July 2004 must comply with the approach of the *MFMA* and MSA as amended.

Priority 9: Completing past financial statements for submission to Auditor-General by 30 April 2004

All municipalities and their corporate municipal entities must ensure that all financial statements for past years (2002/03 and before) have been completed and submitted to the Auditor-General for audit no later than 30 April 2004. This is a deadline in terms of the 2004 Division of Revenue Act, and the National Treasury intends delaying the equitable share grant to any municipality that has failed to comply with this deadline. Municipalities that have failed to meet this deadline must apply for an exemption to the National Treasury, outlining their reasons for this failure, and the date by which they will submit all past financial statements for audit to the Auditor-General.

Step 10: Submitting 2003/04 financial statements to Auditor-General by 30 September 2004 and tabling of annual reports

All municipalities and their corporate municipal entities are expected to comply with this provision to submit their 2003/04 financial statements to the Auditor-General by 30 September 2004, unless specifically exempted by the National Treasury. The National Treasury has extended the normal 60 days requirement to 90 days only for the 2003/04 financial statements. Non-compliance with this provision will transgress section 5 of the 2004 Division of Revenue Act, and may result in the withholding of the equitable share grant. Municipalities are also expected to table an annual report, which will include audited financial statements for the 2003/04 financial year, by 31 January 2005.

All financial statements of municipalities and municipal entities for financial year 2002/03 and before were due to be submitted to the Auditor-General no later than 30 April 2004. Any statements that have not been submitted may result in punitive measures outlined in the Division of Revenue Act.

Step 11: Complying with the membership provisions for tender committees and boards of entities by 1 July 2004

In order to strengthen the oversight role of councillors and prevent conflicts of interest, councillors will not be allowed to serve on any bid/tender committee or board of a municipal entity from 1 July 2004. Note that this prohibition on boards of entities also applies to other elected representatives in Parliament and provincial legislatures. Further, all boards of entities should comply with sections 93E, 93F, 93D and 93I of the MSA (as amended) by 1 July 2004, and ensure that the board consist of at least one third of the directors and the chairperson should be independent and not officials.

Step 12: Comply fully with the 2004 Division of Revenue Act, including section 8 on completing negotiations with service providers in relation to electricity distribution and water supply

Municipalities are reminded that they have to comply immediately with the 2004 Division of Revenue Act, as failure to do so will lead to a delay or withholding of national grants. The Division of Revenue Act contains similar requirements (as a transitional arrangement) to the *MFMA*, on the designation of primary bank accounts, submission of past and 2003/04 financial statements etc.

A further requirement of the Act empowers municipalities to take political responsibility for the provision of services to all their residents and small businesses (but excluding services to major industrial or mining operations). This is affected through the Municipal Systems Act provisions, which require Eskom and Water Boards to provide such services on behalf of a municipality as an external service provider only, in terms of section 80 of the Systems Act. All high capacity municipalities are expected to have completed an agreement with such providers, by 30 November 2004. Medium- and low-capacity municipalities will be expected to complete such agreements by 30 November 2005.

Short and medium-term priorities for implementation

The SHORT to MEDIUM-TERM priorities are generally those that have to be implemented during the next financial year and between 1 July 2004 and 30 June 2006. However, many of these must be completed by high-capacity municipalities by 30 June 2005, with the later deadline of 30 June 2006 and 2007 applying to medium- and low-capacity municipalities.

In addition to the above URGENT STEPS, municipalities will be encouraged to prioritise the following reforms over the next two to three years:

Municipalities to implement chapter 4 for their 2005/06 budget:

- Establish Budget and Treasury Office and appoint CFO
- Conduct an audit of all corporate or municipal entities, to harmonise with chapter 8A of the Municipal Systems Act
- Establish internal audit unit and Audit Committee
- Addressing audit queries raised in 2003/04 and past audits

Priority 1: Municipalities to implement chapter 4 for the 2005/06 Budget

All municipalities will be expected to apply chapter 4 budget process to prepare their 2005/06 Budget, although certain sections will be phased. This means that all mayors will have to table their process for revising their IDPs and preparing their 2005/06 budget by 1 September 2004. Municipalities will be expected to table three-year functional budgets, and to ensure that their IDP and budgets are consistent with each other, and ensure that their revenue projections are realistic. A detailed budget manual and programme of training courses will be made available by National Treasury.

Priority 2: Establish Budget and Treasury Office and appoint CFO
High-capacity municipalities will be expected to comply with this provision by 30 June 2005. Medium- and low-capacity municipalities will have to comply by 30 June 2006. Note that these changes in organisational structure are meant to be more than cosmetic, so municipalities should ensure that they attract the new skills required to implement the Act. In the meantime, the current treasury head or another senior manager can be appointed as CFO in an acting capacity. Refer to a later chapter in this guide for more information.

Priority 3: Conducting an audit of all corporate or municipal entities, to harmonise with chapter 8A of Systems Act
The *MFMA* and Systems Act (as amended) provide a framework to enable sound financial governance over municipal entities. Given the need for better accountability, chapter 8A of the Systems Act (as amended) permits only private companies, service utilities and multi-jurisdictional service utilities. Though existing entities are allowed to continue, it is important that every municipality conduct a feasibility study to explore whether, or when, to convert existing entities into one of the three forms of entities by the new legislation. An update on progress in this regard will be required later in the year.

In addition, any entity must have the same financial year as the municipality by 1 July 2005 so that financial statements and budgets can be consolidated into those of the parent municipality.

Priority 4: Establish internal audit unit and Audit Committee
All high-capacity municipalities will be expected to establish best practice internal controls (including the establishment of internal audit units and audit committees, preparation of risk management plan) by 1 July 2006. Medium-and low-capacity municipalities will be expected to comply by 1 July 2007. Municipalities are urged not to rush to comply nominally with these provisions, but rather spend more time to ensure that appropriate persons are recruited for these committees. The National Treasury will provide a guide to assist municipalities in setting up these committees, and for the preparation of risk management plans. The guide will also explore how municipalities can share audit committees given the relative shortage of appropriate skills.

Priority 5: Addressing audit queries raised in 2003/04 and past audits
The opinion issued by the Auditor-General on the financial statements and performance report of a municipality provides an opportunity for the municipality to institute corrective measures to address any concerns raised in the audit report. Municipalities will be expected (when tabling their 2003/04 annual report) to also table its response to the audit outcome, including the corrective steps it intends to take.

Medium to long-term priorities for implementation

Note that all of the supply chain reforms will be implemented by 1 December 2004 for high capacity municipalities and the Act will be delayed to 30 June 2006 and 2007 for medium- and low-capacity municipalities. Therefore, these municipalities will be expected to prepare interim policies for such implementation from 1 July 2005, to give effect to the spirit of the *MFMA*.

Summary

Although National Treasury will provide support and host regular workshops, the implementation of the Act should be considered a learning process through which best practices may be shared between municipalities through a process facilitated by National Treasury. A dedicated website is available for publications and a *MFMA* email address will deal with implementation queries. Municipalities should provide their latest email addresses to National Treasury to receive updated information, especially where Internet access is unavailable.

Chapter 5: Chapter-by-chapter implementation

The implementation of the MFMA will be accommodated by a phased-in strategy that is based upon municipal capacity. The effective dates of the MFMA, in terms of section 180, have been published in Gazette number 26510, notice number 772, on Friday 25 June 2004. The Gazette announces that the MFMA takes effect on 1 July 2004; however certain provisions have been delayed to take effect on later specified dates. An additional Gazette, number 26511, notice number 773, was published on 1 July 2004 and lists certain sections that have been delayed or exempted in terms of section 177. The period of time of the delay or exemptions is based upon the capacity of each municipality.

The delays and exemptions are based on whether a municipality has been determined as having a low, medium or high level of capacity to implement the MFMA. Municipalities with a higher capacity will be required to comply sooner than those with lower capacities. The chart below presents a high level summary of the phased-in implementation strategy:

High level Summary of Implementation Strategy

Description	**Effective Date**	***Comments***
Role of the provincial treasuries Sections 5(3), (4) and (8)	Delayed for 1 year Applies from 1 July 2005	NT will undertake this role during interim
Municipal Budget – multi-year, new formats and process, performance measures and long term capital plans Section	Phased in according to capacity • High – 2005/06 • Medium – 2006/07 • Low – 2007/08	Linked to phase-in provisions for financial reporting; Regulations under development.
Financial reporting Section 122, 126	Generally the 2004/04 financial year Phase in new accounting standards according to capacity • High – 2005/06 • Medium – 2006/07 • Low – 2007/08	Accounting standards issued by the ASB
Annual reporting Section 121, 123-125, 127-134	Phased in according to capacity • High – 2004/05 • Medium – 2005/06 • Low – 2006/07	Guidelines developed
Supply Chain Management, Public and Private Partnerships	Generally 1 December 2004 Phased for certain provisions according to capacity • High – 1 December 2004 • Medium – 1 July 2006 • Low – 1 July 2007	Regulations to be finalised for consultation in September
Financial interventions Chapter 13	Delayed to 1 July 2005	Chapter 13
Audit committees and internal units	Phased in according to capacity • High – 1 July 2005 • Medium – 1 July 2006 • Low – 1 July 2007	Guidelines under development.
Competency levels for officials Sections 83, 107 and 119	Delayed to 1 July 2006	Unit standards submitted to SAQA
Bank account details report Section 9.	Delayed to 1 April 2005	

The phased-in implementation strategy establishes the outside boundaries of when sections of the MFMA must be in place. Municipalities that have the capacity are encouraged to implement the sections earlier.

The following chapter-by-chapter implementation outline provides a summary of the phased implementation strategy. Further information on implementation dates and the *Gazettes* have been place on the National Treasury website.

Chapter 1 – Interpretation, Object, Application and Amendment

The entire chapter is applicable from 1/7/2004.

Chapter 2 – Supervision over Local Government Finance Management

This chapter is applicable from 1/7/2004 with the exception of provisions that require further capacity to be built in the relevant organ of state prior to implementation.

Chapter 3 – Municipal Revenue

This critical chapter is applicable from 1/7/2004 except for where the DoRA applies. In this case the *MFMA* will apply on 1/4/2005 and the DoRA applies in the interim.

Chapter 4 – Municipal Budgets

The provisions of this chapter apply mainly to the 2005/06 budget. The main exceptions include the following:

- Provisions relating to multi-year budgets are delayed until the 2006/07 budget for medium and 2007/08 for low capacity municipalities.
- Provisions relating to measurable performance objectives are delayed until 2006/07 budget for high, 2007/08 budget for medium and 2008/09 budget for low capacity municipalities.
- Capital projects and contracts having future budgetary implications are delayed until the 2006/07 budget for medium and 2007/08 for low capacity municipalities.

Chapter 5 – Co-operative Government

This chapter covers responsibilities of the three spheres of government in terms of information sharing, support and monitoring.

Responsibilities of municipalities take effect for the 2005/06 budget process and include consulting other municipalities. The process leading up to the 2005/06 budget will, however, need to be implemented in high-capacity municipalities from August 2004.

Support responsibilities of the national and provincial governments take effect for the 2004/05 budget. Monitoring responsibilities and publishing of municipal allocations take effect for the 2005/06 budget to allow the national and provincial government spheres to develop appropriate capacity.

Provisions relating to the stopping of allocations to municipalities take effect from 1/4/2005 and are covered by the DoRA in the interim.

Chapter 6 – Debt

All provisions relating to municipal debt take effect from 1/7/2004 except for section 45(4)(a), which requires municipalities to pay off short-term debt within the financial year. This provision will be fully enforced in four years (by 1/7/2008) and in the meantime municipalities are required to gradually reduce their short-term borrowing, by at least 25 percent each year.

Chapter 7 – Responsibilities of Mayors

All reporting responsibilities, except those relating to the service delivery and budget implementation plan and measurable performance objectives, are generally effective from 1/7/2004. Exceptions are applicable based on capacity.

All responsibilities in relation to the budget process, except those relating to the service delivery and budget implementation plan and measurable performance objectives, are generally applicable to the 2005/06 budget process. Exceptions are applicable based on capacity.

Chapter 8 – Responsibilities of Municipal Officials

Where the provision requires the accounting officer to take all reasonable steps to ensure that various systems and controls are in place, the provision is delayed until the 2006/07 budget for medium and 2007/08 for low capacity municipalities.

Accounting officers of high-capacity municipalities must comply by 1/7/2004 and should therefore ensure that they have plans in place to review all relevant systems and are able to justify that they have taken all reasonable steps. For medium and low-capacity municipalities, the accounting officer has some time to ensure that systems are reviewed and plans are put in place. The accounting officer's responsibilities for revenue management take effect immediately for all municipalities owing to the critical importance of this for the survival of the municipality. The accounting officer's responsibilities for monthly reporting are delayed according to capacity.

Where the provisions relate to responsibilities of other top management they take effect on 1/7/2004.

Chapter 9 – Municipal Budget and Treasury Offices

Establishment of a budget and treasury office is delayed according to municipal capacity to allow for structures to be put in place.

Competency levels are currently being developed and therefore the relevant provisions are delayed until 1/7/2006 to ensure that professional finance officials can satisfy these requirements. If the relevant officials do not meet the competency levels as at the effective date, municipalities should take steps to replace them with appropriately qualified professionals.

Chapter 10 – Municipal Entities

The majority of the provisions in this chapter will apply from 1/7/2004, with budget-related provisions applying to the 2005/06 budget. Provisions relating to competency levels will apply from 1/7/2006 in line with other provisions on competency.

Chapter 11 – Goods and Services

Stand-alone provisions will apply from 1/7/2004, including provisions relating to unsolicited bids and the preclusion of councillor representation on tender committees.

Provisions relating to the implementation of prescribed policy and procedures will be delayed according to municipal capacity. An interim framework will be released in 2004 to enable high-capacity municipalities to implement for the 2005/06 year.

Provisions relating to competency levels will apply from 1/7/2006 in line with other provisions on competency.

Chapter 12 – Financial Reporting and Auditing

Provisions relating to annual reports are delayed according to municipal capacity.

Some disclosure requirements will take effect on 1/4/2005 as the DoRA currently covers them.

Disclosures concerning councillors, directors and officials and other compulsory disclosures apply from 1/7/2004.

Auditor-General responsibilities will generally apply from 1/7/2005 for the 2004/05 financial year.

Chapter 13 – Resolution of Financial Problems

Chapter 13 takes effect on 1/7/2005 to allow for capacity to be built in the relevant departments. However, in the interim, interventions will be guided by section 139 of the Constitution of the Republic.

Chapter 14 – General Treasury Matters

This chapter generally takes effect on 1/7/2004.

Provisions relating to internal audit units will take effect from 1/7/2006 for high, 1/7/2007 for medium and 1/7/2008 for low capacity municipalities. Provisions relating to audit committees will take effect on 1/7/2006 for all municipalities, as municipalities may share audit committees.

Chapter 15 – Financial Misconduct

This chapter takes effect on 1/7/2004. However, before any party attempts to take action against any person under the provisions of this chapter, they must first consult with the National Treasury.

Chapter 16 – Miscellaneous

The chapter takes effect on 1/7/2004. The Municipal Accountants Act will be repealed as at 1/7/2005.

PART THREE

ORGANISATIONAL REFORMS

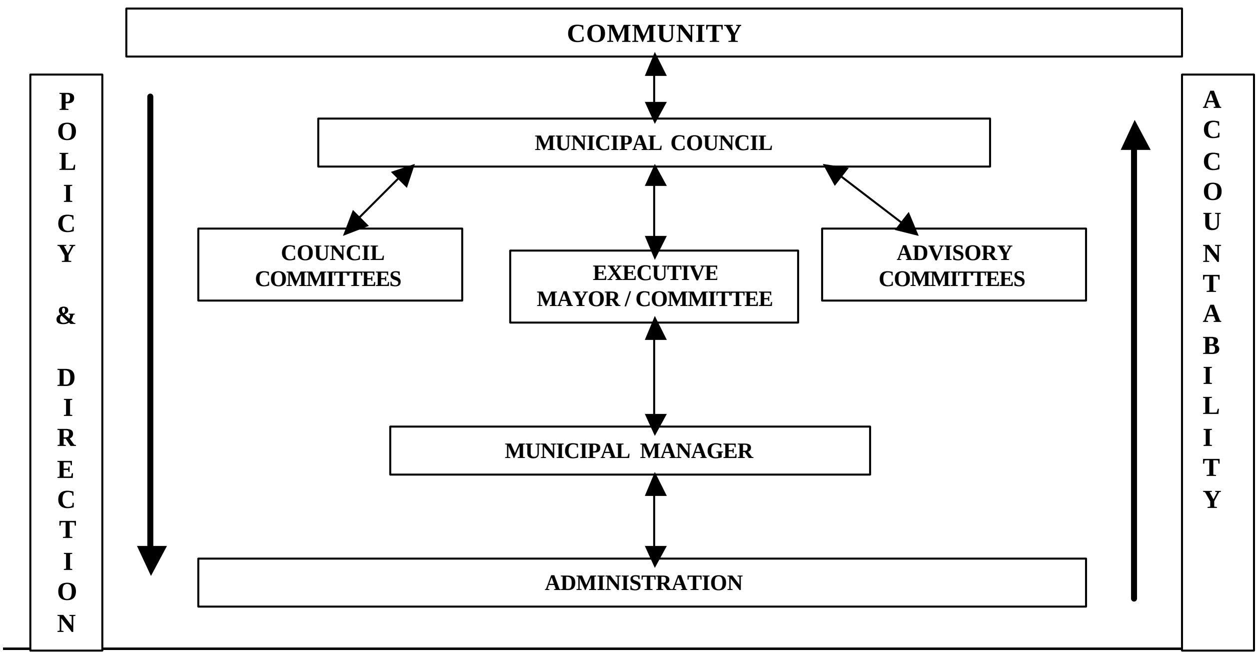
Chapter 6: Clarifying roles and responsibilities

New roles and responsibilities

The *MFMA* together with the Municipal Systems Act and the Municipal Structures Act provides clear guidance on the roles and responsibilities of councillors and officials.

The diagram below illustrates certain aspects of governance and accountability and the political and administrative structures required for accountability.

Political and Administrative Accountability



Oversight and clear lines of authority

In accordance with the financial governance principles discussed, the *MFMA* clearly establishes a **separation of roles** and responsibilities between the mayor and council and between the mayor and the municipal manager and other senior officials.

It thus creates a clearer and ***single*** **line of authority** between the council, which must approve council policy; the mayor, who must provide political leadership and manage the implementation of the policy; and the municipal manager, who is accountable to the mayor and council for implementing those policies.

Role of the council

The *MFMA* recognises the municipal council as the highest authority in the municipality and strengthens the power of the council by vesting it with significant powers of approval and oversight.

A council delegates its executive authority to the executive mayor or committee, but does not delegate its legislative powers and also retains its power to approve policy and budgets and to exercise oversight over the mayor in the implementation of policy, budgets and by-laws. As the representative body of the residents that it serves, it remains accountable to residents and to other stakeholders like businesses, customers and users of its services.

Role of the non-executive councillor

Apart from the Speaker, non-executive councillors generally function in a part-time capacity and are expected to play a political role in representing residents and other stakeholders in the municipality. Councillors provide the critical political linkage between the executive (mayor or executive committee) and the community. Councillors can therefore facilitate the consultative processes envisaged in both the *MFMA* and the Municipal Systems Act, particularly with regard to budgets, IDPs, budget-related policies, tariff-setting for services, indigency policies, long-term borrowing and c contracts.

The Municipal Systems Act and the *MFMA* also provide non-executive councillors with important recommendation and approval roles: they are expected to review, debate, modify and approve the policies recommended by the executive (mayor or committee). These include by-laws and policies on priorities that impact on council service delivery.

Both the Municipal Systems Act and the *MFMA* also expand the role of councillors to include an oversight role through council (or committee) meetings. Councillors ensure the establishment of effective operational and financial policies and procedures that will produce desired outcomes. To be effective in their role, councillors need to fully understand their oversight responsibilities. As overseers, they must refrain from involvement with the implementation of policies, procedures and directions that they have determined necessary for the community. Councillors cannot have an operational role, as this would interfere with the role of the executive (mayor or committee) and also weaken the accountability of officials to the council (since councillors cannot be both players and referee). This is in line with the role of elected representatives in Parliament and the provincial legislatures, who do not become involved in the day-to-day activities of the executive.

The oversight role of councillors may be summarised as—

- setting the direction for municipal activities;
- setting policy parameters to guide these activities;
- setting strategic objectives and priorities stating what outcomes and outputs are to be achieved;
- monitoring the implementation of policies and priorities by evaluating reports of outputs and outcomes;
- ensuring that corrective action is taken where outputs deviate from plans; and
- accounting back to the community for performance in terms of objectives.

Given the importance of this oversight role, both the Municipal Systems Act and the *MFMA* protect the councillors' policy-making role by separating it from the implementation role played by officials. Councillors are therefore not allowed to be members of either the boards of entities (section 93F of the Municipal Systems Act), audit committees (section 166(5) of the MFMA, or a tender or bid committee (section 117 of the *MFMA*). Previous legislation was inconsistent in this regard, and it is expected that where such legislation and regulations are out of line with the approach of the MSA and the *MFMA* they will be amended over the next two years. Government will also amend other planning legislation to the extent necessary to ensure that councillors do not serve on planning tribunals and other approval forums either, as participation in such forums falls within the implementation responsibilities.

The *MFMA* also anticipates that each municipal council will strengthen its oversight role by forming portfolio committees within the council to facilitate the oversight role councillors can play through such committees. The Municipal Structures Act can be utilised in this respect, through sections 79 and 80, which allows a council to form a budget and finance committee, a public accounts committee, a municipal services committee (to cover water, electricity, refuse removal), etc.

Under the *MFMA*, the council is expected to undertake a number of financial management tasks to fulfil its oversight function. These include the following:

- Considering and approving the annual budget and ensuring the budget and IDP are aligned
- Approving budget-related policies on appropriate taxes, user charges, indigency policies, credit control and supply chain management
- Considering the views of the community and government regarding the budget and in establishing a municipal entity
- Reviewing the budget and performance of entities under council control
- Dealing with audit and annual reports, and adopting an oversight report once the report is received
- Considering capital projects and contracts with financial implications of more than three budget years
- Taking responsibility for incurring debt and determining security over debt (although some aspects of this may be delegated for short-term debt, subject to certain conditions)
- Considering the sale, disposal or transfer of all capital assets (although this may be delegated to the municipal manager to a value determined by the council)
- Reviewing unauthorised and unforeseen expenditure and reporting on unauthorised, irregular and fruitless and wasteful expenditure
- Investigating allegations of financial misconduct and taking appropriate action where necessary

The council is primarily responsible for avoiding, identifying and resolving its own financial problems as they arise.

Role of the executive mayor or committee

As the executive authority of the council, the executive mayor or committee must provide political guidance over the policy, budget and financial affairs of the municipality and must ensure that the municipality complies with its obligations under the legislation. Without interfering in the day-to-day administration of the municipality, the mayor should monitor and oversee the municipal manager and senior managers to ensure that they are carrying out their duties in an appropriate manner. The key tools for doing so are the annual service delivery and budget implementation plan (SDBIP) and the performance agreement with its clear measurable outputs.

The mayor remains accountable to council for proposing and implementing policy and overseeing the implementation of this policy by the administration. The following are some of his or her specific responsibilities:

- Providing political guidance on the budget process
- Co-ordinating the budget process with the municipal manager

- Reviewing IDP and budget-related policies and ensuring consistency with the budget
- Ensuring that the municipality complies with the legislative deadlines for the tabling and approval of the budget
- Approving the service delivery and budget implementation plan within 28 days after the approval of the budget, and approving the performance agreements of the municipal manager and senior management
- Monitoring the financial performance of the municipality through monthly financial reports submitted by the municipal manager
- Providing council with quarterly budget reports and taking action where necessary
- Reporting instances of potential or real non-compliance with the budget chapter of the *MFMA* or in relation to issues that may necessitate provincial intervention
- Tabling an adjustments budget
- Reporting instances of unforeseeable or unavoidable expenditure
- Guiding the municipality in its dealings with its municipal entities
- Tabling the annual report to council each year

The approach of the *MFMA* is also consistent with the Code of Conduct set out in Schedule 1 of the *Municipal Systems Act*, which clearly requires councillor disclosure of conflicts of interest and prohibits councillor involvement in tender boards or the boards of municipal entities.

Role of the municipal manager (the accounting officer)

The municipal manager is the accounting officer and the administrative authority for the municipality and is responsible for the implementation of approved council policy and the achievement of the objectives set out by the mayor. In the first instance the municipal manager is accountable to the mayor for the implementation of specific agreed outputs. In the second instance the municipal manager is accountable to the council for the overall administration of the municipality.

The municipal manager is therefore the key officer responsible to the mayor and council for the successful implementation of the legislation. In this capacity, the municipal manager must be fully aware of the reforms required in order to provide the mayor, councillors, senior officials and municipal entities with the appropriate guidance and advice on financial and budget issues. Whilst the municipal manager may delegate many tasks to the chief financial officer or to other senior officials, this must be done carefully to ensure that all tasks are completed appropriately.

The municipal manager must project manage at the highest level the change management process, establishing appropriate objectives for senior staff, project milestones, timeframes and responsibilities whilst managing those outputs effectively and regularly reporting back to the mayor and council on progress. A skilled and well-rounded senior management complemented with some financial management background and knowledge is desirable, since their roles and responsibilities, depending on the extent of delegations by the municipal manager, will greatly support the expeditious implementation of good financial management and governance. It is also appropriate to have the chief financial officer regularly update senior management on finance-related policies and areas of relevance. The delegation of financial management tasks to junior officials should be avoided.

The municipal manager is now required to take on a number of specific responsibilities, including certifying the correctness of the reports, under the *MFMA*, which include, but are not limited to, the following:

- Budget preparation role
    - Assisting the mayor in preparing the budget
    - Assisting in conducting community participation meetings
    - Making public the draft budget

- Assisting the mayor in preparing the adjustment budget
- Assisting in the preparation of budget-related policies

- Budget Implementation and other administrative roles
  - Making public the approved budget
  - Implementing the approved budget
  - Developing and submitting the service delivery and budget implementation plan
  - Ensuring revenue collection and expenditure is in line with the budget
  - Certifies where necessary to shift funds across budget years
  - Administering all municipal bank accounts
  - Submitting annual performance agreements for all senior managers
  - Developing and implementing a supply chain management policy
  - Providing an assessment of municipal performance for inclusion in the annual report

- Reporting and publishing role
  - Reporting unauthorised, irregular or fruitless and wasteful expenditure
  - Reporting impending shortfalls or overspending, and any overdraft position
  - Reporting on monthly and mid-year budget progress
  - Reporting other matters as prescribed, including staff expenditure
  - Making public and inviting comment on draft contracts with a term greater than three years
  - Ensuring information is supplied to council and the public on debt proposals
  - Making public any proposal to establish or participate in a municipal entity
  - Preparing the annual financial statements for audit, verifying salaries and benefits paid
  - Making public the annual report and the council's oversight report
  - Monitoring entities to ensure that their reporting obligations are met

The municipal manager is responsible for the financial management of the municipality, ultimately ensuring that all financial systems are in place and are properly maintained.

Misconduct

Municipalities are requested to operate in an accountable and transparent manner. Good governance requires that any municipal council or manager instituting disciplinary action should follow the legal prescripts in spirit and to the letter. Hence, in order to ensure appropriate applicability of the relevant misconduct sections in the *MFMA* it is recommended that actions undertaken should be clearly within the bounds of "grossly negligent or wilful transgressions" and the National Treasury should be consulted on with respect to any action in this regard.

Summary

This chapter attempts to set out and delineate the role and responsibility of councillors and officials in the financial management of a municipality. In so doing, it highlights the policy-making and oversight role that councillors play on the one hand and the administrative and implementation role that the officials in a municipality are employed to play on the other.

Chapter 7: Top management and delegation of accounting officer responsibilities

Background

The *MFMA* establishes a major role for the municipal manager, who is the accounting officer of the municipality. Chapter 8 of the Act spells out the accounting officer's fiduciary and other responsibilities. These responsibilities are additional to all the other management responsibilities expected of the municipal manager as head of the administration, including the responsibilities outlined in the Municipal Systems Act.

Sharing of responsibilities

The *MFMA* expects the municipal manager to share these responsib ilities with other senior managers and anticipates a senior management structure in section 77 of the Act. The top management team under the municipal manager comprises the chief financial officer and all the senior managers who head various functions or departments and are responsible for the budget of that function or department (e.g. water and sanitation, electricity, roads and transport, housing, etc.).

Delegations and accountability

Where an accounting officer delegates any of the accounting officer responsibilities to such senior managers, and where they are properly qualified AND have the necessary experience to play this role, senior managers will be held primarily accountable for any transgressions in exercising these accounting officer responsibilities. The liability of the accounting officer will be limited provided that the delegation is reasonable and appropriate, on condition that the accounting officer actively monitors the performance of the senior managers, including acting in terms of the monthly budget monitoring system based on section 71 of the Act, as the accounting officer is not divested of the responsibility for the exercise of a delegated power.

The municipal manager may delegate tasks allocated to him or her under the *MFMA* to the chief financial officer, except those of maintaining municipal bank accounts and developing the municipal budget. The chief financial officer may in turn delegate certain tasks to other senior officials.

Delegations to be in writing

In all instances, dele gations must be in writing and may be subject to change or amendment. The official delegating the task should always ensure that appropriate systems are in place to guarantee that proper control and accountability remain with him or herself. Delegations should be limited and any delegation to junior officials should be avoided.

The supporting annexure provides a detailed schedule of the responsibilities that may be delegated by the municipal manager to other senior officials in the municipality.

Performance agreements

The Service Delivery and Budget Implementation Plan (SDBIP) is to be drafted and adopted with the multi-year budget and made public by the mayor no later than 14 days after its approval. This will be one of the tools to measure the performance of senior managers. The performance agreement between the mayor and the municipal manager will contain key strategic and delivery outcomes translated into clear outputs. These will also cascade into the performance agreements of the top management team in the first instance and flow into the operational plans and agreements of other managers and staff. It is expected that the SDBIP will contain details on the execution of the budget, and include information on programmes and projects broken down by ward. It will provide commencement, phases and completion dates, revenue and expenditure, quarterly service delivery targets and performance indicators. Moreover, there should be regular reporting on progress on the programme or projects, which will assist in facilitating better non-financial and financial reporting. The intention of the SDBIP is also to empower councillors to perform their oversight responsibilities better.

A guide will be issued containing more information on the contents of a SDBIP.

Monitoring, reporting and staff performance agreements

The primary oversight mechanism for a mayor to ensure that the council's requirements are being met by the municipal manager is the municipal manager's annual performance agreement, detailed in section 57 of the Municipal Systems Act and referred to in sections 53 and 69 of the *MFMA*.

It is important that councils recognise the importance of the performance-based management process in managing their affairs. Individual employee performance contracts should be based on measurable outputs and relate to the achieving certain objectives and outcomes set by the Council.

The success or otherwise of the municipality meeting these objectives should bear a direct relation to an employee's success or otherwise.

This should inform council decisions relating to the payment of employment bonuses and other contract conditions.

Chapter 8: Budget and treasury office

One of the key institutional and organisational reforms required by the *MFMA* is the establishment of a budget and treasury office (BTO) and the appointment of a chief financial officer (CFO) to head the BTO. This organisational reform must be seen as part of the creation of a top management team in terms of section 77 of the Act. This chapter provides municipalities with some guidance on how to go about setting up the BTO and appointing an appropriately qualified CFO and their link to the senior management team.

The chief financial officer

The chief financial officer is the administrative head of the budget and treasury office. The CFO has an essential function in assisting the municipal manager to carry out his or her financial management responsibilities, in areas ranging from budget preparation to financial reporting and the development and maintenance of internal control procedures.

The CFO plays a central role in implementing the financial reforms at the direction of the municipal manager with the assistance of appropriately skilled finance staff.

Establishing a BTO

Municipalities should NOT see the establishment of a budget and treasury office (BTO) merely as a cosmetic change and simply rename their current treasury department as a BTO. Similarly, it would be wrong to assume that the current head of the treasury will be the new CFO heading the BTO. For this reason, the establishment of the BTO in terms of section 80 has been delayed until 30 June 2005 or 2006 according to capacity.

The BTO has many more powers than current municipal treasury departments, as its responsibilities go beyond traditional accounting or treasury functions like operating bank accounts, cash management, collecting revenue or overseeing revenue collection, authorising or making payments and preparing financial statements. In addition, the role involves playing a more strategic advisory role to the accounting officer and other senior officials, one that is forward-looking and takes the lead in the budgeting and planning processes. It is also expected to take on both a management (rather than administrative) role and an oversight role. The BTO will have a critical function in producing monthly management information for the municipal manager and mayor.

Similarly, the CFO is expected to be part of the top management team under the municipal manager, together with all the other senior managers who are heads of department (and responsible for key budget programmes or votes like water and electricity), in terms of section 71 of the Act. Although Chapter 7 of the Act vests responsibilities in the municipal manager as the accounting officer, the Act anticipates that such responsibilities will be shared with the top management team. The CFO therefore has to be a professional with strong management and leadership skills. Providing leadership for the budget and planning process does not necessarily require accounting skills. Hence not all officials in the BTO will have financial skills and, conversely, not all financial staff will be in the BTO – in many large municipalities, most major departments (e.g. water and sanitation) will need to have financial officials in those departments, outside the BTO.

For this reason, section 83 of the Act requires the CFO to undergo training and to meet minimum standards of qualification and experience. The National Treasury is assisting in preparing courses that all CFOs will be required to attend (and pass). CFOs failing to pass these courses may not be eligible for appointment. Though the courses will be made compulsory for CFOs only from 1 July 2006, it is strongly recommended that all municipalities make the passing of these courses a condition of employment. The courses will have to be taken annually, with all CFOs required to accumulate a minimum number of points each year. This should be enforced as part of employment contracts and form part of performance agreements.

Note that appropriate courses are being designed and will also be compulsory for all other officials in finance and supply chain activities, and similarly for all non-financial senior managers.

A further important objective is to facilitate and promote the mobility of finance officials between all three spheres of government. The underlying approach of both the *MFMA* and the PFMA (Public Finance Management Act) is similar, and it is hoped that finance or treasury officials will generally have the expertise to implement both pieces of legislation. The Minister of Finance has called on finance officials from both spheres to break from the current traditions and form one professional body that includes finance officials from all three spheres of government.

The Minister of Finance mentioned in a speech delivered to SALGA in November 2002 that –

"*… the creation of an association of budget and finance professionals is needed to facilitate mobility of such professionals between the three spheres of government. I have made calls on the leadership of the two main professional bodies representing public finance professionals in SA, the Institute of Municipal Finance Officers (IMFO – local government) and the Institute for Public Finance and Auditing (IPFA – provincial and national government), to form a single association. I want to volunteer the National Treasury to assist in this process. Such a single body must reflect the transformation sweeping our country. It must lead the fight to create a new type of professional, ready to implement the spirit of the MFMA and reform agenda. Such a body must champion better management in the public sector. It must strive to be more representative of our society. I would like to see more opportunities offered to new entrants in the finance arena, and better schooled and trained staff that can help find solutions to the challenges facing local government.*"

Summary

The chapter highlights the importance of a well-structured organisation with appropriately skilled personnel, including the head of the BTO. It also points out the weaknesses and raises the need for ongoing skills development. The National Treasury will play a facilitation and guiding role by issuing supporting material in this regard.

PART 4

KEY BUDGET AND REPORTING REFORMS

Chapter 9: Three-year budgeting and planning

The budget preparation process

The mayor must lead the budget preparation process through a co-ordinated cycle of events that commences at least ten months prior to the start of each financial year.

Overview

A central element of the reforms is a change to the way that municipalities prepare their budgets.

The *MFMA* requires a council to adopt three-year capital and operating budgets that take into account, and are linked to, the municipality's current and future development priorities (as contained in the IDP) and other finance-related policies (such as those relating to free basic service provision).

These budgets must clearly set out revenue by source and expenditure by vote over three years and must be accompanied by performance objectives for revenue and expenditure, a cash flow statement and particulars on borrowing, investments, municipal entities and service delivery agreements, grant allocations and details of employment costs.

The budget may be funded only from reasonable estimates of revenue and cash-backed surplus funds from the previous year and borrowings (the latter for capital items only).

Budget preparation timetable

The first step in the budget preparation process is to develop a timetable of all key deadlines relating to the budget and to review the municipality's IDP and budget-related policies.

The budget preparation timetable should be prepared by senior management and tabled by the mayor for council adoption by 31 August (ten months before the commencement of the next budget year).

Budget preparation and review of IDP and policy

The mayor must co-ordinate the budget preparation process and the review of council's IDP and budget-related policy, with the assistance of the municipal manager.

The mayor must ensure that the IDP review forms an integral part of the budget process and that any changes to strategic priorities as contained in the IDP document have realistic projections of revenue and expenditure. In developing the budget, the management must take into account national and provincial budgets, the national fiscal and macro-economic policy and other relevant agreements or Acts of Parliament. The mayor must consult with the relevant district council and all other local municipalities in that district as well as the relevant provincial treasury and the National Treasury when preparing the budget, and must provide the National Treasury and other government departments with certain information on request.

This process of development should ideally occur between August and November, so that draft consolidated three-year budget proposals, IDP amendments and policies can be made available during December and January. This allows time during January, February and March for preliminary consultation and discussion on the draft budget.

Tabling of the draft budget

The initial draft budget must be tabled by the mayor before council for review by 30 March.

Publication of the draft budget

Once tabled at council, the municipal manager must make public the appropriate budget documentation and submit it to both the National Treasury and the relevant provincial treasury and any other government departments as required. At this time, the local community must be invited to submit representations on what is contained in the budget.

Opportunity to comment on draft budget

When the draft budget is tabled, council must consider the views of the local community, the National Treasury and the relevant provincial treasury and other municipalities and government departments that may have made submissions on the budget.

Opportunity for revisions to draft budget

After considering all views and submissions, council must provide an opportunity for the mayor to respond to the submissions received and if necessary to revise the budget and table amendments for council's consideration.

Following the tabling of the draft budget at the end of March, the months of April and May should be used to accommodate public and government comment and to make any revisions that may be necessary. This may take the form of public hearings, council debates, formal or informal delegations to the National Treasury, provincial treasury and other municipalities, or any other consultative forums designed to address stakeholder priorities.

Adoption of the annual budget

The council must then consider the approval of the budget by 1 June and must formally adopt the budget by 30 June. This provides a 30-day window for council to revise the budget several times before its final approval.

If a council fails to approve its budget at its first meeting, it *must* reconsider it, or an amended draft, again within seven days and it must continue to do so until it is finally approved – *before* 1 July.

Once approved, the municipal manager must place the budget on the municipality's website within five days.

Budgets of municipal entities

The board of directors of a municipal entity must submit a proposed budget to the municipality by 31 January, or earlier if agreed. The municipality must consider the budget and return any recommendations to the board of directors, who may submit a revised budget not later than the middle of March.

Entity budgets to be considered with municipal budgets
The revised budget must then be tabled by the mayor at the same time as the municipal budget is tabled. The board of directors must approve the budget by 1 June, and it must then be made public. The board of directors may revise the budget with the approval of the mayor.

Budget implementation

Implementation management – the service delivery and budget implementation plan
The municipal manager must within fourteen days of the approval of the annual budget (by 14 July at the latest) submit to the mayor for approval a draft service delivery and budget implementation plan and draft annual performance agreements for all pertinent senior staff.

A service delivery and budget implementation plan is a detailed plan for implementing the delivery of municipal services contemplated in the annual budget and should indicate monthly revenue and expenditure projections and quarterly service delivery targets and performance indicators.

The mayor must approve the draft service delivery and budget implementation plan within 28 days of the approval of the annual budget (by 28 July at the latest).

This plan must then be monitored by the mayor and reported on to council on a regular basis.

Managing the implementation process
The municipal manager is responsible for implementation of the budget and must take steps to ensure that all spending is in accordance with the budget and that revenue and expenditure are properly monitored.

Variation from budget estimates
Generally, councils may incur expenditure only if it is in terms of the budget, within the limits of the amounts appropriated against each budget vote – and in the case of capital expenditure, only if council has approved the project.

Expenditure incurred outside of these parameters may be considered to be unauthorised or, in some cases, irregular or fruitless and wasteful. Unauthorised expenditure must be reported and may result in criminal proceedings.

Revision of budget estimates – the adjustments budget
It may be necessary on occasion for a council to consider a revision of its original budget, owing to material and significant changes in revenue collections, expenditure patterns, or forecasts thereof for the remainder of the financial year.

In such cases a municipality may adopt an adjustments budget, prepared by the municipal manager and submitted to the mayor for consideration and tabling at council for adoption.

The adjustments budget must contain certain prescribed information, it may not result in further increases in taxes and tariffs and it must contain appropriate justifications and supporting material when approved by council.

The supporting annexure contains a summary of the budget and financial management cycle.

Summary

This chapter serves to highlight the importance of the budget process, the use of the budget in implementing services, and the need to have credible and balanced budgets with regular monitoring of performance against budget.

It should be noted that the National Treasury will be conducting workshops and publishing a comprehensive guide on budgeting later this year.

Chapter 10: In-year reporting

Financial reporting

The system of reporting developed in the *MFMA* will assist in making available improved and regular internal and external information and will commence on 1 July 2004. Managers, as part of implementing policy, should use this opportunity to provide regular and relevant information in order to analyse performance and address shortcomings and improve internal controls and service delivery. Recommendations and explanations should assist the mayor and councillors to play their oversight roles, to monitor implementation of the budget and to make informed policy decisions.

The monthly, quarterly, semi-annual and annual reports will often come with a lag, for example the first-quarter reports must be available by the 30th day of the month after the end of the first quarter. These reports should be made public after debate in council. At this meeting the in-year performance must be monitored and corrective action taken. It is important to note that the six-month report together with the audit and oversight reports of the previous year will be presented to council by 25 January, allowing for the mayor to recommend and council to consider adjustments to the budget.

Financial transparency and ongoing performance

In order to achieve an effective oversight mechanism and the appropriate fiscal discipline and managerial accountability, financial management systems must provide sufficient **transparency** to accurately measure the **ongoing performance** of the municipality.

The Act facilitates this by requiring the municipality to develop measurable performance objectives for revenue and expenditure, taking into account the IDP, and to report against these measures in the mid-year and annual reports.

Monitoring progress and financial reporting

Managerial oversight of performance should operate in the first instance within the municipality itself. With this in mind, the Act has stipulated that certain **reporting mechanisms** must be established within a municipality to monitor the financial position of the municipality and review **ongoing progress** toward performance objectives.

In addition to this, and mindful of the role of national and provincial government, the Act requires the municipality to report on certain issues that identify problems as they arise, in order to ensure that, where required, prompt remedial action is taken by the province or National Treasury.

Non-financial reporting:

Practitioners should note that in order to communicate performance effectively, reports must contain both financial and non-financial information. Non-financial information, such as subjective narratives on service delivery backlogs, the number of electricity and water connections and explanations of council policy on indigents and free basic services, will supplement financial data and key performance measures.

In-year reporting

Monthly budget statements

By the 10th working day of each month, the municipal manager must submit a report on budget progress to the mayor and the relevant provincial treasury. On receiving the report, the mayor must take the appropriate steps to identify and resolve any financial problems that may be evident. In this regard the Division of Revenue Act (DoRA) applies for the 2004/05 financial year.

Quarterly budget statements

By the 30th day following the last month of each quarter, the mayor must submit a report on budget implementation and the municipality's financial position to council. Once adopted, the municipal manager must place the report on the municipality's website within five days.

Mid-year budget and performance assessment

By 25 January each year (and in addition to the monthly budget report), the municipal manager must submit a mid-year budget report and performance assessment (based on the council's service delivery and budget implementation plan) to the mayor, the National Treasury and relevant provincial treasury. This report may be used to inform the mayor of any need to consider an adjustments budget and should be used to inform the budget process for the following year.

General in-year reporting obligations

The municipal manager must advise the National Treasury, the relevant provincial treasury and the Auditor-General about all bank accounts as they are opened and must report to council, the provincial treasury and the Auditor-General the details of certain prescribed withdrawals each quarter. The municipal manager must also report on any unauthorised, irregular or fruitless and wasteful expenditure as it occurs and on any impending budget shortfalls or overspending. Details of expenditure on staff benefits must be reported to council regularly. The mayor must also report to the MEC for local government any issue that necessitates provincial intervention as it arises. The chief executive officer of a municipal entity must provide the municipal manager of the parent municipality with regular reports on finance and performance.

Chapter 11: Annual reports

Annual reports

Preparation of the annual report and annual financial statements

Every municipality and municipal entity must prepare an annual report each year to provide a record of the activities and performance of the municipality over the year and to promote accountability to the community for its decisions.

This requires the collection of information about the nature and extent of services provided, with references to key performance targets and actual performance data, explanations of variations and a narrative of policy and strategy.

The annual report must include audited financial statements that disclose a range of information to adequately reflect the financial position of the municipality at year-end.

Such disclosures must include information on allocations received and made, particulars of employment costs of councillors and officials, details of bank accounts, investments and contingent liabilities, particulars of non-compliance with the Act and details of any material losses from unauthorised expenditure.

Annual Reports for 2002/03 and 2003/04

The National Treasury, after consulting with other departments, issued a circular in 2003 to advise and guide municipalities in the preparation of their annual reports. The circular contains information on best practice approaches and assists with formats and contents covering aspects such as the mayor's inputs, overview, background on services provided, human resources and other organisational management, audited statements and related aspects, functional service delivery reporting and disclosure of demographic and other related information.

The 2004 Division of Revenue Act highlights further reporting and disclosure required in municipal and transferring departments' annual reports, including information on receipts and spending, their utilisation to achieve the purpose and outputs attained, whether any funds were withheld and the reasons for this. This relates to all intergovernmental transfers, conditional and unconditional grants.

The 2004/05 annual report should be prepared in terms of the *MFMA* as elaborated below. It is expected that continuous improvements to the quality and content of financial and non-financial information disclosed in annual reports will empower the community to measure the performance of a municipality in its financial management and service delivery.

Submission and tabling of the annual report and annual financial statements

Annual reports must be tabled in council by 31 January. The chief executive officer of a municipal entity must provide the parent municipality with the entity's annual report at least one month earlier.

Annual financial statements must be submitted to the Auditor-General by 31 August, or by 30 September in the case of those municipalities with a municipal entity. In the latter instance, the municipal entity must provide the parent municipality with statements by 31 August.

The Auditor-General must return a report to the municipal manager or chief executive officer within three months of receiving the statements for audit, i.e. by 30 November or 31 December as the case may be.

Oversight reports

Although there is no reason not to prepare and present an oversight report for the current financial year, this requirement will take effect only for the 2004/05 budget, financial statements and audits.

The council must consider the annual report within two months of it being tabled, by 31 March at the latest. The council must then adopt an oversight report containing its comments on the annual report, whether it approves, rejects or wishes it to be referred back for further revision. A public accounts type of committee should be established to deal with annual reports.

Meetings to discuss the annual report

A council meeting open to the public must be convened to discuss the annual report, at which the council addresses issues raised. The provincial MEC for local government must assess the statements to ensure that the council has addressed the appropriate issues and responded accordingly. Any omissions by the municipality must then be reported to the provincial legislature for further action.

The municipal manager must attend meetings and make the oversight report and minutes of the meeting available to the Auditor-General and the national and provincial government.

The schedule of reporting cycles will be available on the Treasury website shortly.

Chapter 12: Supply chain management and PPPs

Supply Chain Management

The Public Finance Management Act, Act 1 of 1999 (as amended by Act 29 of 1999), as well as the *MFMA* compel accounting officers to accept full responsibility and accountability for all expenditure incurred.

Government commenced with public sector procurement reform in 1995 and several interim and other measures were introduced as part of the reform process. This included the interim ten-point plan and the enactment of the Preferential Procurement Policy Framework Act, Act 5 of 2000, to give effect to section 217(c) of the Constitution. The National Treasury, in consultation with local and international experts and representatives of various provincial and national departments, assessed the now outdated procurement and provisioning systems that are being or were utilised by the various organs of state. To align our systems with international best practices, the concept of supply chain management (SCM) was developed and is currently being introduced in national and provincial government and public entities.

SCM is an integral part of financial management and can be described as a systematic approach that ensures that goods and services are delivered to the right place, in the right quantity, with the right quality, at the right cost and at the right time. SCM commences with demand management when, at the strategic planning phase to determine the functions and goals of the entity, the goods and services are identified, budgeted for and programmed. This includes a detailed analysis of the goods and services required, following the best-cost approach to obtain the goods and services. Following on from demand management is acquisitioning management, at which stage a strategy is determined on how to approach the market, preparation of detail descriptions and specifications of what will be acquired, bids are evaluated and recommendations are made. Logistics and disposal management forms the later parts of this integrated system. Supply chain performance captures various issues that should be monitored and evaluated on a continuous basis, such as achievement of goals, compliance with norms and standards, cost-efficiency of the process, etc.

Cabinet approved a Policy Strategy to Guide Uniformity in Procurement Reform Processes in Government. A Framework for Supply Chain Management was promulgated in terms of section 76(4)(c) of the PFMA. Four practice notes were issued in terms of this framework with the aim of ensuring uniformity. A Supply Chain Management Guide for Accounting Officers/ Authorities was also issued to assist with the implementation of this new concept.

The Municipal Finance Management Act (*MFMA*) requires the introduction of supply chain management in every municipality. The express provisions on supply chain management relate to the implementation of policies within the prescribed framework that must be fair, equitable, transparent, competitive and cost-effective. The framework covers a range of matters from tender procedures and quotations to auctions and other types of competitive bidding processes. It also deals with screening processes and compulsory disclosure of conflict of interest and bars councillors from serving on tender or bidding processes.

The Act is clear on measures for combating fraud, corruption, favouritism and unfair and irregular practices and seeks to promote the ethical behaviour of officials and other role-players involved in supply chain management. In keeping with the financial governance concepts previously discussed, councillors cannot oversee the supply chain management policy and be involved in its implementation. Therefore, councillors may neither be a member of a tender committee, nor in any way take part in the tender process. Tender committees are appointed by and are responsible to the accounting officer. It is expected that tender committees will be formed from among senior officials of the municipality. The municipal manager through the tender committee will administer the supply chain management policy adopted by council.

The section on supply chain management should not be read in isolation of other sections such as section 33, which deals with long-term contracts, section 113 on unsolicited bids and related sections dealing with interference by any person in the supply chain management processes. Of particular importance to officials involved in supply chain management is the competency testing that will be introduced over the medium term.

A phased approach will be followed, commencing during the latter half of this year. However, section 117 barring councillors from serving on tender committees and section 118 dealing with interference of the supply chain management policy will apply as at 1 July 2004. Implementation will be undertaken through a consultation process with selected municipalities. This implies that certain sections will be phased in over the next year or two. It is recognised that an interim framework to guide municipalities during this phase will be required and the Treasury plans to issue this framework later this year.

The policy document, framework, practice notes and guide, that relate to national and provincial government, are available for perusal on the Treasury website. Municipalities were invited to comment on these documents to ensure that specific circumstances unique to municipalities were accommodated.

Public Private Partnerships

The PPP legislative processing and policy development is similar to that expressed in the supply chain management development. Given their history, municipalities face enormous challenges in the delivery of public services and infrastructure. Although government has implemented a range of infrastructure delivery programmes that have significantly increased access to services, large backlogs remain. Addressing backlogs in essential public services while maintaining fiscal prudence requires greater efficiency in the delivery of public services. This enhances the scope for increasing access to services and for providing higher quality services. Correctly structured public private partnerships (PPPs) are a useful service delivery option from both an operational and a strategic perspective.

Operationally, the benefits of PPPs include efficiency gains, output focus, economies generated from integrating the design, building, financing and operation of assets, innovative use of assets, managerial expertise and better project identification. These benefits can result in some combination of better and/or more services for the same price, and savings, which can be used for other services or for more investment elsewhere. Strategically, partnership contracts enhance accountability by clarifying responsibilities and focusing on the key deliverables of a service.

Public-private partnerships are an integral component of government's overall strategy for the provision of public services and public infrastructure across all sectors. This does not imply that public-private partnerships are the preferred option for improving the efficiency of service delivery, but rather that they enjoy equal status among a range of possible service delivery options available at all spheres of government.

Municipal Services and Private Public Partnerships

The legislative framework as amended in the Municipal Systems Act and the provisions of the *MFMA* that deal with PPPs (section 120) should be read together to formulate a coherent understanding of this alternative service delivery mechanism. The *MFMA* prescribes that PPPs must provide value for money, present an appropriate allocation of risks between the contracting parties and be affordable in terms of current and projected budget provisions. It requires a regulatory framework to be developed and prescribed by the National Treasury. It also requires municipalities to conduct feasibility studies before concluding PPPs and states that the National Treasury may assist in carrying out and assessing these studies. Finally, the accounting officer in each municipality must formally solicit the views and recommendations of the National Treasury, along with other relevant departments, once the feasibility study has been completed. To assist municipalities in meeting these requirements, the National Treasury will present a package of integrated reforms to strengthen the enabling environment in support of municipal PPPs.

These will entail prescribing a clear policy framework to ensure that PPPs are a coherent option for municipalities. International and recent South African experience has shown that the private sector option needs to be supported by sound regulatory practices. The lack of effective regulatory mechanisms creates the potential for municipalities to engage in PPPs that are not affordable. A framework is needed to balance priorities between sectors and to maintain prudent control over government's financial commitments.

Municipalities will need to enhance their capacity to use PPPs in a sound and effective manner. Ensuring effective service delivery through PPP arrangements typically requires additional functional capacity in financial, technical and managerial areas that are not normally associated with the operations of a municipality. Moreover, while it could be argued that government officials have developed skills as contract managers for simpler forms of PPP arrangements, such as service and basic management contracts, this does not apply to more complex PPP contracts. The requisite skills for long-duration contracts that entail significant risks are still in relatively short supply in the government sector and will have to be developed over time. A balanced approach is therefore required both to build the required capacity and to reduce the demand on capacity by adopting, for example, measures that reduce the complexity of PPP arrangements.

The first set of regulations in terms of the PFMA was gazetted in May 2000. Experience gained since then has led to refinements in the regulatory regime. The latest revision was gazetted in January 2004 and clarified a number of definitions and procedures. These regulations apply to national and provincial departments and public entities. They provide for a three-tier approval process that assesses project affordability, value for money and risk profile. A copy of the regulation is available on the Treasury website. Municipal managers and councillors are urged to peruse these regulations to assist in gaining a broader understanding of the subject.

Current sets of guidelines include topics such as project finance, recruiting transaction advisors, how to conduct feasibility studies, how to draft request for proposal documents, unsolicited bids, departmental budgeting and tender procedures. Based on experience and feedback, the guidelines will be revised and expanded. New guidelines are being developed to cover PPP law in South Africa, PPP inception, project development facility, PPP procurement, black economic empowerment in PPP, PPP contract management, PPP close-out report and case studies, Auditor-General's requirement in PPPs and Accountant-General's requirements in PPPs. Many of the principles of these documents will be equally applicable to municipal PPP projects, to varying degrees. A working group that includes municipal managers will be set up to comment on the draft documents.

Black Economic Empowerment (BEE)

PPPs lend themselves very well to genuine BEE. They are long-term projects, typically involving at least three critical empowerment areas: equity participation in projects over a significant period, the use of SMMEs in construction and operational activities and meaningful transfer of financial and technical skills. Each PPP has the advantage of sustained government expenditure over the life of the project, meaning that through stringent financial penalty systems the government can enforce contractual BEE provisions. Similarly, incentives for exceeding empowerment objectives can be put in place through a variety of financial and contractual mechanisms. The PPP Unit has released a draft Code of Good Practice for BEE in PPPs.

Municipalities are invited to comment on these documents, which are obtainable on the Treasury website. Feedback should be directed to mfma@treasury.gov.za

Chapter 13: Development of unit standards and training

Background

A project is underway to design and develop a qualification to give effect to professional standards focusing on municipal financial management and more general financial management.

Development of unit standards

The National Treasury in consultation with key stakeholders such as LGWSETA, SALGA and DPLG, among others, is close to finalising unit standards that will result in a Level 6 qualification for registration with the South African Qualifications Authority (SAQA) and use by approved training programmes for senior municipal officials so that they can provide strategic leadership and management in transforming the local government sphere. In the short to medium term, the qualification will complement the various support mechanisms utilised by the National Treasury to implement the financial management reforms. In the long term, the qualification will assist municipalities to build their capacity – in terms of the right quantity and quality of competencies – necessary to ensure the sustainability of these reforms as well as to give effect to the provisions of the *MFMA*.

Standards to support training

The qualification will serve as a basis for the competency testing of CFOs in the medium term. Its structure will support the development of the skills that are required. Unless senior municipal officials have the relevant knowledge in financial management, economics and accounting, the appropriate skills to apply that knowledge and the right attitude towards change, the outcomes that government is seeking to achieve through the reforms and the *MFMA* will be unattainable.

Capacity-building

With respect to capacity building in the local government sphere, the qualification will help give effect to government's Framework for Municipal Capacity-Building by informing those programmes or projects that strengthen the administrative, financial, institutional, human, infrastructure and community capacities of a municipality. As indicated in that framework, budget and financial management skills, strategic management and planning skills as well as technical service delivery skills are all key to municipal capacity-building. The first two of these broad areas of competence thus constitute the nucleus of the Level 6 municipal financial management qualification currently being finalised for submission to SAQA.

Type of qualification

The Level 6 municipal financial management qualification will not address the technical aspects of financial management and accounting. It is expected that these will be catered for in the Level 5 public sector financial management qualification currently being developed elsewhere.

Instead, this qualification seeks to teach general and financial management-related competencies that are of a strategic nature within the local government sphere.

Target group of qualification

The municipal financial management qualification is targeted at both senior financial and senior non-financial managers in the local government sphere. This target group includes municipal managers, chief financial officers, entity managers and strategic managers.

Entry requirements

It is envisaged that the candidates for this Level 6 municipal financial management qualification will be in possession of an undergraduate degree or similar qualification or experience. In the event of some candidates lacking previous training or experience in the prerequisite areas of competence, they will have to undergo training at a lower level to gain entry to the municipal financial management qualification.

Framework of qualification

The Level 6 municipal financial management qualification is a unit standards-based postgraduate certificate covering no less than twenty areas of competence.

Training

The National Treasury has set up an approval board to review training material offered in terms of the PFMA. This board will also be utilised to review all training material offered in terms of the *MFMA*.

As soon as the qualification mentioned above has been registered, the National Treasury will invite all service-providers to submit bids for approval. This process will ensure quality and relevance in terms of content so as to ensure value for money.

In the interim, all municipal managers have been cautioned not to send their officials to training courses that purport to be of high quality and offering assistance in the implementation of the Act.

Summary

The *MFMA* sets out to modernise financial management in a holistic manner. In order to achieve these objectives, ongoing skills development, training and re-training will be required if we are to keep pace with international best practice.

PART FIVE

MISCELLANEOUS

Chapter 14: Role of national and provincial government

Background

The *MFMA* and recent amendments to the Municipal Systems Act require a closer co-operative relationship within and between the different spheres of government, especially on planning, budgeting and financial management and in areas of service delivery. The *MFMA* provides a role for national and provincial government support, capacity-building and monitoring of municipalities, while providing mechanisms in which parastatals and other public entities are required to engage with municipalities. Although the power to implement the *MFMA* has been assigned to the National Treasury, these responsibilities will be delegated to provincial treasuries as capacity is developed over the medium term. Provincial treasuries will be required to work closely with other departments such as local government and housing, health, etc. in the provinces to implement the *MFMA*. Provincial governments are closer to municipalities and in a better position to provide capacity-building and other support and are more likely to respond appropriately to local circumstances.

National government

The National Treasury is, however, responsible for prescribing all regulations, frameworks, budget formats, inflation limits and other information required by the Act in order to ensure uniform norms and standards for implementation. Regular consultation with provincial treasuries has been established to ensure that they have adequate capacity to discharge their responsibilities when these come into effect. This is planned for 1 July 2005. In recognition of their current inadequate capacity, the initial implementation and monitoring will be performed by the National Treasury. However, once provincial treasuries have been geared for their monitoring and reporting obligations, they will be responsible for monitoring compliance and addressing weaknesses in municipal reporting and compliance. The National Treasury will continue to provide policies, frameworks and adequate support and will focus its monitoring on the largest municipalities for macro-economic management purposes.

The monitoring and reporting obligations will allow for early warning and efficient responses in the case of municipalities experiencing financial distress, with appropriate interventions being instituted to ensure that municipalities recover. Intervention by the National Treasury would be necessary only where all other options have failed. In order to reduce onerous requirements for reports and information, all reports will be shared with relevant provincial departments and published on websites or in gazettes.

Other national government departments also have a key role to play in policy development and the execution of programmes in provinces and municipalities. National departments such as the Provincial and Local Government have an overarching responsibility, while departments such as Water Affairs and Forestry, Minerals and Energy, Transport, Housing, etc. have a direct role in monitoring sector-specific outcomes and service delivery. The monitoring responsibilities will be made easier on municipalities and these departments with the production of relevant documentation also addressing the needs of the sectors. In this regard it is imperative that municipalities prepare their capital and operating budgets, in-year reporting, annual reports, etc. with this in mind and provide information that will support decision-making. A uniform set of data and budget formats is therefore required in the *MFMA* and the National Treasury plans to issue regulations to ensure the adequacy of information reported. Municipalities are reminded of the provisions in the Division of Revenue Act and the guidance provided in the Circular on Annual Reports during 2003 mentioned earlier.

Provincial government

In the short term, and in respect to financial management matters in municipalities, provincial government will continue with current practices until the provisions of the *MFMA* are fully implemented. In the interim, any new initiatives should be consistent with the spirit of the *MFMA*. Discussions are being held with the affected provincial departments to ensure the system is maintained over this period.

Summary

The delegations and responsibilities will be devolved over the medium term, as capacity is developed to execute the roles and responsibilities envisaged in the *MFMA*. Municipalities are requested to contact the National Treasury should questions arise.

Chapter 15: Internal controls, audits and audit committees

The powers and responsibilities of the Auditor-General provided in the Constitution of the Republic serve to underscore the independence and responsibility in auditing the finances and financial management of all national and provincial governments and municipalities. Reports are required from the Auditor-General and are to be made public. These measures therefore serve to promote public accountability. The *MFMA* requires municipalities to create and maintain appropriate structures, internal controls and committees to ensure proper management of public resources. Given the capacity of many municipalities, these provisions will be phased in from 1 July 2005 based upon capacity.

Internal control and audit

The Act contains various references to requirements for councils to implement appropriate financial management systems and internal controls. Where possible, the Act prefers to legislate the requirement for a financial management system or internal control methodology rather than stipulating the process or procedure to be used.

Management of financial systems and internal control procedures

Chapter 8 of the Act requires that the municipal manager take responsibility for the management of the municipality's income and expenditure, cash and banking, investments and borrowings and assets and liabilities, including the development of appropriate internal controls and financial management systems, subject to certain delegations of responsibility.

The Act also stipulates clear controls for the management of bank accounts and withdrawals from accounts (Chapter 3) and for incurring or providing security for short or long-term debt (Chapter 6).

Chapter 10 places responsibilities similar to those of the municipal manager on the chief executive officer of a municipal entity. The chief executive officer must report details of the entity's bank accounts to the municipal manager of the parent entity. Appropriate systems and policies must be in place to manage the entity's income and expenditure, assets and liabilities, budgets and financial reporting. The council of the parent municipality must also oversee compliance with these provisions.

Internal audit and the audit committee

The Act requires municipalities to have an internal audit unit and an audit committee to further strengthen the separation of functions relating to financial management. The internal audit unit should provide the municipal manager and the chief financial officer with advice and assistance on internal controls and on risk assessment and management. The council audit committee must be established to provide the council of the municipality and the board of directors of a municipal entity with independent advice, to review financial statements, to respond to the council on audit queries, to conduct investigations into specific financial problems and to assist council as required. These provisions will be phased in over two years. Sharing of resources between municipalities in the interim is encouraged.

Chapter 16: Conclusion

The National Treasury and provincial treasuries will provide municipalities implementing the MFMA with ongoing support and assistance.

This introductory guide provides municipalities with a broad overview of matters to be addressed, including aspects of governance, roles and responsibilities of councillors and officials, public accountability, financial management and budget processes, linkages with other legislation, supply chain management and training and capacity building. The phased implementation strategy recognises the capacity differences between municipalities. Further guides are being prepared and will be issued on a regular basis to support municipalities in implementing the Act. The National Treasury, along with the provincial treasuries, will play a facilitation role and are committed to providing municipalities with appropriate advice and assistance over the medium term for a successful implementation of the *MFMA*.

The following support can be expected from the National Treasury:

- Regular workshops and training sessions
- Regular updates on their websites and issuing of guides and support material
- Finalisation of regulations and frameworks
- Development of accreditation process for trainers
- Dedicated email address to receive and respond to enquiries

Forthcoming guides and support material include the following topics:

- Annotated Guide
- Service Delivery and Budget Implementation Guide
- Councillor Guide
- Entities Guide
- Annual and Financial Reporting Guide
- Cash Management Guide
- Roles and Responsibilities of Accounting Officers
- Supply Chain Management and PPPs
- Borrowing Guide
- Costing Guide
- Economic Reporting and Classification
- Assets and Liabilities Management
- Audit Guide
- Internal controls and Risk Management
- Project and Change Management
- Support and Interventions
- Financial Misconduct
- Unit Standards
- Investment Framework

General enquiries on the *Municipal Finance Management Act*, including its interpretation, should be directed to mfma@treasury.gov.za or 012 315 5850 (tel) or 012 315 5230 (fax).

PART SEVEN

THE MFMA IN DETAIL

Purpose of the Act

The **objective of the Act** is to secure sound and sustainable management of the fiscal and financial affairs of municipalities and municipal entities by establishing norms and standards and other requirements for –

- ensuring transparency, accountability and appropriate lines of responsibility in the fiscal and financial affairs of municipalities and municipal entities;
- the management of their revenues, expenditures, assets and liabilities and the handling of their financial dealings;
- budgetary and financial planning processes and the co-ordination of those processes with the processes of organs of state in other spheres of government;
- borrowing;
- the handling of financial problems in municipalities;
- supply chain management; and
- other financial matters.

Application of the Act

The Act applies to –

- all municipalities;
- all municipal entities; and
- national and provincial organs of state in relation to their financial dealings with municipalities.

Chapter One – Interpretation, Object, Application and Amendment of Act

Chapter summary

Chapter 1 provides definitions of the terms and concepts used in the Act. It outlines the scope of the legislation and to whom it applies and it determines the conditions under which amendments to the legislation may be made.

Chapter One in detail

Definitions

Definitions for terms used in the Act are listed. The meanings of other terms that have a bearing on the interpretation of clauses of the Act are found in other legislation, primarily the *Division of Revenue Act*, the *Municipal Structures Act* and the *Municipal Systems Act.* Some may also be found in policy documents such as the *Intergovernmental Fiscal Review* (IGFR), which is available from the National Treasury.

Object of the Act

In summary, the objective of the legislation is to ensure the financial sustainability of municipalities by establishing clear and uniform standards of good governance and financial management.

Institutions to which the Act applies

The *MFMA* applies to all municipalities, municipal entities and national and provincial departments in relation to their financial dealings with municipalities. It must prevail in instances where there is inconsistency between this and any other Act on matters that regulate the fiscal and financial affairs of municipalities.

Amendments to the Act

The Minister and the Financial and Fiscal Commission must agree in writing to any proposed law or amendments to law that may conflict with the *MFMA.*

Chapter Two – Supervision over Local Government Finance Management

Chapter summary

Chapter 2 deals with the powers of the National Treasury and all provincial treasuries with regard to local government finances and fiscal powers. It allows the Minister to delegate the powers of the National Treasury to national or provincial departments.

Chapter Two in detail

General functions of the National Treasury and provincial treasuries

The *Constitution*, the *Public Finance Management Act* and the *MFMA* establish certain responsibilities that must be fulfilled by the National Treasury and provincial treasuries. Chapter 13 of the *Constitution* and Chapter 2 of the *MFMA* provide more detail on these responsibilities. The responsibilities must be carried out within a framework of co-operative government and apply when co-ordinating intergovernmental financial relations and enforcing compliance with certain legislation.

In order to comply with the above requirements, the National Treasury may monitor, review, investigate and make recommendations on the different financial management systems of municipalities (including budgets, income, expenditure and borrowings) to ensure that they comply with the *MFMA* and other national policy and to promote good financial management. The National Treasury may be required to take further action against a municipality under certain circumstances where a serious or persistent breach of the legislation occurs.

A provincial treasury must monitor and assist municipalities in its province in their efforts to comply with the legislation and must perform any duties delegated to it by the National Treasury.

The Minister, as head of the National Treasury, takes all relevant decisions in terms of the *MFMA* except those delegated in terms of the Act. Similarly, the MEC for finance in a province, as head of the provincial treasury, takes all relevant decisions in terms of the *MFMA* except those delegated in terms of the Act.

Delegations by the National Treasury

The Minister may delegate the powers or duties assigned to the National Treasury under the *MFMA* to the Director-General of the National Treasury or to the MEC responsible for a provincial government department, subject to the agreement of the MEC of the province. The provincial MEC for finance may also delegate the powers or duties assigned to the provincial treasury under the *MFMA* to the head of the relevant provincial department.

The Minister cannot, however, delegate the power to stop funds to a municipality for a serious or persistent breach of the legislation.

The *provincial treasury* must promote the objects of the *MFMA* and assist the National Treasury in enforcing compliance within the constitutional framework.

Chapter Three – Municipal Revenue

Chapter summary

Chapter 3 sets out the framework for municipal bank accounts and cash, investment and asset management. It deals with the opening and control of bank accounts by municipalities, it grants power to the National Treasury to prescribe a framework for cash management and management of investments and it establishes certain parameters around the disposal of capital assets.

Chapter Three in detail

Part 1: Municipal bank accounts

Opening of bank accounts

Every municipality must open and maintain at least one bank account. All moneys received must promptly be paid into a bank account in the name of the municipality in accordance with the Act. Municipalities may not open a bank account abroad or with an institution not registered as a bank in the Republic of South Africa.

Primary bank account: Bank account details to be submitted to provincial treasuries and Auditor-General

The municipal manager must advise the National Treasury, the relevant provincial treasury and the Auditor-General in writing, details of its primary bank account, or any change to its primary bank account, for the purpose of receiving income from allocations, investments or municipal entities or entities collecting on behalf of municipalities. All allocations due to the municipality from another sphere of government must be paid into the primary bank account.

Control of municipal bank accounts

The municipal manager must administer all bank accounts and is accountable to the council for them. Some aspects of the administration of these accounts may be delegated to the chief financial officer only.

Withdrawals from municipal bank accounts

Only the municipal manager or chief financial officer may withdraw or authorise the withdrawal of monies from a municipal bank account. This power may be delegated to another senior finance official in writing and subject to certain conditions. Withdrawals may be made only in accordance with the Act and a consolidated report on withdrawals is to be submitted to the council, the relevant provincial treasury and the Auditor-General on a quarterly basis.

Relief, charitable, trust and other funds

Relief, charitable, trust and other funds may be established only in the name of the municipality, with only the municipal manager as the accounting officer.

Part 2: Cash, investment and asset management

Cash management and investments

Each year, all banks and other financial institutions must provide the Auditor-General and, where requested, the National Treasury with details in writing of every bank account and every investment held by a municipality. The Minister may prescribe a framework for municipalities to manage their cash and investments.

Disposal of capital assets

A municipality may not dispose of a capital asset needed to provide a minimum level of basic municipal services. Other capital assets may be disposed of after a public meeting except if disposal of to another municipality, municipal entity or organ of state.

Chapter Four – Municipal Budgets

Chapter summary

Chapter 4 determines the budget process for municipalities, over a three-year budgeting framework. It standardises the format of budget documentation and links the budget to other related policy and planning processes. It modernises the budget process, allowing for a system of votes on expenditure, a capital and an operating budget and a consultative process of hearings after the tabling of the budget. Councils are made ultimately responsible for approving budgets, within a local government financial management framework.

Chapter Four in detail

Appropriation of funds for expenditure
Unless specifically provided in the Act, a municipality may incur expenditure only in terms of an approved budget within the limits of the amounts appropriated in each budget vote.

Annual budgets
The mayor must table the annual budget before council by 31 March. Council must approve the budget by 30 June.

Contents of annual budgets and supporting documents
The annual budget must be presented in a prescribed format, divided into operating and capital, setting out revenue by source and expenditure by vote for three years. When tabled at council, it must be accompanied by the following information:

- Draft council resolutions approving the budget and imposing municipal taxes and tariffs
- Performance objectives for revenue from each source and for each budget vote linked to the integrated development plan
- A cash flow statement
- Proposed amendments to the integrated development plan and budget related policies
- Investment particulars
- Particulars of municipal entities and service delivery agreements
- Details of allocations or grants by the municipality
- Details of employment costs of elected members, boards of directors and senior management staff

Funding of expenditure
The budget may be funded only from realistically anticipated revenues, cash-backed surplus funds from the previous year and borrowings (the latter for capital expenditure only).

Capital projects
A municipality may spend money on a capital project only if the money for the project has been allocated in the capital budget and if the project is approved by council and the sources of funding are available and not committed for other purposes. Before approving a project, the council must consider the projected cost and the future operational costs and revenue on the project, including tax and tariff implications.

Matters to be prescribed
The Minister must prescribe the form of the annual budget and may prescribe various other matters, including inflation projections, the form of budget resolutions and certain uniform norms and standards. The Minister may also ensure that a municipality does not materially and

unreasonably prejudice national economic policies, economic activities across municipal boundaries and the national mobility of goods, services, capital or labour.

Budget preparation process
The mayor must co-ordinate the budget preparation process and the review of the integrated development plan and budget-related policies. The mayor must table at council a timetable of key deadlines relating to these processes. The mayor must take into account the municipality's integrated development plan, including any revisions, and national and provincial legislation, policy and budgets and must consult with other parties affected by the budget. The mayor must also provide the National Treasury, the relevant provincial treasury and other affected parties with information on the budget.

Publication of annual budget
Immediately after the annual budget is tabled in council, the municipal manager must make public all documentation and invite the community to submit its views. The municipal manager must submit the budget to the National Treasury, the relevant provincial treasury and other affected parties.

Consultations on tabled budgets
Once the budget has been tabled, the council must consider the views of the community, the National Treasury, the relevant provincial treasury and other parties affected by the budget. After considering all submissions, the council must allow the mayor an opportunity to respond to the submissions received and revise the budget if necessary.

Approval of annual budgets
The council must consider approval of the budget by 1 June each year. It must be approved by resolution by 30 June. Once approved, it must be sent by the municipal manager to the National Treasury and relevant provincial treasury.

Failure to approve budget before start of budget year
If a council fails to approve a budget, it must reconsider it again within seven days. This process must be repeated until a budget is approved. If it has still not approved a budget by 1 July, the mayor must immediately report the matter to the provincial MEC for local government.

Consequences of failure to approve budget before start of budget year
If the budget or any revenue-raising measures are not approved by 1 July, the provincial executive must intervene. This may include dissolving the council and appointing an administrator in the interim and approving a temporary budget or revenue raising measures to provide for the ongoing functioning of the municipality.

Non-compliance with provisions of the Chapter
The mayor, once aware of any impending non-compliance with legislation, must inform the provincial MEC for finance. On becoming aware of any actual non-compliance with this chapter of the Act, the mayor must inform the council, the MEC for finance and the National Treasury in writing.

Municipal adjustments budgets
A municipality may revise an approved budget through an adjustments budget. The adjustments budget must contain certain prescribed information and should be limited in timing and frequency during the course of a year. It must contain appropriate justifications and supporting material.

Unforeseen and unavoidable expenditure
The mayor may in certain circumstances authorise unforeseeable and unavoidable expenditure. The mayor must report such expenditure to the council at its next meeting and it must be

allocated in an adjustments budget. If the adjustments budget is not passed, however, the expenditure becomes unauthorised.

Unspent funds

Unless specifically appropriated in a multi-year budget, funds that remain unspent at the end of the financial year lapse.

NOTE: The MFMA does not specifically deal with outstanding legal commitments at the end of a financial year. National Treasury should consider making a recommendation that these outstanding legal obligations be re-appropriated in an amendments budget.

Shifting of funds between multi-year appropriations

Expenditure in a capital programme appropriated for more than one year may exceed that year's appropriation, but by no more than 20%. It must be funded from next year's budget. The increase must first be approved by the mayor, and the municipal manager must certify that the decision can be appropriately funded.

Unauthorised, irregular or fruitless and wasteful expenditure

Unauthorised expenditure includes overspending of money by vote or by total budget and expenditure from a vote that is unrelated to the department concerned (a vote is one of the main segments that divide a budget, which is based around departments or functional areas). It also refers to incorrect spending against a specific purpose, allocation or grant condition.

Irregular expenditure includes expenditure made that is not in accordance with certain legislation with or policies on supply chain management.

Fruitless and wasteful expenditure is expenditure made in vain that could have been avoided with reasonable care.

Councillors and officials may be liable in certain circumstances for unauthorised expenditure, and each has clear and distinct responsibilities to prevent such expenditure. Parties must also report under law all cases of expenditure that constitute a criminal offence and all cases of theft and fraud.

Contracts having future budgetary implications

A municipality may enter into a contract imposing financial obligations beyond one budget year. Council must consult with the community and other government agencies on any proposal to enter into a contract beyond the three years covered in the multi-year budget.

Chapter Five – Co-operative Government

Chapter summary

Chapter 5 deals with co-operative government. It requires national and provincial government to assist local government in building its financial management capacity. It outlines the process whereby national and provincial government is required to make three-year budgeted grant allocations to municipalities to enable those municipalities to prepare their three-year budgets. The chapter also discusses the stopping of funds by national or provincial governments under certain circumstances, monitoring of prices for bulk resources and disputes between different spheres of government.

Chapter Five in detail

Capacity-building

Notwithstanding a municipality's own responsibilities for compliance with the Act, national and provincial governments must assist and support municipalities in building their capacity and in identifying and resolving their financial problems.

Promotion of co-operative government by national and provincial institutions

National and provincial governments must promote co-operative government, they must meet their financial commitments promptly and provide timely information to enable municipalities to properly plan and develop their annual budget and integrated development plan.

National and provincial allocations to municipalities

The accounting officer of a national or provincial government department must each year notify the National Treasury or the relevant provincial treasury of all proposed allocations to be transferred to each municipality over the next three financial years. The Minister or the provincial MEC for finance must make the allocations public when tabling the national or provincial budget.

Promotion of co-operative government by municipalities

Municipalities must also promote co-operative government; they must meet their financial commitments and provide relevant municipalities and national and provincial departments with the appropriate financial information promptly.

Stopping of funds to municipalities

The National Treasury may, after consultation as prescribed, stop certain grant allocations to a municipality where the municipality commits a serious or persistent breach of the *Constitution* or any terms or conditions by which the allocation is made.

Stopping of equitable share allocations to municipalities

A decision to stop the equitable share allocation must be approved by Parliament.

Stopping of other allocations to municipalities

The accounting officer of the national or provincial department responsible for stopping a municipal allocation must report this in the department's annual financial statements.

Monitoring of prices and payments for bulk resources

The National Treasury must monitor the pricing structure for electricity, water and certain other services as prescribed that are supplied to municipalities and municipal entities by national or provincial departments.

Price increases of bulk resources for provision of municipal services

A national or provincial organ of state wishing to increase the price of electricity, water or any other bulk resource as prescribed must consult with the National Treasury and local government prior to submitting the proposal to its executive authority and any regulatory agency for approval. Unless determined otherwise by the Minister, a price increase shall take effect at the earliest on 1 July (if determined before 15 March) or at the earliest on 1 July the following year (if determined after 15 March).

Applicability of tax and tariff capping to municipalities

Unless determined otherwise by the Minister, any tax and tariff capping by a national or provincial department shall take effect at the earliest on 1 July (if determined before 15 March) or at the earliest on 1 July the following year (if determined after 15 March).

Disputes between organs of state

Any disputes between different spheres of government must be resolved out of court where possible. If not party to the dispute, the National Treasury may help mediate if so requested.

Chapter Six – Debt

Chapter summary

Chapter 6 deals with the borrowing of money by municipalities, both long-term and short-term. It discusses certain conditions on borrowing and issues of security, disclosure and municipal guarantees.

Chapter Six in detail

Short-term debt

A council may resolve to incur short-term debt to bridge operating shortfalls in expectation of realistic anticipated income or for capital shortfalls in expectation of enforceable allocations. This may only be incurred if the mayor and municipal manager sign a council resolution approving the debt. All short-term debt is to be repaid within the financial year and cannot be extended beyond that. Lenders may not extend credit to a municipality for the purpose of renewing or refinancing short-term debt. Municipalities with short-term debt at 1 July 2004 will be required to pay off the short-term debt in full by 1/7/2008. In the meantime these municipalities are required to gradually reduce their short-term borrowing, by at least 25 percent each year.

Long-term debt

A council may resolve to incur long-term debt only for capital expenditure on property, plant or equipment required for the purpose of achieving the objectives of local government or for refinancing existing long-term debt. Such debt may be incurred only if the mayor and municipal manager sign a council resolution approving the debt. It is a requirement for the public to be provided with particulars of the proposed debt and invited to comment prior to the council meeting convened to consider the proposal.

Conditions applying to both long-term and short-term debt

Debt may be incurred only in rand value and may not be indexed to, or affected by, fluctuations against any foreign currency.

Security

A municipality may provide security for debts ranging from physical assets through to rights to future revenue. If a council provides security in the form of a physical asset that is necessary for the provision of basic services, then the council must resolve how that minimum level of service will be protected.

Disclosure

Persons representing the municipality to borrow money must disclose all information fully and accurately.

Municipal guarantees

A council may provide a municipal guarantee only for an organ of state and a municipal entity under its sole control or, in the case of a municipal entity under shared control or any other person, with the approval of the National Treasury and subject to obtaining adequate insurance for the financial exposure. All guarantees must be within the limits specified in the approved budget of the municipality.

National and provincial guarantees

Neither National nor provincial governments may guarantee debt for a municipality or a municipal entity.

Chapter Seven – Responsibilities of Mayors

Chapter summary

Chapter 7 outlines the role and responsibilities of the mayor, representing the executive authority of the council. Issues relating to the roles and responsibilities of the mayor are discussed in detail in Chapter 5 of this guide.

Chapter Seven in detail

General responsibilities

The mayor exercises the powers and duties assigned by the Act or delegated by council. The mayor provides political guidance on the financial affairs of the municipality and must ensure that the municipality complies with its legislated functions. Without interfering, the mayor may monitor and oversee the exercise of the responsibilities of the municipal manager and chief financial officer.

Budget processes and related matters

The mayor provides the political guidance on the budget process and must ensure that the municipality complies with the budget requirements, including those relating to the service delivery and budget implementation plan and annual staff performance agreements. The mayor must submit a budget implementation and finance report to the council quarterly.

Budgetary control and early identification of financial problems

On receiving from the municipal manager monthly or mid-year budget reports, the mayor must take appropriate action to identify and resolve any financial problems that are evident.

Report to provincial executive if conditions for provincial intervention exist

The mayor must report to the MEC for local government issues that may necessitate provincial intervention.

Exercise of rights and powers over municipal entities

The mayor must guide the municipality in its dealings with municipal entities to ensure that they remain accountable to the municipality and comply with the Act.

Municipalities that do not have mayors

A council that does not have a mayor must delegate to a councillor the powers and functions of a mayor as contained in this Act.

Municipalities with executive committees

The mayor of a council that has an executive committee must exercise his or her powers and functions in consultation with the executive committee.

Delegations of mayoral powers and duties

The powers and functions of a mayor as contained in this Act may be delegated to another councillor under certain circumstances and subject to certain conditions.

Chapter Eight – Responsibilities of Municipal Officials

Chapter summary

Chapter 8 outlines the role and responsibilities of municipal officials, representing the administrative authority of the council. Issues relating to the roles and responsibilities of municipal officials are discussed in detail in Chapter 5 of this guide.

Chapter Eight in detail

Part 1: Accounting officers

Municipal managers to be accounting officers
The accounting officer of a municipality is the municipal manager, who must exercise the powers and duties assigned in the Act and provide the municipality and municipal entities with guidance and advice.

Fiduciary responsibilities of accounting officers
As the accounting officer, the municipal manager must act with honesty and in the best interests of council and disclose all available facts that may influence the decisions of council. The position may not be used for personal gain or to improperly benefit others.

Financial management

General financial management functions
The municipal manager is responsible for the financial management of the municipality. This includes ensuring that resources are used effectively, full and proper financial records are kept and appropriate control systems are maintained. The municipal manager must ensure that unauthorised, irregular or fruitless and wasteful expenditure is prevented and that disciplinary or criminal proceedings are instituted when required.

Asset and liability management
The municipal manager is responsible for the management of the municipality's assets and liabilities, ensuring that the appropriate systems and policies are in place to adequately safeguard and maintain the municipality's assets.

Revenue management
The municipal manager is responsible for the management of the municipality's revenue, which includes the development and maintenance of appropriate revenue-raising and collection systems.

Expenditure management
The municipal manager is responsible for the management of the municipality's expenditure. This includes the development and maintenance of appropriate expenditure management systems.

Expenditure on staff benefits
The municipal manager must report to council on staff salaries, wages, allowances and benefits.

Funds transferred to organisations and bodies outside government
The municipal manager may transfer funds to organisations outside of government only if satisfied that the organisation meets certain financial requirements.

Budget preparation
The municipal manager must assist the mayor in the preparation of the budget and provide the necessary administrative support and information to help the mayor in the performance of that function.

Budget implementation
The municipal manager must implement the approved annual budget and when necessary prepare an adjustments budget. The municipal manager must, within fourteen days of the approval of the annual budget, submit to the mayor a draft service delivery and budget implementation plan and draft annual performance agreements for all senior managers that report to the municipal manager.

Impending shortfalls, overspending and overdrafts
The municipal manager must report to council impending shortfalls and overspending and must report to the National Treasury any overdraft position.

Reports and reportable matters

Monthly budget statements
The municipal manager must submit to the mayor and relevant provincial treasury monthly reports on budget progress in the prescribed format and with the appropriate details. The relevant provincial treasury must submit to the National Treasury and make public a consolidated statement of the budget progress of each municipality within that province monthly. The provincial MEC for finance must provide to the provincial legislature with a consolidated statement each quarter.

Mid-year budget and performance assessment
The municipal manager must submit a mid-year budget report and performance assessment to the mayor, the National Treasury and the relevant provincial treasury by 25 January.

Reports on failure to adopt or implement budget-related and other policies
The municipal manager must inform the provincial treasury in writing of any failure by the council or an office-bearer to adopt or comply with budget-related policies.

General reporting obligation
The municipal manager must submit to the National Treasury, provincial treasury and provincial department of local government or Auditor-General such information as may be prescribed or required.

Information to be placed on websites of municipalities
It is the responsibility of the municipal manager to place on the municipality's website certain financial documentation within five days of its being tabled at council or made public.

Protection of accounting officer
No action may be taken by a council or councillor against a municipal manager solely owing to that officer's compliance with any provision of this Act.

Part 2: Financial administration

Top management of municipalities
Top management consists of the municipal manager, the chief financial officer, all senior managers responsible for managing budget votes and any other senior officials designated by the municipal manager. These managers are required to assist the municipal manager in managing and co-ordinating the finances of the municipality.

Senior managers and other officials of municipalities

Each senior manager and each official exercising financial management responsibilities must take appropriate steps to manage the municipality's finances correctly, subject to the direction of the municipal manager.

Delegations

The municipal manager must develop and review an appropriate system of delegations. Powers or duties assigned to the municipal manager may be delegated to top management or other senior officials.

Chapter Nine – Municipal Budget and Treasury Offices

Chapter summary

Chapter 9 requires that municipalities establish a budget and treasury office, under the control of a chief financial officer accountable to the municipal manager. It outlines the responsibilities of the chief financial officer and provides for delegations and minimum competency levels for officials with any financial management responsibility.

Chapter Nine in detail

Establishment

Every municipality must have a budget and treasury office, which consists of the chief financial officer, municipal officials allocated to the chief financial officer and other staff contracted to work in that office. The municipal manager appoints the chief financial officer and allocates officials to the chief financial officer.

Role of chief financial officer

The chief financial officer runs the budget and treasury office, advises the municipal manager on his or her accounting responsibilities, assists the municipal manager to manage the municipality's bank accounts and helps prepare and implement the annual budget. The chief financial officer advises other senior managers and officials on their accounting responsibilities and performs budgeting, accounting, financial reporting, cash and debt management, supply chain management, financial management and other duties that are delegated by the municipal manager.

Delegations

The chief financial officer may delegate any of the above functions to certain officials or other staff, except the role of assisting the municipal manager regarding bank accounts and annual budgets. If anything is delegated to someone who is not an employee of the municipality, the chief financial officer must ensure that sufficient systems and procedures are in place to ensure proper control and accountability.

Competency levels of professional financial officials

The municipal manager, chief financial officer, senior managers and other financial officials must meet prescribed standards of competency. The municipality must help train officials by providing appropriate resources and opportunities for development.

Chapter Ten – Municipal Entities

Chapter summary

Chapter 10 establishes the financial governance framework for municipal entities. It establishes the chief executive officer as the accounting officer responsible to the board of directors and sets out the powers and functions of that officer. It also discusses roles and responsibilities of the council and the municipal manager in regard to an entity.

Chapter Ten in detail

The following important definitions relating to municipal entities are contained in amendments to the *Municipal Systems Act* (see section 1 of the *Local Government: Municipal Systems Amendments Act*, Act 44 of 2003):

A municipal entity is defined as:

> "a company, co-operative, trust, fund or any other corporate entity established in terms of any applicable national or provincial legislation and which operates under the ownership control of one or more municipalities, and includes, in the case of a company under such ownership control, any subsidiary of that company; a private company; a service utility; or a multi-jurisdictional service utility."

A parent municipality is defined:

a) "in relation to a municipal entity which is a private company in respect of which effective control vests in a single municipality, [as] that municipality;
b) in relation to a municipal entity which is a private company in respect of which effective control vests in two or more municipalities collectively, [as] each of those municipalities;
c) in relation to a municipal entity which is a service utility, [as] the municipality which establishes the entity; or
d) in relation to a municipal entity which is a multi-jurisdictional service utility, [as] each municipality which is party to the agreement establishing the service utility."

Part 1: Establishment

Financial implications for municipalities

A municipality, when considering establishment of or participation in a municipal entity, must determine the function or service that entity would perform on its behalf and make an assessment of the impact that the shift would have on the municipality's staff, assets and liabilities. The municipal manager must then make the proposal public and invite comment from the community and other affected parties. The council must take into account the views of stakeholders in any subsequent decision.

Part 2: Financial governance

Bank accounts

Entities must open and maintain at least one bank account. All moneys received must be paid into a bank account in the name of the entity. Entities may not open a bank account abroad or with an institution not registered as a bank or without the approval of the board of directors. The accounting officer of the entity must administer that entity's bank accounts and is accountable to its board of directors.

Bank account details
The chief executive officer of an entity must advise the municipal manager in writing of details of its bank accounts. The municipal manager must then provide the Auditor-General, the National Treasury and the relevant provincial treasury with these details.

Budgets
The board of directors of an entity must submit a proposed budget to the municipality by 31 January or earlier if agreed. The council must consider the budget and return any recommendations to the board of directors, who may submit a revised budget by 22 March. The revised budget must then be tabled by the mayor at the same time that the municipal budget is tabled. The board of directors must approve the budget by 1 June and it must then be made public. The board of directors may revise the budget with the approval of the mayor and only under certain circumstances.

The accounting officer of an entity must report budget progress to the municipal manager of the parent municipality in a prescribed format each month.

Mid-year budget and performance assessment
The chief executive officer of an entity must submit a mid-year budget report and performance assessment to the board of directors and parent municipality by 20 January.

Remuneration packages
The municipality must determine the upper limits and ensure that the entity reports on the cost of the remuneration of the chief executive officer and senior managers of the entity.

Disposal of capital assets
Ownership of capital assets required to provide the minimum level of basic municipal services may not be transferred. Council must consult with the community on any proposal to dispose of an asset not considered necessary to provide the minimum level of basic services. This section does not apply to assets to be disposed, sold or transferred to another government department of entity.

Financial year
The financial year of an entity is the same as that of a municipality, i.e. 1 July to 30 June.

Audit
The Auditor-General must audit and report on the accounts and financial statements of all entities.

Part 3: Accounting officers

Chief executive officer to be the accounting officer
The accounting officer of an entity is the chief executive officer.

Fiduciary duties of accounting officers
As the accounting officer, the chief executive officer must act with honesty and in the best interests of the entity and disclose all available facts that may influence the decisions of the council and board of directors. The position may not be used for personal gain or to improperly benefit others.

General financial management functions of accounting officers

The chief executive officer is responsible for the financial management of the entity. This includes ensuring that resources are used effectively, full and proper financial records are kept and appropriate control systems are maintained. The chief executive officer must ensure that unauthorised, irregular or fruitless and wasteful expenditure is prevented and that disciplinary or criminal proceedings are instituted when required.

Asset and liability management

The chief executive officer is responsible for the management of the entity's assets and liabilities and for ensuring that the appropriate systems and policies are in place to adequately safeguard and maintain the entity's assets.

Revenue management

The chief executive officer is responsible for the management of the entity's revenue, which includes the development and maintenance of appropriate revenue-raising and collection systems.

Monthly reconciliation of revenue and accounts

The chief executive officer must ensure that revenue received and accounts are reconciled monthly.

Expenditure management

The chief executive officer is responsible for the management of the entity's expenditure, which includes the development and maintenance of appropriate expenditure management systems.

Budget implementation

The chief executive officer is responsible for implementing and monitoring the entity's annual budget.

Part 4: Reports and reportable matters

Impending under-collection, shortfalls, overspending, overdrafts and non-payment

The chief executive officer must report in writing to the board of directors and municipal manager any financial problems experienced by the entity. The municipal manager must table a report on this matter to the council at its next meeting.

Irregular or fruitless and wasteful expenditure

The board of directors must promptly report in writing to the mayor and municipal manager and the Auditor-General any irregular or fruitless and wasteful expenditure. The board of directors must also report any irregular expenditure or other loss resulting from real or suspected criminal conduct.

Reporting of improper interference by councillors

The chief executive officer must report to the Speaker of the municipality interference by a councillor outside of that councillor's assigned duties, relating to the financial affairs of the entity or the responsibilities of the board of directors.

General reporting obligations

The chief executive officer is responsible for all reporting obligations as required by the Act, unless otherwise stated. If the chief executive officer is unable to fulfil those responsibilities, the municipal manager must be advised.

Part 5: Other officials of municipal entities

Duties of other officials

Each official exercising financial management responsibilities must take appropriate steps to manage the entity's finances correctly, subject to the direction of the chief executive officer.

Delegation of powers and duties by accounting officers

Powers or duties assigned to the chief executive officer may be delegated to an official of that entity.

Competency levels of professional finance officials

The chief executive officer, senior managers and other finance officials must meet the prescribed financial management competency levels.

Part 6: General

Borrowing of money

An entity may borrow money only in accordance with its business plan and generally in line with the provisions of Chapter 6 of the Act.

Financial problems in municipal entities

If an entity experiences serious or persistent financial problems and the board of directors fails to act effectively, the municipality must either take action in relation to the service delivery agreement or impose a financial recovery plan or liquidate and disestablish the entity.

Chapter Eleven – Goods and Services

Chapter summary

Chapter 11 deals with the procurement of goods and services by a municipality and municipal entity. It discusses the supply chain management policy and process, as well as public-private partnerships, ensuring that the framework for these processes is fair, equitable, transparent, competitive and cost-effective.

Chapter Eleven in detail

Part 1: Supply chain management

Application
Supply chain management applies to the procurement of goods and services, the disposal of goods not required and the selection of contractors to supply services to a municipality or entity. It does not apply in instances where a municipality or entity contracts with another government department.

Supply chain management policy
Each municipality and entity must have and implement a supply chain management policy.

Supply chain management policy to comply with prescribed framework
The supply chain management policy of a municipality or entity must be fair, equitable, transparent, competitive and cost-effective and comply with the prescribed regulatory framework.

Unsolicited bids
A municipality or entity is not obliged to consider an unsolicited bid outside of its normal bidding or tender process. If it decides to consider an unsolicited bid, it may do so only in accordance with the prescribed framework.

Approval of tenders not recommended
If a tender other than the one recommended is approved, the municipal manager or chief executive officer must advise the Auditor-General, the National Treasury and the relevant provincial treasury in writing of the reasons for the decision.

Implementation of system
The municipal manager or chief executive officer must implement the supply chain management policy and must ensure that proper mechanisms are in place to minimise fraud, corruption, favouritism and unfair and irregular practices.

Contracts and contract management
Contracts or agreements procured through the supply chain management policy must be in writing, and must stipulate certain terms and conditions of the contract or agreement. The municipal manager and chief executive officer must ensure that contracts and agreements are properly procured and that contractor performance is monitored and reported as necessary. Contracts and agreements may be amended by either party, but only after reasons for the amendment are tabled in council and the local community has been consulted.

Councillors barred from serving on municipal bid committees

A councillor may not be a member of a municipal bid committee or any other committee evaluating or approving tenders, quotes, contracts or bids, nor may a councillor attend such meetings as an observer.

Interference

No person may interfere with the supply chain management system of a municipality or entity or amend or tamper with any tender or bid after submission.

Competency levels of officials involved in municipal supply chain management

The municipal manager and chief executive officer involved in the implementation of a supply chain management policy must meet the prescribed competency levels. The municipality must help train officials by providing resources or opportunities for development.

Part 2: Public-private partnerships

Conditions and process for public-private partnerships

A municipality may enter into a public-private partnership agreement if it can demonstrate that the agreement will provide value for money, is affordable and will transfer the appropriate technical, operational and financial risk to the private party. Before such an agreement is concluded the municipality must conduct a thorough feasibility study of the proposal and make public the findings for comment.

Chapter Twelve – Financial Reporting and Auditing

Chapter summary

Chapter 12 outlines requirements and procedures for the preparation, adoption and auditing of the annual financial statements of both municipalities and municipal entities. It details disclosure requirements and describes the consequences of non-compliance with certain provisions.

Chapter Twelve in detail

Preparation and adoption of annual reports

Every municipality and municipal entity must prepare an annual report for each year, which must be dealt with by council by 31 March. Its purpose is to provide a record of the activities and performance of the municipality during the year and to promote accountability to the community for its decisions. The annual report must also include the following:

- Audited annual (and consolidated) financial statements, together with any explanation and clarifications
- Auditor-General's audit report
- Annual performance report
- Municipal manager's assessment of performance against measurable budget objectives
- Particulars of corrective action taken on audit reports
- Recommendations made by the audit committee

Preparation of financial statements

Every municipality and municipal entity must prepare annual financial statements for each year in accordance with the provisions of the Act and generally recognised accounting practice.

Disclosures on intergovernmental and other allocations

The annual financial statements must disclose information on allocations received from or paid to national or provincial government or another municipality, how allocations were spent, compliance with any terms and conditions of those allocations and reasons for any non-compliance.

Disclosures concerning councillors, directors and officials

Notes to the financial statements must disclose information on the employment costs of councillors (or the board of directors for municipal entities) and certain officials, including money owed by councillors for rates unpaid.

Other compulsory disclosures

Notes to the financial statements must include a list of all municipal entities, contributions and details of certain expenditure items together with details of bank accounts and investments, contingent liabilities, particulars of non-compliance with provisions of the Act and any material loss from unauthorised expenditure with steps taken to recover that loss.

Submission and auditing of annual financial statements

The municipal manager must prepare the annual financial statements of the municipality and submit them to the Auditor-General by 31 August. Municipalities with municipal entities must prepare a consolidated financial statement and submit those statements to the Auditor-General by 30 September. The chief executive officer of a municipal entity must prepare the financial statements of the entity and submit them to the municipal manager and the Auditor-General by 31 August. The Auditor-General must submit an audit report to the municipal manager or chief executive officer within three months of receipt of the statements. If unable to do so, the Auditor-General must report the reasons for the delay to the municipal manager and the relevant provincial legislature and parliament.

Submission and tabling of annual reports
The chief executive officer of a municipal entity must provide the municipal manager of the parent municipality with the entity's annual report by 31 December, or earlier if agreed.

The mayor must table at council the annual reports of the municipality and any municipal entity by 31 January. If not able to do so, the mayor must provide council with the reasons for their not being ready. Once tabled in council, the municipal manager must publicise the annual report and invite community comment.

Compliance to be monitored
The municipal manager of the parent municipality must monitor compliance of its municipal entities with regard to annual reporting requirements.

Oversight reports on annual reports
The council must consider the annual report within two months of it being tabled. It must then adopt an oversight report containing its comments on the annual report, stating whether it approves, rejects or wishes it to be referred back for further revision. The municipal manager must attend the meeting at which the annual report is discussed and submit the minutes of this meeting to the Auditor-General, the relevant provincial treasury and the provincial department for local government. The municipal manager must also make public the oversight report.

Council meetings open to public and certain public officials
The council meeting(s) at which the annual report is discussed must be open to the public, the Auditor-General and all other national or provincial departments. Sufficient time must be allowed for those attending to address and discuss with the council any submissions made.

Issued raised by Auditor-General in audit reports
The mayor must ensure that the council addresses the issues raised by the Auditor-General in the audit report. The provincial MEC for local government must assess the annual financial statements, audit reports and council responses to those reports and determine whether the municipality has adequately addressed the issues raised. The MEC must then report any omissions by municipalities to the provincial legislature.

Submissions to provincial legislatures
The municipal manager must submit the annual report(s) of the municipality and its municipal entities with the relevant oversight report(s) to the provincial legislature.

Consequences of non-compliance with certain provisions
The Auditor-General must inform the Speaker of the council, the National Treasury, the MEC for local government and the MEC for finance about and issue a special report to Parliament on any failure by a council to submit financial statements to the Auditor-General or to table its annual report in council.

Annual report to Parliament
The Cabinet member for local government must report to Parliament on action taken by MECs for local government to address issued raised by the Auditor-General in audit reports on financial statements.

Chapter Thirteen – Resolution of Financial Problems

Chapter summary

Chapter 13 deals with the resolution of financial problems. It attempts to ensure that effective action is taken early by the municipality when financial problems are identified. Should the municipality be unable to resolve the problem itself, it may seek the assistance of the province. The Chapter gives effect to section 139 of the *Constitution*, which now provides for three types of provincial intervention.

The chapter provides for the management and termination of a financial recovery plan and for municipalities to seek temporary or extraordinary relief from their financial obligations by application to the High Court. The Chapter deals with the establishment of the Municipal Financial Recovery Service, its functions and powers and the appointment of its head and other officials.

Chapter Thirteen in detail

Part 1: Identification of financial problems

Primary responsibility for resolution of financial problems

The municipality is primarily responsible for avoiding, identifying and resolving its own financial problems. If it encounters a serious financial problem, it must immediately seek solutions to the problem and advise the provincial MEC for finance, the provincial MEC for local government and the South African Local Government Association.

Part 2: Provincial interventions

Types of provincial interventions

If the provincial MEC for local government becomes aware of a serious financial problem in a municipality, the MEC must consult the mayor and determine whether the situation necessitates further intervention in terms of section 139 of the *Constitution*.

Discretionary provincial interventions

If the financial problem has been caused by a failure to comply with an executive obligation under legislation and the conditions for an intervention under the *Constitution* are met, the provincial executive must decide whether or not to intervene. If the provincial executive decides to intervene, it must take the appropriate steps to assess the problem and discuss it further with the mayor with a view to resolving it.

Criteria for determining serious financial problems

In order to assess the seriousness of the financial problem for a discretionary intervention, the municipality and the provincial executive must consider a range of matters, including those prescribed.

Mandatory provincial interventions arising from financial crises

If a municipality, in financial crisis, is unable to provide basic services or meet its financial obligations, then the provincial executive must seek the assistance of the Municipal Financial Recovery Service to prepare a financial recovery plan for the municipality.

Criteria for determining serious or persistent material breach of financial commitments
In order to determine the conditions for a mandatory intervention, all relevant matters must be considered, including those prescribed.

Preparation of financial recovery plans
In the case of a discretionary provincial intervention, a financial recovery plan may be prepared by any suitably qualified person. In the case of a mandatory provincial intervention, it must be prepared by the Municipal Financial Recovery Service. Certain steps are prescribed in the development of a financial recovery plan, including a process for stakeholder consultation and comment.

Criteria for financial recovery plans
A financial recovery plan must be aimed at securing the municipality's ability to meet its obligations to provide basic services and to meet its financial commitments. It must therefore contain information as prescribed.

Approval of financial recovery plans
The provincial MEC for local government may approve, with or without amendment, a financial recovery plan prepared through a discretionary intervention. The provincial MEC for finance, in addition to the requirements described, must verify that the process set out in the Act was correctly followed for a mandatory intervention. The responsible MEC must submit the plan to the municipality, the Minister and the Cabinet member responsible for local government, the Auditor-General and the provincial local government association.

Amendment of financial recovery plans
The provincial MEC for finance or the provincial MEC for local government may request amendment of the financial recovery plan

Implementation of financial recovery plans in discretionary provincial interventions
The financial recovery plan must be implemented by the municipality, with progress reported to the provincial MEC for local government each month. The plan binds the municipality in exercising its executive authority, but only to the extent required to resolve its financial problems. If the municipality does not implement the plan, the provincial executive may take further action under the *Constitution* to ensure its implementation.

Implementation of financial recovery plans in mandatory provincial interventions
In the case of mandatory interventions, if the municipality fails to implement the financial recovery plan the provincial executive may either assume responsibility for the implementation of the plan or dissolve the council under certain circumstances and appoint an administrator to take the necessary remedial action.

Regular review of provincial interventions
The provincial MEC for finance or the provincial MEC for local government must each quarter review all interventions and provide the municipality, the Minister, the Cabinet member responsible for local government, the provincial legislature and the provincial local government association with progress reports.

Termination of provincial interventions
Intervention ends when a municipality is in a position to re-establish its financial obligations under legislation. Once ended, the provincial MEC for finance or the provincial MEC for local government must advise the parties involved.

Access to information, records and documents of municipalities
A provincial executive that intervenes in a municipality must have access to the information and documentation required for that intervention.

National interventions
The national executive must act in instances where a provincial executive fails to adequately exercise or perform its duties in terms of an intervention.

Part 3: Debt relief and restructuring

Application for stay of legal proceedings
A municipality unable to meet its financial commitments may apply to the High Court for a stay on legal proceedings, including the execution of legal process and claims by creditors. In an application for extraordinary relief, the municipality may seek from the court an order to suspend or terminate its financial obligations.

Suspension of financial obligations
Before issuing an order in response to a municipality's application for extraordinary relief, the court must be satisfied that the municipality cannot meet its financial obligations and that certain appropriate assets have been liquidated in accordance with the approved financial recovery plan.

Termination of financial obligations and settlement of claims
Where the court agrees to an application for a municipality to suspend its financial obligations, the provincial MEC for finance must appoint a trustee to prepare a distribution scheme for proportional settlement of all legitimate claims.

Matters to be prescribed
The Minister must make regulations to provide for an equitable process for recognition of claims against a municipality for the purposes of a distribution scheme, subject to certain limitations.

Part 4: Municipal Financial Recovery Service

Establishment
The Municipal Financial Recovery Service is formally established within the Public Service and functions within the National Treasury.

Functions and powers
The Municipal Financial Recovery Service exercises the powers and duties assigned by the Act. At the request of an MEC for finance, it may assist municipalities experiencing certain financial problems, prepare a financial recovery plan and monitor and implement that plan.

Appointment of head
The Minister must appoint a person from within the National Treasury as head of the Service.

Responsibilities of head
The head of the Service is responsible for the Service's performance and takes all decisions in the performance of its functions, subject to certain delegations, and directions from the Director-General of the National Treasury.

Staff
The staff of the Municipal Financial Recovery Service consists of the head, persons in the National Treasury and other persons seconded from a national or provincial department or other organisation as designated by or agreed to by the Director-General.

Delegations
The head may delegate certain powers and functions subject to certain conditions.

Chapter Fourteen – General Treasury Matters

Chapter summary

Chapter 14 deals with a number of general treasury matters, including the assignment of powers to the Minister to make regulations or issue instructions or guidelines relevant to the Act or municipal financial management in general. Provisions are also set for the creation of internal audit units and audit committees and in relation to forbidden activities of council and remuneration and benefits that may be paid to political office-bearers.

Chapter Fourteen in detail

Liabilities and risks payable in foreign currencies

Municipalities and municipal entities may not incur a liability payable in a foreign currency, except under specified circumstances.

Forbidden activities

Municipalities and municipal entities may not conduct any commercial activity except in exercising the powers and functions authorised by legislation or provide municipal services outside of their boundaries except with the approval of the council concerned. No municipality or municipal entity may make loans to councillors or officials or directors or members of the public.

Internal audit unit

Every municipality and entity must have an internal audit unit or function. The internal audit unit is required to prepare an audit plan and internal audit programme, provide the municipal manager and chief executive officer with advice and report to the audit committee on matters relating to internal audit and control. The internal audit function may be outsourced under certain circumstances.

Audit committees

Every municipality and entity must have an audit committee. The audit committee must be established as an independent advisory body to provide the council, officials and the board of directors with advice and to review annual financial statements, respond to council on matters raised by the Auditor-General and conduct investigations into financial issues as requested. Under certain circumstances, a single audit committee may be established for district municipalities and the local municipalities within that district or for a municipality and municipal entities under its control.

Councillors' remuneration

Political office-bearers and councillors may be remunerated by municipalities in accordance with the *Public Office-Bearers Act* and the *Constitution*. Payments outside those prescribed represent an irregular expenditure that must be dealt with accordingly. The provincial MEC for local government must report to the provincial legislature any non-compliance with this section of the Act.

Treasury regulations and guidelines

The Minister may make regulations and guidelines on all matters prescribed in the Act. Guidelines are not binding on a council unless that council adopts them.

Consultative process before promulgation of regulations

Prior to the promulgation of any regulations, the Minister must consult local government and publish draft regulations for comment.

Departures from Treasury regulations or conditions

The National Treasury may approve a departure from a Treasury regulation provided that good grounds are shown.

Chapter Fifteen – Financial Misconduct

Chapter summary

Chapter 15 is concerned with financial misconduct within municipalities and municipal entities. It also provides for a legal regime for disciplinary proceedings and empowers the Minister to make regulations prescribing procedures in this regard.

Chapter Fifteen in detail

Part 1: Disciplinary proceedings

Financial misconduct by municipal officials

An official of a municipality commits an act of financial misconduct if that official deliberately or negligently acts outside of the provisions of the Act. A municipality must investigate allegations of financial misconduct and if necessary institute the appropriate disciplinary proceedings.

Financial misconduct by officials of municipal entities

An official of an entity commits an act of financial misconduct if that official deliberately or negligently acts outside of the provisions of the Act. An entity must investigate allegations of financial misconduct and if necessary institute the appropriate disciplinary proceedings.

Part 2: Criminal proceedings

Offences

Municipal councillors and officials and directors and officials of entities are guilty of an offence if they participate in any action listed in this section of the Act.

Penalties

Persons may be liable on conviction of an offence to penalties prescribed in the relevant legislation.

Part 3: General

Regulations on financial misconduct procedures and criminal proceedings

The Minister may make regulations regarding procedures for misconduct and criminal proceedings.

Chapter Sixteen – Miscellaneous

Chapter summary

Chapter 16 provides for miscellaneous aspects. It limits liability in respect of anything done in good faith in terms of the legislation and allows the Minister to exempt municipalities and municipal entities from specific provisions of the legislation.

Chapter Sixteen in detail

Liability of functionaries exercising powers and functions in terms of this Act

Notwithstanding deliberate or negligent unlawful actions, municipalities and entities, and their office bearers and staff, are not liable in respect of any loss or damage resulting from the exercise of any lawful power or performance of an action in good faith.

Delays and exemptions

The Minister may delay the implementation of any provision of the Act or exempt any municipality or entity from any provision for a certain period of time and subject to certain conditions.

Transitional provisions

All municipalities and entities must submit to the National Treasury within three months of the Act coming into effect a list showing their interest in any corporate entity, public-private partnership and other types of contracts worth in excess of R1 million beyond 1 January 2007.

Repeal and amendment of legislation

The following legislation will be repealed as a consequence of this Act:

- Promotion of Local Government Affairs Act, 1993 – Section 17(D)
- Municipal Accountants Act, 1988
- Local Government Transition Act, 1993 – Section 10(G)

Short title and commencement

The legislation is called the *Local Government: Municipal Finance Management Act, 2003*, and takes effect from 1 July 2004, with implementation of certain key provisions to be phased in from 1 July 2004 to 1 July 2007.

Supporting Annexure

Delegations of Powers, Duties, and Functions as Contemplated in the Local Government: Municipal Financial Management Act, 2003

LEGISLATIVE REFERENCE		DETAIL OF DELEGATIONS		
Section	**Section Description**	**Power, Duty or Function**	**Delegated By**	**Delegated To**
10 (2)	Control of municipal bank accounts	(2) The accounting officer may delegate the duties referred to in subsection (1) (c) to the municipality's chief financial officer only.	Accounting officer	Chief financial officer
79 (1)	Delegations	(1) The accounting officer of a municipality– (a) must for the proper application of this Act in the municipality's administration develop an appropriate system of delegation that will both maximise administrative and operational efficiency and provide adequate checks and balances in the municipality's financial administration; (b) may, in accordance with that system [of delegations], delegate to a member of the municipality's top management referred to in section **77** or any other official of the municipality: (i) any of the powers or duties assigned to an accounting officer in terms of this Act; or (ii) any powers or duties reasonably necessary to assist the accounting officer in complying with a duty which requires the accounting officer to take reasonable or appropriate steps to ensure the achievement of the aims of a specific provision of this Act; and (c) must regularly review delegations issued in terms of paragraph (b) and, if necessary, amend or withdraw any of those delegations.	Accounting officer	Any other official of the municipality
79 (2)	Delegations	(2) The accounting officer may not delegate to any political structure or political office bearer of the municipality any of the powers or duties assigned to accounting officers in terms of this Act.	Accounting officer	
79 (3)	Delegations	(3) A delegation in terms of subsection (1): (a) must be in writing; (b) is subject to such limitations and conditions as the accounting officer may impose in a specific case; (c) may either be to a specific individual or to the holder of a specific post in the municipality; (d) may, in the case of a delegation to a member of the municipality's top management in terms of subsection (1) (b), authorise that member to sub-delegate the delegated power or duty to an official or the holder of a specific post in that member's area of responsibility; and (e) does not divest the accounting officer of the responsibility concerning the exercise of the delegated power or the performance of the delegated duty.	Accounting officer	
79 (4)	Delegations	(4) The accounting officer may confirm, vary or revoke any decision taken in consequence of a delegation or sub-delegation in terms of this section, but no such variation or revocation of a decision may detract from any rights that may have accrued as a result of the decision.	Accounting officer	

81 (1)	Role of the chief financial officer	(1) The chief financial officer of a municipality: (a) is administratively in charge of the budget and treasury office; (b) must advise the accounting officer on the exercise of powers and duties assigned to the accounting officer in terms of this Act; (c) must assist the accounting officer in the administration of the municipality's bank accounts and in the preparation and implementation of the municipality's budget; (d) must advise senior managers and other senior officials in the exercise of powers and duties assigned to them in terms of section **78** or delegated to them in terms of section **79**; and (e) must perform such budgeting, accounting, analysis, financial reporting, cash management, debt management, supply chain management, financial management, review and other duties as may in terms of section **79** be delegated by the accounting officer to the chief financial officer.	Accounting officer	Chief financial officer
82 (1)	Delegations	(1) The chief financial officer of a municipality may sub-delegate any of the duties referred to in section **81** (1) (b), (d) and (e): (a) to an official in the budget and treasury office; (b) to the holder of a specific post in that office; or (c) with the concurrence of the accounting officer, to (i) any other official of the municipality; or (ii) any person contracted by the municipality for the work of the office.	Chief financial officer	An official in the budget and treasury office, or. to (i) any other official of the municipality; or (ii) person contracted for the work of the office.
82 (2)	Delegations	(2) If the chief financial officer sub-delegates any duties in terms of subsection (1) to a person who is not an employee of the municipality, the chief financial officer must be satisfied that effective systems and procedures are in place to ensure control and accountability.	Chief financial officer	Person contracted by the municipality for the work of the office.
82 (3)	Delegations	(3) A sub-delegation in terms of subsection (1): (a) must be in writing; (b) is subject to such limitations or conditions as the chief financial officer may impose; and (c) does not divest that chief financial officer of the responsibility concerning the delegated duty.	Chief financial officer	
82 (4)	Delegations	(4) The chief financial officer may confirm, vary or revoke any decision taken in consequence of a sub-delegation in terms of subsection (1), but no such variation or revocation of a decision may detract from any rights that may have accrued as a result of the decision.	Chief financial officer	