KNYSNA
Municipality Munisipaliteit uMasipala

Annexure 4

MFMA Budget Circulars

No. 78 and No. 79

Medium Term

Revenue and Expenditure

Framework (MTREF)

NATIONAL TREASURY

MFMA Circular No. 78

Municipal Finance Management Act No. 56 of 2003

Municipal Budget Circular for the 2016/17 MTREF

CONTENTS

Introduction

The budget circular is compiled annually to guide municipalities on how to prepare their budget inputs. This circular focuses on the preparation of the 2016/17 Medium Term Revenue and Expenditure Framework (MTREF), reference should also be made to the previous circulars. This guidance includes national policy imperatives that should be accommodated and other relevant information. The circular provides a summary of South Africa's economic outlook, inflationary targets, financial management issues and specific reference on how to give effect to National Treasury's Municipal Budget and Reporting Regulations (MBRR). The key focus of this circular is the 2016 Local Government Elections, the demarcation process and the changes to the local government grant allocations.

1. 2016 Local Government Elections and the budget process

Local government elections are likely to be scheduled between May and August 2016; the proposed date is yet to be determined. Elections are important events – when we reaffirm our commitment to democratic and accountable government by choosing representatives of the people who will guide the work of local government for the next five years.

The following four risks need to be explicitly managed:

1. In terms of section 13 of the Municipal Property Rates Act, 2004 (Act No 6 of 2004)(MPRA) and sections 24 and 42 of the Municipal Finance Management Act, 2003 (Act No 56 of 2003)(MFMA), new tariffs for property rates, electricity, water and any other taxes and similar tariffs may only be implemented from the start of the municipal financial year (1 July). This means that the municipal council must approve the relevant tariffs before the commencement of 1 July; and, should this not happen, the municipality will not be able to increase its taxes and tariffs. Failure to obtain Council approval for the annual tariff increases would most likely cause an immediate financial crisis that may lead to the provincial executive intervening in the municipality in terms of section 139 of the Constitution;

2. In terms of section 16 of the MFMA, a municipal council must approve the annual budget for the municipality before the start of the financial year, and should a municipal council fail to do so, section 26 of the MFMA prescribes that the provincial executive **must** intervene. This provincial intervention may include dissolving the municipal council and appointing an administrator to run the municipality;

3. The outgoing council may be tempted to prepare an 'election friendly budget' – with unrealistically low tariff increases and an over-ambitious capital expenditure programme. The outcome of this approach will undoubtedly be unfunded municipal budgets that threaten their respective municipalities' financial sustainability and service delivery; and

4. Given that the timing of election campaigning coincides with the municipal public budget consultations; and there is a risk that these consultations may be neglected or used to serve the narrow interests of political parties.

In the build-up to the 2016 local government elections, municipalities are encouraged to act towards ensuring financial sustainability. Now, more than ever before, it is paramount for sound municipal decision-making so that long-term sustainability of municipal finances and service delivery is achieved beyond the election period.

Municipal finances are presently volatile and there is severe pressure to maintain healthy cash flows and maintain effective cost containment measures. It is therefore imperative that municipalities refrain from suspending credit control and debt collection efforts in a bid to win votes.

Furthermore, as the current composition and leadership of municipal councils will, for the most part, be responsible for the compilation of the 2016/17 medium-term revenue and expenditure (MTREF) budgets, councils are advised to prioritise expenditure appropriations aligned to the policy intent as described in the integrated development plans (IDPs). Infrastructure provisioning for water, sanitation, roads and electricity remain key priorities.

In addition the outgoing council is advised to critically consider the financial implications before entering into new long-term contracts that are not of priority to the municipality and avoid if possible, committing the incoming council. In addition, refrain from purchasing cars and from incurring expenditure at this stage that will financially burden the incoming council.

During this time of transition, all stakeholders should work together to ensure that municipalities continue to perform their functions efficiently and effectively. The Mayor and municipal manager should now be engaging in the process of the annual review of the fifth and last year of the IDP in terms of section 34 of the Municipal Systems Act (MSA) and the 2016/17 budget preparation process in terms of section 21 of the MFMA. It is particularly important to ensure that arrangements for the review of IDPs and preparation of budgets continue seamlessly as these processes cannot be delayed in anticipation of the announcement of an election date.

The uncertainty of the date of Election Day means that the newly elected councils may not be duly constituted by 31 May 2016 and therefore they will be unable to consider the annual budget before the start of the new municipal financial year. If the election date falls within the latter part of May 2016 and if there is any delay in declaring the election results or if the results are legally contested then it is unlikely that the new councils will be able to consider and pass the annual budget before the start of the new municipal financial year. In fact, in the case of district municipalities, there is a high probability that they will not be constituted in time to consider the annual budgets since they depend on the finalisation of the local municipality election results relevant to their respective districts. The same will apply if the election is held in June, July or August. It is for this reason that it is recommended that the outgoing council should adopt the 2016/17 MTREF budget before the start of the new financial year.

In deciding on the schedule for the 2016/17 budget process, the Mayor and municipal manager must also note that the MFMA read together with the Municipal Budget and Reporting Regulations only allows for a ‘main adjustments budget’ to be tabled after the mid-year budget and performance assessment has been tabled in council, i.e. after 1 January 2017. In addition, the permitted scope of an adjustments budget is quite limited in that taxes and tariffs may not be increased or decreased (refer to section 28(6) of the MFMA), and any additional revenues may only be appropriated to programmes and projects already budgeted for (refer to section 28 of the MFMA). Therefore the idea of the current council passing a ‘holding budget’ which the new council will change substantially through an adjustments budget soon after the start of the municipal financial year is not legally permitted.

Though an IDP is a five year strategic document of council, municipalities should note that when a new council takes office after each local government election, the norm has been that the first year of such a new council is primarily confined to implementing the last adopted IDP. Subsequent to this, it is normally in the second year of the new council where the newly elected council will adopt its new and thoroughly interrogated and consulted IDP. This process mostly leads to an overlap of the last year of outgoing council into the new council.

It is each municipal council's prerogative to decide when to approve its annual budget. However, to assist municipalities, National Treasury proposes that councils consider adopting the following approach for their 2016/17 budget process:

Outgoing council approves 2016/17 budget
1. Current Mayor prepares a budget schedule that brings the review of the IDP and the tabling of the budget forward to late February or the beginning of March 2016; 2. Community consultations on the annual budget conducted in the remainder of March and early April 2016; 3. Officials complete technical work on annual budget by mid-April 2016; 4. Current council approves annual budget and reviewed IDP before the end of April 2016; and 5. Council implements annual budget from 1 July 2016.
Benefits
• Minimises the risk of being without an approved budget at the start of the financial year; • Ensures continuity of operations; and • Safeguards the financial sustainability of the municipality by ensuring tariff increases are locked in before the start of the financial year.
Risks
• New council may not concur with the priorities set out in the annual budget approved by the outgoing council, and therefore they may be reluctant to be held accountable for the implementation thereof.
Mitigating factors
• New council should note the overlapping year of the last year of the IDP into the first year of new council; and • Note that MFMA section 28(6) does not allow for tariff increases during the financial year of implementation of the adopted budget.

2. Financial Implications of the demarcation process

According to section 21 of the Municipal Demarcation Act, 1998 (Act No 27 of 1998), the Municipal Demarcation Board (MDB) must determine municipal boundaries and may re-determine any municipal boundaries. In June 2011, the MDB began an intensive three year consultative process of reviewing municipal boundaries. This process was concluded in 2013, and resulted in 17 local municipalities being affected by major boundary redeterminations. As a result of these changes the total number of municipalities is reduced by 8 municipalities.

Following the 2013 cycle of municipal boundary redeterminations, the Minister of Cooperative Governance and Traditional Affairs (CoGTA) submitted additional proposals requesting the MDB to consider the re-configuration of boundaries of certain municipalities. These proposals were submitted to the MBD in January, February and April 2015 in terms of section 22(2) of the Act, which gives the Minister of CoGTA the right to request the MDB to consider specific boundary changes. The process of considering these applications was finalised in 2015, resulting in 32 local municipalities being affected. As a result of these changes the total number of municipalities is reduced by a further 13 municipalities.

In total there will be a net reduction of 21 municipalities resulting in a total number of 257 municipalities in the country. A list of affected municipalities is attached as Annexure B.

Implications for municipalities that are merging (if the election is held before 1 July 2015):

- The demarcation changes are only effective from the date of the local government elections, therefore each existing municipality must compile an individual budget for the 2016/17 MTREF;
- The individual budgets will be consolidated for the newly demarcated municipality after the local government elections, regardless of the new allocations that will be published in the 2016 Division of Revenue Bill;
- In order to ensure seamless consolidation of budgets after the elections, the merging municipalities are urged to start working as a team on the planning and technical processes; and
- During the period between the date of the election and the start of the new municipal financial year on 1 July 2016 the current arrangements for the payment of staff and creditors are required to be maintained.

In addition, municipalities should be aware of the role of the Change Management Committee (CMC) of overseeing joint planning between the municipalities in preparation for the consolidated budget after the local government elections.

National Treasury will provide further information on the implications of the mergers if the elections are after the start of the 2016/17 municipal financial year. This will be done in the second budget circular to be issued in March 2016. In this scenario the currently existing municipalities would continue to exist for the beginning of the 2016/17 financial year before the mergers come into effect on the date of the election. Existing councils will have to adopt budgets and municipalities will be eligible to receive a pro-rata portion of their equitable share and some grant allocations for the period prior to the new municipal boundaries coming into effect.

2.1 Support provided to municipalities

To support the newly amalgamated municipalities to undertake a smooth transition, the Municipal Demarcation Transition Grant (MDTG) was established with a time span of three years (2015/16 to 2017/18). The purpose of the grant is to subsidise the additional institutional and administrative costs arising from major boundary changes due to come into effect after the 2016 local government elections. The grant only subsidises additional administrative costs related to the mergers (such as merging and changing administrative systems and costs related to transferring staff). It does not provide for any infrastructure funding.

All affected municipalities are also being supported by provincial departments of cooperative governance. A Change Management Committee has been established for each re-demarcation, with representation from all of the affected municipalities and their respective district municipalities and the provinces. The Department of Cooperative Governance has also established a national Municipal Demarcation Transitional Committee with the aim of coordinating the various transitional measures that need to be put in place for the affected municipalities.

The 2016 DORA will set out the funding that will be provided to the affected municipalities, and these municipalities, CMCs and affected provinces must ensure that they adhere to the conditions attached to the MDTG. In particular, business plans must be timeously submitted to the Department of Cooperative Governance so as to ensure that transfers are done in accordance with the payment schedules.

2.2 Impact of demarcation changes on financial transfers to municipalities

Implications for Local Government Equitable Share (LGES) allocations
The LGES is allocated through a formula that takes account of several factors including the number of poor households and households in a municipality, their incomes and the ability of the municipality to raise its own revenue. In calculating municipalities' equitable share allocations for 2016/17 all of these indicators will be updated in line with the new municipal boundaries. The resultant changes in the affected municipalities' equitable share allocations will be implemented by National Treasury and details of the new allocations will be published in the 2016 Division of Revenue Bill.

Implications for Municipal Infrastructure Grant (MIG) allocations
The MIG is allocated through a formula in a similar manner to the LGES (the MIG formula is based on infrastructure backlogs). The MIG formula will also be updated with data reflecting the changed municipal boundaries. The resultant changes in the affected municipalities' MIG allocations will be implemented by National Treasury and details of the new allocations will be published in the 2016 Division of Revenue Bill.

Implications for other conditional grant allocations
Allocations of other conditional grants are made to municipalities by the responsible national departments, often on a project basis. Allocations for conditional grants are only made for one year and the amounts published for the outer years in the schedules of the Division of Revenue Act are published for indicative purposes only and are not guaranteed. Departments will make their allocations for the 2016/17 financial year based on the new boundaries of municipalities. For municipalities that have been merged this means that previous indicative allocations are likely to be made to the new municipality that incorporates the municipal area where a project was planned and indicative amounts were published, however there is no guarantee of this.

Preparations for each major boundary re-determination are being overseen by a Change Management Committee (CMC). These CMCs are expected to play a coordinating role and exercise oversight over the preparation of a joint budget as well as any business plans required for conditional grants. The business plans can then be approved by the new council as soon as it has been constituted.

Transfers to municipalities will be gazetted in terms of the new municipal boundaries for the 2016/17 financial year.

2.3 Implications for assets and liabilities of municipalities

The changes to municipal boundaries are published by the MECs for local government in provincial gazettes in terms of section 12 of the Municipal Structures Act, 1998 (Act No 117 of 1998)(LGMSA). Section 14 of this Act regulates the effects that changes to municipal boundaries will have on existing municipalities. It also stipulates that the section 12 notice issued by the MEC for local government must provide for:

- The disestablishment of a municipality (or part of a municipality);
- The vacation of office by councilors of the existing municipality;
- The transfer of staff from the existing municipality to the superseding municipality (this must be done in accordance with labour legislation);
- The transfer of assets, liabilities and administrative and other records from the existing municipality to the superseding municipality (creditors of the existing municipality must be paid by the new municipality); and
- The extent to which existing by-laws will still apply.

The 2016/17 municipal budget preparation must make provision for any changes contained in these section 12 notices. The outgoing Council will as a result still be responsible for the preparation and conclusion of the Annual Financial Statements and the audit process.

3. The South African economy and inflation targets

The 2015 Medium Term Budget Policy Statement notes that the global economic outlook has been weaker than anticipated. Growth in developing economies has moderated in response to lower commodity prices, subdued domestic demand and reduced capital inflows. Growth in some developed economies has offset this slowdown. The South African economy is expected to grow by 1.5 per cent in 2015, 1.7 per cent in 2016 and 2.6 per cent in 2017. Domestic inflation is lower, largely as a result of declining oil prices. However, the depreciation of the Rand and the current drought gripping many parts of the country, however, pose some risk to the inflation outlook. Furthermore the electricity supply shortages pose the largest domestic risk to growth.

Persistent high unemployment remains one of South Africa's most pressing challenges. Difficult trading conditions and low business confidence levels have limited hiring during 2015. The formal sector lost 76 000 jobs, with sharp declines in manufacturing and construction, as well as community, social and personal services.

These economic challenges will continue to pressurise municipal revenue generation and collection hence a conservative approach is advised for projecting revenue. These circumstances make it essential for municipalities to reprioritise expenditure and implement stringent cost-containment measures.

Municipalities must take the following macro-economic forecasts into consideration when preparing their 2016/17 budgets and MTREF.

Table 1: Macroeconomic performance and projections, 2014 - 2018

Fiscal year	2014/15	2015/16	2016/17	2017/18	2018/19
	Actual	Estimate		Forecast	
CPI Inflation	5.6%	5.5%	6.0%	5.8%	5.8%

Source: Medium Term Budget Policy Statement 2015

Note: the fiscal year referred to is the national fiscal year (April to March) which is more closely aligned to the municipal fiscal year (July to June) than the calendar year inflation.

4. Key focus areas for the 2016/17 budget process

4.1 Local government conditional grants and additional allocations

The purpose of the conditional grants is to deliver on national government priorities relating to service delivery. Additional funding is allocated in the form of unconditional allocations such as the equitable share and the sharing of the general fuel levy. The main purpose of the equitable share is to fund the provision of free basic services to the poor.

The *2015 Medium Term Budget Policy Statement* indicates that over the 2016 MTEF period, transfers to local government total R350.6 billion, with 59.5 per cent transferred as unconditional allocations and the rest as conditional grants. The division of available funds to local government have increased to R106.9 billion or 9.2 per cent of the national revenue for 2016/17. These funds are expected to increase to R128.4 billion by 2018/19.

Municipalities are advised to use the indicative numbers as set out in the 2015 Division of Revenue Act to compile their 2016/17 MTREF. In terms of the outer year (2018/19 financial year), it is proposed that municipalities conservatively limit funding allocations to the indicative numbers as proposed in the 2015 Division of Revenue Act for 2017/18. The DoRA is available at http://www.treasury.gov.za/legislation/acts/2015/Default.aspx

It is imperative that municipalities reflect the conditional grant allocations as per the 2016 Division of Revenue Bill once available, and plan effectively to utilise these allocations appropriately so as to avoid requesting roll-overs.

Changes to local government allocations

- The *local government equitable share* is being increased by R6 billion over the MTEF to provide some relief for the impact of increasing costs of bulk water and electricity and rapid growth in households.

- The *municipal demarcation transition grant* allocation is being increased to subsidise the additional administrative costs in respect of the re-demarcations. This includes increased allocations for demarcations approved in 2013 and allocations for demarcations approved in 2015.

- The *municipal systems improvement grant* will become an indirect grant so that it can support more strategic capacity building interventions at municipalities. The initiatives funded from this grant will be aligned to the Back-to-Basics strategy and the Department of Cooperative Governance and the National Treasury will jointly decide on the details of how this programme will work.

- The *municipal human settlements capacity grant* was introduced in 2014/15 to facilitate the development of capacity to manage human settlements programmes in anticipation of the assignment of the housing function to cities. However, there is no longer a need for this standalone grant as the assignment process was subsequently suspended indefinitely. The grant will be terminated in 2016/17. Cities will be allowed to use 3 per cent of the *urban settlements development grant* to improve their capacity with regard to the built-environment functions.

- The indirect *bucket eradication programme grant* was due to end in 2015/16 but will be extended to 2016/17 to complete the eradication of bucket sanitation systems in formal residential areas. Sanitation upgrading and bucket system eradication in informal areas will continue to be funded through the *urban settlements development grant*, *human settlements development grant* and *municipal infrastructure grant*.

Reforms to local government fiscal framework

The second phase of the collaborative review of the local government infrastructure grant system led by the National Treasury has been concluded. Several changes will be introduced over the 2016 MTEF period to streamline these grants and improve the value and sustainability of associated investments. Proposed reforms to be introduced from 2016 include:

- Enabling the use of funds for the renewal, refurbishment and rehabilitation of existing infrastructure, alongside asset management systems to plan and prioritise maintenance;

- Reforming the public transport network grant to support financially sustainable transit networks in large cities by using a formula to allocate the grant, thereby giving cities a clear financial envelope within which to plan;

- Consolidating urban grants over the MTEF to tackle challenges in the built environment;

- Rationalising grants to reduce complexity and administrative burdens. Several water and sanitation grants are being merged;

    - The *municipal water infrastructure grant*, the *water services operating subsidy grant* and the *rural households infrastructure grant* will be merged into a single grant that will be targeted at reticulation and on-site-solutions in low capacity municipalities.

- Introducing greater differentiation between urban and rural areas. Secondary cities in particular will see changes to their planning requirements.

National Treasury has initiated a process of reviewing development charges. A national draft policy framework on development charges has been developed and processes are underway to consult on the policy. The consultations will convene early next year. More detailed information on these consultation processes will be provided in due course. For more information in this regard, you can contact Ms Judy Mboweni at Judy.Mboweni@treasury.gov.za or Ms Mmachuene Mpyana at Mmachuene.Mpyana@treasury.gov.za.

4.2 Reporting indicators

The National Treasury has engaged in a process of rationalising the reporting regime for the eight metropolitan municipalities with an aim to reduce the reporting burden whilst also creating a pool of indicators that will enable government to monitor progress on the outcomes and impact of municipal spending. This process has progressed significantly with regards to the outcomes and impact indicators whilst the rationalisation of the inputs, activities and output indicators is still undergoing rigorous consultations. The metropolitan outcomes and impact indicators are linked to the Built Environment Performance Plans (BEPPs) and therefore the Integrated City Development Grant (ICDG); whereas the inputs, outputs and activities indicators are linked directly to the Service Delivery Budget Implementation Plan (SDBIP) only as it relates to the built environment. When finalised, these indicators will assist the process of standardising the SDBIP.

The functional outcomes indicators are due to be finalised for the next budget cycle whilst the work on the input and output indicators is ongoing. Over time these reforms will also be extended to non-metropolitan municipalities.

4.3 Municipal Standard Chart of Accounts (*m*SCOA)[1]

The *m*SCOA Regulations apply to all municipalities and municipal entities with effect from 1 July 2017 and only eleven months remain for preparation and implementation readiness as the 2017/18 MTREF budgets will all have to be aligned to *m*SCOA.

The implementation of *m*SCOA must be considered a business reform and it requires a significant change in municipal business processes; and it involves systems conversion and/

[1] The Minister of Finance promulgated the Municipal Regulations on a Standard Chart of Accounts in government gazette Notice No. 37577 on 22 April 2014.

or re-implementation. Further, *m*SCOA requires organisational change as it is not only a financial reform that is being introduced.

The 2016/17 tabled budget or consolidated budget must include an annexure containing the municipality's *m*SCOA project plan and progress to date.

National Treasury has a dedicated website to support municipalities with their *m*SCOA readiness efforts. The following information is available:

- The current *m*SCOA classification framework;
- The *m*SCOA Project Summary Document;
- All Municipal SCOA Circulars, providing hands-on support on how to undertake preparation and implementation;
- Integrated Consultative Forum (ICF) – documentation and presentations of the *m*SCOA piloting process; and
- The Frequently Asked Questions Database (FAQ Database) – where previously asked questions and responses can be accessed and new questions may be logged.

For more information on *m*SCOA and other benefits of the reform, visit: http://mfma.treasury.gov.za/RegulationsandGazettes/MunicipalRegulationsOnAStandardChartOfAccountsFinal/Pages/default.aspx

5. The revenue budget

National Treasury continues to encourage municipalities to keep increases in rates, tariffs and other charges at levels that reflect an appropriate balance between the interests of poor households, other customers and ensuring the financial sustainability of the municipality. For this reason municipalities ***must justify in their budget documentation all increases in excess of the 6.0 per cent*** projected inflation target in the budget narratives.

Municipalities are not maximising the revenue generation potential of their revenue base and this, together with the increasing unemployment and the decline in economic growth means that there is just not sufficient municipal own revenue to supplement the national funding sources to local government.

It is therefore necessary for municipalities to ensure that their tariffs are adequate to, at the minimum, cover the costs of bulk services and also to ensure that all properties are correctly billed for property rates and all services rendered.

5.1 Eskom bulk tariff increases

In terms of the Multi Year Price Determination (MYPD) for Eskom's tariffs approved by the National Energy Regulator of South Africa (NERSA), a tariff increase of 8 per cent has been approved for the 2016/17 financial year. However, Eskom has applied to NERSA to use tariff increases in 2016/17 to compensate for an under-recovery of R22.8 billion in 2013/14. Such an application is allowed in terms of the NERSA's methodology for calculating the MYPD. A similar Eskom application was approved by NERSA for 2015/16.

NERSA is now in the process of reviewing this application. Until a decision on Eskom's application is announced by NERSA, municipalities are advised to base their planning on the 8 per cent increase already approved by NERSA. However, municipalities should be aware that it is possible that a higher tariff increase could be approved and take this possibility into account in their planning for the 2016/17 MTREF. NERSA expects to make a decision on Eskom's application by February 2016.

Municipalities are urged to examine the cost structure of providing electricity services and to apply to NERSA for electricity tariff increases that reflect the total cost of providing the service so that they work towards achieving financial sustainability.

5.2 Water and sanitation tariff increases

Municipalities should consider the full cost of rendering the water and sanitation services when determining tariffs related to these two services. If the tariffs are low and result in the municipality not recovering their full costs, the municipality should develop a pricing strategy to phase-in the necessary tariff increases in a manner that spreads the impact on consumers over a period of time. Should this not be the case, municipalities will be required to clearly articulate the reasons and remedial actions to rectify this position in their budget document. It is expected that the tariffs will differ per municipality depending on the bulk water tariff increases charged by their respective water boards.

Municipalities are urged to design an Inclining Block Tariff (IBT) structure that is appropriate to its specific circumstances, and ensures an appropriate balance between 'low income customers' and other domestic, commercial and business customers, and the financial interests of the municipality. While considering this structure, municipalities are advised to evaluate if the IBT system will be beneficial to them depending on consumption patterns in their areas.

In light of the current drought being experienced across large parts of the country, and to mitigate the need for water tariff increases, municipalities must put in place appropriate strategies to limit water losses to acceptable levels. In this regard municipalities must ensure that water used by its own operations is charged to the relevant service, and not simply attributed to water losses.

6. Funding choices and management issues

Municipalities should carefully consider the costs associated with service delivery while keeping in mind affordability and inflation when setting revenue raising measures. Once again, approving tariffs that are far below levels representing cost of providing the services would negatively impact on the financial sustainability of municipalities.

Furthermore municipalities must consider the following when compiling their 2016/17 MTREF budgets:

- improving the effectiveness of revenue management processes and procedures; and
- pay special attention to cost containment measures by, amongst other things, controlling unnecessary spending on nice-to-have items and non-essential activities.

6.1 Employee related costs

The South African Local Government Bargaining Council recently entered into a three-year *Salary and Wage Collective Agreement* for the period 01 July 2015 to 30 June 2018. The agreement reached is as follows:

- *2015/16 Financial Year – 7 per cent*
- *2016/17 Financial Year – average CPI (Feb 2015 – Jan 2016) + 1 per cent*
- *2017/18 Financial Year – average CPI (Feb 2016 – Jan 2017) + 1 per cent*

Municipalities are advised to use this Salary and Wage Agreement preparing their 2016/17 MTREF budgets.

6.2 Remuneration of councilors

Municipalities are advised to budget for the actual costs approved in accordance with the gazette on the Remuneration of Public Office Bearers Act: Determination of Upper Limits of Salaries, Allowances and Benefits of different members of municipal councils published annually by the Department of Cooperative Governance.

6.3 Service level standards

In spite of a broad guideline on the minimum service standards having been issued with MFMA Circular No. 75, many municipalities did not incorporate the service level standards in their respective budget documentation nor submit these to National Treasury. All municipalities are again advised to formulate service level standards which must form part of their 2016/17 MTREF tabled budget documentation. The said service level standards must, together with the budgets, tabled before their respective municipal councils by no later than 31 March 2016.

It is noted that the same service level standards do not apply across all municipalities. Therefore, the hereon provided outline is intended to guide municipalities with the development of their respective service level standards. The outline can be amended to suit the requirements of individual municipalities. Municipalities are advised to also consider other guideline documents issued by other institutions available on the link indicated below.

> A framework was developed as an outline to assist municipalities in finalising their service level standards. The outline can be accessed on the link below: http://mfma.treasury.gov.za/Circulars/Documents/Forms/AllItems.aspx?RootFolder=/Circulars/Documents/Circular 75 - 2015 MTREF&FolderCTID=&View={06AB24E7-1C64-4A80-A0FA-273E6A829094}

6.4 Outcomes of the Financial Management Capability Maturity Model (FMCMM)

In prioritising the upcoming MTREF decisions, municipalities should review the detailed analysis of the results of the FMCMM assessments with the results of the 32 financial ratios that provide a holistic picture of the financial capability and sustainability of the municipality. These reports have been communicated to all municipalities and should be read in conjunction with the most recent budget reviews and feedback provided by National Treasury and Provincial Treasuries. Key aspects requiring attention should be discussed with the municipal council and management so that they can be prioritised for resource allocation and implementation.

> Comments on these assessments and any other related legislative advice on the MFMA can be submitted to the MFMA helpdesk facility at: MFMA@treasury.gov.za

6.5 Hand-over reports for the newly elected council

Each municipal manager, working together with the Chief Financial Officer (CFO) and senior managers, is encouraged to prepare a hand-over report that can be tabled at the first meeting of the newly elected council. The aim of this hand-over report is to provide the new councils important orientation information regarding the municipality, the state of its finances, service delivery and capital programme, as well as key issues that need to be addressed.

It is proposed that the hand-over report should include:

- An overview of the demographic and socio-economic characteristics of the municipality;

- An overview of the organisational structure of the municipality, with the names and numbers of senior managers;
- An overview of key municipal policies that councillors need to be aware of, and where they can obtain the full text of such policies;
- An overview of issues that still need to be addressed in relation to the municipality's turnaround strategy;
- An overview of the municipality's financial health, with specific reference to:
  - Its cash and investments, and its funding of commitments (Table A8);
  - Cash coverage of normal operations (see Supporting Table SA10);
  - Creditors outstanding for more than 30 days, along with reasons for delayed settlement;
  - Current collection levels and debtors outstanding for more than 30 days; and
  - Extent of existing loans, and associated finance and redemption payments.
- The municipality's 2014/15 audit outcome, and its strategy to address audit issues;
- An overview of the provision of basic services, including plans to address backlogs;
- An overview of the state of the municipality's assets, with particular reference to the asset management plan, and repairs and maintenance requirements;
- A list of the main infrastructure projects planned for the 2016/17 budget and MTREF;
- A list of key processes requiring council input over the next six months, e.g. revision of the IDP, approval of specific policies etc. and
- Any other information deemed to be important.

In addition to the hand-over report, each new councillor should be given the municipalities' revised IDP, the adopted 2016/17 budget (if already passed), the mid-year budget and performance assessment report for 2015/16, and the latest monthly financial statement, and the annual report for 2014/15.

Municipal managers should submit their municipality's hand-over report to the relevant provincial department responsible for local government, provincial treasuries, the Department of Co-operative Governance (DCoG) and to National Treasury.

7. Conditional Grant Transfers to Municipalities

7.1 Pledging of conditional grants

Read together with paragraph 4.5 of MFMA Circular No. 51, all conditions for the considerations of the conditional grant pledge should be aligned with the provisions of section 46 of the MFMA regarding long-term borrowing.

While pledging of conditional grants assists in accelerating capital projects, municipalities are cautioned that pledging will only be approved for projects that have gone through a proper planning process as well as meeting the criteria for pledging as per MFMA Circular No. 51.

8. The Municipal Budget and Reporting Regulations

National Treasury has released Version 2.8 of Schedule A1 (the Excel Formats). This version incorporates minor changes (see Annexure A). Therefore **ALL** municipalities **MUST** use this version for the preparation of their 2016/17 Budget and MTREF.
Download Version 2.8 of Schedule A1 by clicking HERE

The Municipal Budget and Reporting Regulations, formats and associated guides are available on National Treasury's website at: http://mfma.treasury.gov.za/RegulationsandGazettes/Pages/default.aspx

8.1 Assistance with the compilation of budgets

If municipalities require advice with the compilation of their respective budgets, specifically the budget documents or Schedule A1, they should direct their enquiries to their respective provincial treasuries or to the following National Treasury official as follows:

	Responsible NT officials	Tel. No.	Email
Eastern Cape	Templeton Phogole Matjatji Mashoeshoe	012-315 5044 012-315 6567	Templeton.Phogole@treasury.gov.za Matjatji.Mashoeshoe@treasury.gov.za
Free State	Vincent Malepa Cethekile Moshane Katlego Mabiletsa	012-315 5539 012-315 5079 012-395 6742	Vincent.Malepa@treasury.gov.za Cethekile.moshane@treasury.gov.za Katlego.Mabiletsa@treasury.gov.za
Gauteng	Kgomotso Baloyi Nomxolisi Mawulana	012-315 5866 012-315 5460	Kgomotso.Baloyi@treasury.gov.za Nomxolisi.Mawulana@treasury.gov.za
KwaZulu-Natal	Bernard Mokgabodi Johan Botha	012-315 5936 012-315 5171	Bernard.Mokgabodi@treasury.gov.za Johan.Botha@treasury.gov.za
Limpopo	Una Rautenbach Sifiso Mabaso	012-315 5700 012-315 5952	Una.Rautenbach@treasury.gov.za Sifiso.Mabaso@treasury.gov.za
Mpumalanga	Jordan Maja Anthony Moseki	012-315 5663 012-315 5174	Jordan.Maja@treasury.gov.za Anthony.Moseki@treasury.gov.za
Northern Cape	Willem Voigt Mandla Gilimani	012-315 5830 012-315 5807	Willem.Voigt@treasury.gov.za Mandla.Gilimani@treasury.gov.za
North West	Sadesh Ramjathan Makgabo Mabotja	012-315 5101 012-315 5156	Sadesh.Ramjathan@treasury.gov.za Makgabo.Mabotja@treasury.gov.za
Western Cape	Vuyo Mbunge Kevin Bell	012-315 5661 012-315 5725	Vuyo.Mbunge@treasury.gov.za Kevin.Bell@treasury.gov.za
Technical issues with Excel formats	Elsabe Rossouw	012-315 5534	lgdataqueries@treasury.gov.za

National Treasury, together with the provincial treasuries, will undertake a compliance check and, where municipalities have not provided complete budget information, the municipal budgets will be returned to the mayors and municipal managers of the affected municipalities for the necessary corrections. Municipal managers are reminded that the annual budget must be accompanied by a 'quality certificate' in accordance with the format as set out in item 31 of Schedule A in the Municipal Budget and Reporting Regulations.

The National Treasury would like to emphasise that where municipalities have not adhered to the Municipal Budget and Reporting Regulations, ***those municipalities will be required to go back to the municipal council and table a complete budget document aligned to the requirement of the Municipal Budget and Reporting Regulations.***

Municipalities with municipal entities are once again reminded to prepare consolidated budgets and in-year reports for both the parent municipality and its entity or entities in that they to produce:

- An annual budget, adjustments budget and monthly financial reports for the parent municipality in the relevant formats; and
- A consolidated annual budget, adjustments budget and monthly financial reports for the parent municipality and all its municipal entities in the relevant formats.

The A Schedule that the municipality submits to National Treasury must be a consolidated budget for the municipality (plus entities) and not the budget of the parent municipality only.

9. Budget process and submissions for the 2016/17 MTREF

9.1 Submitting budget documentation and schedules for 2016/17 MTREF

To facilitate oversight of compliance with the Municipal Budget and Reporting Regulations, accounting officers are reminded that:

- Section 22(b)(i) of the MFMA requires that ***immediately*** after an annual budget is tabled in a municipal council, it must be submitted to the National Treasury and the relevant provincial treasury in both printed and electronic formats. If the annual budget is tabled to council on 31 March 2016, the final date of submission of the electronic budget documents and corresponding electronic returns is **Friday, 01 April 2016**. The deadline for submission of hard copies including council resolution is **Friday, 8 April 2016**.
- Section 24(3) of the MFMA, read together with regulation 20(1), requires that the approved annual budget must be submitted to both National Treasury and the relevant provincial treasury ***within ten working days*** after the council has approved the annual budget. If the council only approves the annual budget on 30 June 2016, the final date for such a submission is **Thursday, 14 July 2016**, otherwise an earlier date applies.

The municipal manager must submit:

- the budget documentation as set out in Schedule A (version 2.8) of the Municipal Budget and Reporting Regulations, including the main Tables (A1 - A10) and ALL the supporting tables (SA1 – SA37) in both printed and electronic formats;
- the draft service delivery and budget implementation plan in both printed and electronic format;
- the draft integrated development plan;
- the council resolution;
- signed Quality Certificate as prescribed in the Municipal Budget and Reporting Regulations; and
- schedules D, E and F specific for the entities.

Municipalities are required to send electronic versions of documents and the A1 schedule to lgdocuments@treasury.gov.za.

If the budget documents are too large to be sent via email (exceeds 4MB) please submit to lgbigfiles@gmail.com. Any problems experienced in this regard can be addressed with Elsabe Rossouw at Elsabe.Rossouw@treasury.gov.za.

Municipalities are required to send printed submissions of their budget documents and council resolution to:

For couriered documents	***For posted documents***
Ms Linda Kruger	Ms Linda Kruger
National Treasury	National Treasury
40 Church Square	Private Bag X115
Pretoria, 0002	Pretoria, 0001

In addition to the above mentioned budget documentation, metropolitan municipalities must submit the Built Environment Performance Plan (BEPP) tabled in council on 31 March 2016 to Yasmin.coovadia@treasury.gov.za. If the BEPP documents are too large to be sent via email (exceeds 4MB) please submit to yasmin.coovadia@gmail.com or send to Yasmin Coovadia via Dropbox; any problems experienced in this regard can be addressed with

Yasmin.Coovadia@treasury.gov.za. Hard copies of the BEPP may be sent to Yasmin Coovadia, National Treasury, 3rd floor 40 Church Square, Pretoria, 0002 or Private Bag X115, Pretoria, 0001.

9.2 Budget reform returns to the Local Government Database for publication

For publication purposes, municipalities are still required to use the Budget Reform Returns to upload budget and monthly expenditure to the National Treasury Local Government Database. All returns are to be sent to lgdatabase@treasury.gov.za. Municipalities are requested to submit returns for both the draft budget and the final adopted budget. This will assist the National and provincial treasuries with the annual benchmark process.

The aligned electronic returns may be downloaded from National Treasury's website at the following link: http://mfma.treasury.gov.za/Return_Forms/Pages/default.aspx.

9.3 Publication of budgets on municipal websites

In terms of section 75 of the MFMA, all municipalities are required to publish their tabled budgets, adopted budgets, annual reports (containing audited annual financial statements) and other relevant information on the municipality's website. This will aid in promoting public accountability and good governance.

All relevant documents mentioned in this circular are available on the National Treasury website, http://mfma.treasury.gov.za/Pages/Default.aspx. Municipalities are encouraged to visit it regularly as documents are regularly added / updated on the website.

Contact

national treasury
Department: National Treasury
REPUBLIC OF SOUTH AFRICA

Post	Private Bag X115, Pretoria 0001
Phone	012 315 5009
Fax	012 395 6553
Website	http://www.treasury.gov.za/default.aspx

JH Hattingh
Chief Director: Local Government Budget Analysis
07 December 2015

Annexure A – Changes to Schedule A1 – the 'Excel formats'

As noted above, National Treasury has released Version 2.8 of Schedule A1 (the Excel Formats). It incorporates the following changes:

No.	Sheet	Amendment	Reason
1	A10	Cost of free basic services	Improve reporting of cost of free basic services provided including in informal settlements.
2	SA1	Revenue foregone	Improve reporting on revenue foregone and cost of free basic services.
3	SA9	Provision of free basic services	To provide detailed breakdown of free basic services which links to A10.

Annexure B – Municipalities affected by redeterminations

Redeterminations Finalised by the MDB in 2013 and 2015

Province	Affected Local Municipalities	Impact
Redeterminations finalised in 2013		
Gauteng	Randfontein and Westonaria	Reduction of 1 Municipality
KwaZulu - Natal	Vulamehlo and Umdoni	Reduction of 1 Municipality
	Hlabisa and The Big 5 False Bay	Reduction of 1 Municipality
	Umtshezi and Imbabazane	Reduction of 1 Municipality
	Ezingoleni and Hibiscus Coast	Reduction of 1 Municipality
	Emnambithi/Ladysmith and Indaka	Reduction of 1 Municipality
	Kwa Sani and Ingwe	Reduction of 1 Municipality
	Ntambanana, Mthonjaneni and uMhlathuze	Reduction of 1 Municipality. (Ntambanana disestablished with 8 wards. Ward s1-4 incorporated into Mthonjaneni; wards 5-8 incorporated into uMhlatuze)
Redeterminations finalised in 2015		
KwaZulu - Natal	Mooi Mpofana and Umvoti	No reduction in number of Municipalities. Portion of Mooi Mpofana (Cadham voting district) incorporated into Umvoti.
Mpumalanga	Mbombela and Umjindi	Reduction of 1 Municipality
Free State	Mangaung and Naledi	Reduction of 1 Municipality
North West	Ventersdorp and Tlokwe	Reduction of 1 Municipality
Northern Cape	Mier and //Khara Hais	Reduction of 1 Municipality
Limpopo	Mutale, Thulamela, Makhado and Musina	Reduction of 1 Municipality (Mutale disestablished. Parts of Mutale are incorporated into Thulamela and Musina. Parts of Makhado and Thulamela are incorporated to form a new municipality.)
	New Municipality	Parts of Makhado and Thulamela are incorporated to form a new municipality.
	Aganang, Blouberg, Molemole and Polokwane	Reduction of 1 Municipality. (Aganang disestablished; parts of Aganang incorporated into Blouberg, Molemole and Polokwane).
	Fetakgomo and Greater Tubatse	Reduction of 1 Municipality
	Modimolle and Mookgopong	Reduction of 1 Municipality
Eastern Cape	Gariep and Maletswai	Reduction of 1 Municipality
	Nxuba and Nonkobe	Reduction of 1 Municipality
	Inkwanca, Tsolwana and Lukanji	Reduction of 2 Municipalities (all 3 amalgamated into 1)
	Camdeboo, Baviaans and Ikwezi	Reduction of 2 Municipalities (all 3 amalgamated into 1)

Annexure C – Previous MFMA Circulars

Budget management issues dealt with in previous MFMA Circulars

Municipalities are reminded to refer to MFMA Circulars 48, 51, 54, 55, 66, 67 and 70 with regards to the following issues:

1. *Mayor's discretionary funds and similar discretionary budget allocation* – National Treasury regards allocations that are not designated for a specific purpose to be bad practice and discourage them (refer to MFMA Circular 51).
2. *Unallocated ward allocations* – National Treasury does not regard this to be a good practice, because it means that the tabled budget does not reflect which ward projects are planned for purposes of public consultation and council approval (refer to MFMA Circular 51).
3. *New office buildings* – Municipalities are required to send detailed information to National Treasury if they are contemplating building new main office buildings (refer to MFMA Circular 51).
4. *Virement policies of municipalities* – Municipalities are reminded of the principles that must be incorporated into municipal virements policies (refer to MFMA Circular 51).
5. *Providing clean water and managing waste water* – Municipalities were reminded to include a section on 'Drinking water quality and waste water management' in their budget document (refer to MFMA Circular 54).
6. *Renewal and repairs and maintenance of existing assets* – Allocations to repairs and maintenance, and the renewal of existing infrastructure must be prioritised. Municipalities must provide detailed motivations in their budget documentation if allocations do not meet the required benchmarks set out in MFMA Circular 55 and 66.
7. *Credit cards and debit cards linked to municipal bank accounts are not permitted* – On 02 August 2011 National Treasury issued a directive to all banks informing them that as from 01 September 2011 they are not allowed to issue credit cards or debit cards linked to municipal bank accounts (refer to MFMA Circular 55).
8. *Water and sanitation tariffs must be cost reflective* - refer to MFMA Circular 66.
9. *Solid waste tariffs* – refer to MFMA Circular 70.
10. *Variances between 4th Quarter section 71 results and annual financial statements* – refer to Circular 67.
11. *Additional In-Year reporting requirements* – refer to MFMA Circular 67.
12. *Appropriation statement (reconciliation: budget and in-year performance)- reference is made to circular 67.* It came to the attention of National Treasury that a number of municipalities did not include the appropriation statement as part of their 2012/13 or 2013/14 annual financial statement. In terms of the Standards of GRAP 24 on the Presentation of Budget Information in Financial Statements, municipalities are required to present their original and adjusted budgets against actual outcome in the annual financial statements. This is considered an appropriation statement and the comparison between the budget and actual performance should be a mirror image of each other as it relates to the classification and grouping of revenue and expenditure as has been the case in a national and provincial context. This statement is subject to auditing and accordingly supporting documentation would be required to substantiate the compilation of this statement.
13. *Eliminating non-priority spending* – The 2013 MTBPS emphasised the need for government to step-up its efforts to combat waste, inefficiency and corruption (refer to MFMA circular 70).
14. *Council oversight over the budget process* – refer to MFMA Circular 70.

Conditional grant issues dealt with in previous MFMA Circulars

Municipalities are reminded to refer to MFMA Circulars 48, 51, 54, 55 and 67 with regards to the following issues:

1. *Accounting treatment of conditional grants*: Municipalities are reminded that in accordance with accrual accounting principles, conditional grants should only be treated as 'transfers recognized' revenue when the grant revenue has been 'earned' by incurring expenditure in accordance with the conditions of the grant.
2. *VAT on conditional grants:* SARS has issued a specific guide to assist municipalities meeting their VAT obligations – ***VAT 419 Guide for Municipalities***. To assist municipalities accessing this guide it has been placed on the National Treasury website at: http://mfma.treasury.gov.za/Guidelines/Pages/default.aspx
3. *Interest received and reclaimed VAT in respect of conditional grants:* Municipalities are reminded that in MFMA Circular 48, National Treasury determined that:
   - Interest received on conditional grant funds must be treated as 'own revenue' and its use by the municipality is not subject to any special conditions; and
   - 'Reclaimed VAT' in respect of conditional grant expenditures must be treated as 'own revenue' and its use by the municipality is not subject to any special conditions.
4. *Appropriation of conditional grants that are rolled over* – As soon as a municipality receives written approval from National Treasury that its unspent conditional grants have been rolled-over it may proceed to spend such funds (refer to MFMA Circular 51 for other arrangements in this regard).
5. *Pledging of conditional grant transfers* – the 2015 Division of Revenue Bill contained a provision that allows municipalities to pledge their conditional grants. The end date for the pledges is extended to 2017/18. The process of application as set out in MFMA Circular 51 remains unchanged.
6. *Separate reporting for conditional grant roll-overs* – National Treasury has put in place a separate template for municipalities to report on the spending of conditional grant roll-overs. Municipalities are reminded that conditional grant funds can only be rolled-over once, so if they remain unspent in the year in which they were rolled-over they MUST revert to the National Revenue Fund.
7. *Payment schedule* – National Treasury has instituted an automated payment system of transfers to municipalities in order to ensure appropriate safety checks are put in place. Only the primary banking details verified by National Treasury will be used for effecting transfers.
8. *Conditional grant transfers/payments, the responsibilities of transferring and receiving authorities and the criteria for the rollover of conditional grants –* It is important that the transfers made to municipalities' are transparent, and properly captured in the municipalities' budgets. MFMA Circular no: 67 in this regard refers. The criterion for the rollover of conditional grants is stipulated in MFMA Circular no: 51.

MBRR issues dealt with in previous MFMA Circulars

Municipalities are reminded to refer to MFMA Circulars 48, 51, 54, 55 with regards to the following issues:

1. *Budgeting for revenue and 'revenue foregone'* – The 'realistically anticipated revenues to be collected' that must be reflected on the Budgeted Statement of Financial Performance (Tables A2, A3 and A4) must exclude 'revenue foregone'. The definition

of 'revenue foregone' and how it is distinguished from 'transfers and grants' is explained in MFMA Circular 51.

2. *Preparing and amending budget related policies* – Information on all budget related policies and any amendments to such policies must be included in the municipality's annual budget document (refer to MFMA Circular 54).
3. *2013/14 MTREF Funding Compliance Assessment* – All municipalities were required to perform the funding compliance assessment outlined in *MFMA Funding Compliance Guideline* and to include the relevant information outlined in MFMA Circular 55 in their 2015/16 budgets (refer to MFMA Circular 55).
4. *Tabling a funded budget* - It is critical that municipalities adopt and implement funded budgets as per Section 18 of the MFMA. Tables A7 and A8 which if completed correctly by the municipality, it will provide most of the information required to evaluate whether a municipality's operating and capital budgets are **funded** or not.

NATIONAL TREASURY

MFMA Circular No. 79

Municipal Finance Management Act No. 56 of 2003

Municipal Budget Circular for the 2016/17 MTREF

CONTENTS

Introduction

The budget circular is compiled annually to guide municipalities on how to prepare their budget inputs. This circular is a follow-up to the MFMA Budget Circular No.78 that focused on the preparation of the 2016/17 Medium Term Revenue and Expenditure Framework (MTREF). This guidance includes national policy imperatives that should be accommodated and other relevant information. The circular provides a summary of South Africa's economic outlook, inflationary targets, financial management issues and specific reference on how to give effect to National Treasury's Municipal Budget and Reporting Regulations (MBRR). The key focus of this circular is the impact of the date of the 2016 Local Government Elections on municipalities affected by re-demarcations and the changes to the local government grant allocations.

1. 2016 Local Government Elections and the budget process

1.1 Impact of Local Government Elections on demarcation changes

The date of the 2016 local government elections has not yet been declared, which means that it is also not yet known when the new demarcations will come into effect. The re-demarcation could take place before or after the start of the 2016/17 municipal financial year, which begins on 01 July 2016.

Allocations published in the 2016 Division of Revenue Bill are based on the new municipal boundaries because these new demarcations will be in effect for the majority of the 2016/17 municipal financial year. The following guidance was provided in the MFMA Budget Circular No. 78:

If the elections are held before 01 July 2016, merging municipalities will be expected to:

- Compile individual budgets for the 2016/17 MTREF and work as a team with other affected municipalities on the planning and technical processes in compiling the consolidated budget for the newly demarcated municipality; and
- Complete the remaining weeks of the financial year on their existing budget structures (and existing demarcations). The allocations published in the 2016 Division of Revenue Bill will then be transferred to the re-demarcated municipalities from 01 July 2016.

However, additional clauses have been added to section 38 of the 2016 Division of Revenue Bill to enable the National Treasury to gazette revised allocations if the elections take place after 01 July 2016.

If elections are held after 01 July 2016, the following is expected:

- Revised allocations to be transferred to the current 278 municipalities for the period between 01 July 2016 and the date of the elections (when the re-demarcated municipal boundaries will come into effect);
- The remaining allocations will be transferred to the re-demarcated municipalities after the elections;
- Merging municipalities to compile individual budgets for the 2016/17 MTREF and work as a team with other affected municipalities on the planning and technical processes in compiling the consolidated budget for the newly demarcated municipality; and
- Municipalities to implement the individual budgets until the new re-demarcations come into effect.

In areas affected by major re-demarcations the focus of the budget process for the 2016/17 MTREF should be on preparing the budget of the new municipalities that will come into effect on the date of the 2016 local government elections. Public consultations and decisions regarding tariffs and spending priorities should be focused on how these new institutions will be funded and deliver services. As elections must be held by mid-August (in terms of the requirements of section 24 of the Municipal Structures Act) these new municipalities will be responsible for delivering services for the majority of the 2016/17 financial year and over the rest of the medium term period. Preparation of these budget documents should be led by the Change Management Committee established to manage the implications of re-demarcations in each area.

The councils of the pre-election municipalities affected by the boundary change must jointly consider the budget for the new municipality to be established to ensure that all the issues are addressed e.g. budget related policies. The draft budget prepared by the Change Management Committee and agreed to by the pre-election councils should then be adopted by the newly elected council as soon as possible after it is constituted. If there are changes to be made, they must be considered during the 2016/17 adjustments budget or the 2017/18 MTREF.

Municipalities that will be merged or disestablished on the date of the local government elections must also prepare 2016/17 MTREF budgets for their existing municipality. If the election is held after 01 July then expenditure and the collection of revenue will be done in terms of this budget until the budget of the new council is adopted. The budgets that these municipalities prepare must be aligned to the budget for the new municipality described above.

If two municipalities are merging then the total of the transfers they budget to receive should be equal to the total allocated to the new municipality in the 2016 Division of Revenue Bill. Municipalities can use the proportion of funds allocated to each municipality in terms of the 2015 Division of Revenue Act as a guide to how to apportion 2016/17 MTEF allocations between the existing municipalities. For example, if municipality 1 and municipality 2 are merging to form municipality 3 and municipality 1 received an equitable share twice as large as municipality 2 in 2015/16, then municipality 1 should prepare a 2016/17 MTREF budget based on receiving 66.6 per cent of the equitable share allocation published for municipality 3 in the 2016 Division of Revenue Bill.

If the local government election date is after 01 July 2016, National Treasury will gazette how much will be transferred to each pre-election municipality for the period between 01 July 2016 and Election Day. In terms of the requirements and process set out in section 38 of the 2016 Division of Revenue Bill, this gazette will be issued within 2 weeks after the election date is announced or the Bill is enacted (whichever date is later).

The changes to municipal boundaries result in some significant changes to municipal allocations in 2016/17. To cushion the impact of these changes, all municipalities will receive at least 95 per cent of the equitable share formula allocation indicatively allocated to them in 2016/17 in the 2015 Division of Revenue Act. For merged municipalities, this guarantee will be based on the sum of the equitable share allocations to the previously separate municipalities. In cases where a municipality has been split, the guarantee is applied to an area's share of the former municipality's equitable share, based on its portion of the population in the former municipality.

The role of the Change Management Committee is critical in ensuring that budget policies for the newly demarcated municipalities are developed. The MECs for local government have issued provincial gazettes in terms of section 14 of the Municipal Structures Act, 1998 (Act No 117 of 1998)(LGMSA) detailing the transitional process for municipalities affected by re-demarcations.

2. The South African economy and inflation targets

The 2016 Budget Review notes that since the tabling of the Medium Term Budget Policy Statement (MTBPS) in October 2015 the global economic crisis has deepened, exposing the depth of South Africa's external vulnerabilities and the internal constraints that limit its potential for growth. Global conditions have exposed South Africa's own economic weaknesses, with projected GDP growth revised down to 0.9 per cent for 2016 improving gradually to 1.7 per cent in 2017 and 2.4 per cent in 2018.

The weaker outlook is as a result of lower commodity prices, higher borrowing costs, drought and diminished business and consumer confidence. Constrained electricity supply continues to limit growth and deter fixed investment. Exchange rate depreciation is contributing to a higher inflation outlook during 2016.

These factors are expected to ease over the medium term. An upturn in global trade and investment, improved policy certainty, recovering consumer and business confidence, and greater availability and reliability of electricity in the outer years should support stronger growth.

Job creation remains one of the most pressing concerns for the economy. Headline employment grew by 3.7 per cent in the first three quarters of 2015. According to Statistics South Africa, 19 000 jobs were created in the formal sector and 273 000 in the informal sector in the first three quarters of 2015. The unemployment rate stood at 25.5 per cent in the third quarter of 2015, with the number of South Africans categorised as long-term unemployed 5.7 per cent higher than in 2014.

Higher inflation and weaker employment growth will impact on the ability of all municipalities to generate and collect revenue on services, to keep expenditures within budgeted allocations, and to borrow to fund capital expenditure programmes at affordable rates. Therefore it is critical for municipalities to review how they conduct their business to ensure value for money is obtained in all their expenditures, that revenue administration systems are operating effectively, that borrowing programmes are realistic, and that creditors (including bulk service providers) continue to be paid timeously and in full.

Municipalities must take the following macro-economic forecasts into consideration when preparing their 2016/17 budgets and MTREF.

Table 1: Macroeconomic performance and projections, 2014/15 – 2018/19

Fiscal year	2014/15	2015/16	2016/17	2017/18	2018/19
	Actual	Estimate		Forecast	
CPI Inflation	5.6%	5.4%	6.6%	6.2%	5.9%
Real GDP growth	1.6%	0.9%	1.2%	1.9%	2.5%

Source: 2016 Budget Review

Note: the fiscal year referred to is the national fiscal year (April to March) which is more closely aligned to the municipal fiscal year (July to June) than the calendar year inflation.

3. Key focus areas for the 2016/17 budget process

3.1 Local government conditional grants and additional allocations

The purpose of the conditional grants is to deliver on national government priorities relating to service delivery. Additional funding is allocated in the form of unconditional allocations such as the equitable share and the sharing of the general fuel levy. The main purpose of the equitable share is to fund the provision of free basic services to the poor.

Over the 2016 MTEF period, R339.6 billion will be transferred directly to local government and a further R22.9 billion has been allocated to indirect grants. Direct transfers to local government over the 2016 MTEF period account for 9.1 per cent of national government's non-interest expenditure. The total spending on local government increases to 9.8 per cent of national non-interest expenditure when indirect transfers are added.

Direct transfers to local government grow at an annual average rate of 6.8 per cent over the 2016 MTEF period. Transfers to local government tabled in the 2016 MTEF have been reduced to make funding available for other government priorities. Over the MTEF period, local government allocations decrease by R967 million. Despite these reductions, total allocations to local government still grow at an annual average rate of 6.7 per cent over the MTEF period.

Municipalities are reminded that all allocations included in the budgets must correspond to the allocations listed in the Division of Revenue Bill. All the budget documentation can be located on the National Treasury website by clicking on the link below:
http://www.treasury.gov.za/documents/national%20budget/2016/

Changes to local government allocations

- The *local government equitable share* - the 2016 budget reduces the baseline allocation by R300 million, or 0.6 per cent, in 2016/17. In 2017/18 and 2018/19, R1.5 billion and R3 billion are added respectively to offset the rising costs of basic services. These amounts revise downwards the 2015 MTBPS medium-term projection of an additional R6 billion. This change is as a result of government's reprioritisation of expenditure.

- The *municipal demarcation transition grant* allocation – a total of R409.3 million has been allocated in 2016/17 and 2017/18 to fund the changes in municipal boundaries in affected municipalities.

- The *municipal systems improvement grant* has been reconfigured as an indirect grant from 2016/17 to help poorly performing municipalities with revenue collection, performance management and record keeping. Regional management support will also be provided to groups of municipalities facing common institutional weaknesses.

- A total of R350 million is added to the *bucket eradication programme grant* in 2016/17 to complete the eradication of bucket sanitation systems in formal residential areas. The *urban settlements development grant,* the *human settlements development grant* and the *municipal infrastructure grant* will continue to fund the upgrade of sanitation in informal settlements through various projects focused on improving these areas. An amount of R155 million is also reprioritised into the *regional bulk infrastructure grant*.

- There is also a small shift of funds from the *municipal infrastructure grant* to the *urban settlements development grant* to account for the absorption of Naledi Local Municipality (which receives the *municipal infrastructure grant*) into Mangaung Metropolitan Municipality (which receives the *urban settlements development grant*).

Reforms to local government infrastructure grants

The National Treasury, in collaboration with the Department of Cooperative Governance, the Department of Planning, Monitoring and Evaluation, SALGA and the FFC, has reviewed the system of local government infrastructure grants. Following an intergovernmental review of the local government infrastructure grant system, significant changes are being made to the way these grants are structured. The changes include:

- Allowing municipalities to use conditional grant funds to repair and refurbish existing infrastructure. Spending of grant funds on refurbishment should be focused on infrastructure serving the poor and does not remove the responsibility of municipalities to fund routine maintenance from the equitable share and own revenues. This will improve services and secure future revenue streams.

- Reducing the number of water and sanitation grants from four to two by merging of the previous *municipal water infrastructure grant*, the *water services operating subsidy grant* and the *rural household infrastructure grant* to create a new *water services infrastructure grant*. The regional bulk infrastructure grant is to fund large bulk-water and sanitation projects, and the water services infrastructure grant is to fund construction and refurbishment of reticulation schemes and on-site services in rural municipalities.

- A new formula to allocate the R6 billion per year set aside to upgrade public transport in 13 cities. The previous system incentivised cities to plan overly expensive systems in the hope of receiving more funding. The new formula provides greater certainty about the long-term support government will provide, and allows cities to plan affordable and sustainable infrastructure upgrades.

4. Revenue management

National Treasury continues to encourage municipalities to keep increases in property rates, tariffs for trading services and charges for other municipal own revenue sources within the parameters of the country's inflation rate. Furthermore, municipalities must adopt a tariff setting methodology that achieves an appropriate balance between the interests of poor households and other customers while ensuring financial sustainability of the municipality. Demand management is becoming increasingly necessary as the country faces water shortages and an unstable electricity supply. The approach to tariff setting should consider all these factors and strive to achieve an equitable balance.

It is anticipated that the cost of providing municipal services will grow at a faster rate than the transfers from national government. Resource scarcity will most likely increase the cost of bulk purchases in respect of water and electricity beyond the country's inflationary targets.

Furthermore, providing for free basic services in the case of poorer households must be carefully considered and, where some municipalities have opted to provide this benefit to ALL households, this may not be financially sustainable in the long-term. Where appropriate, a municipality should re-evaluate the costs and benefits of universal or targeted provision of free basic services subsidies, in order to protect their delivery to poor households in particular. At no point should the provision of these subsidies remove resources from programmes that will expand access to infrastructure services for presently un-served households.

Where municipalities do not have an adequate revenue base and where municipalities face a combination of challenges such as resource scarcity, high unemployment and slower than average economic growth, an aggressive approach to curbing non-core spending and improving operational efficiencies is strongly advised.

4.1 Tariff setting

There are several tools available and methodologies employed to determine the appropriate tariffs for water and electricity services. Municipalities may favour different approaches but the principles of tariff setting should be consistently applied.

Municipalities should consider the following practicalities when setting tariffs:

- Costs of bulk purchases and the fluctuation in the seasonal cost thereof;
- Consumption patterns to enable better demand planning and management; and
- In the event that municipalities have been under recovering costs, embark on a process to correct their tariff structures over a reasonable time period so that cost reflective tariffs are achieved.

The tariff setting process is reliant on sound baseline information such as the number of properties within the municipal area of jurisdiction, the values of these properties, the number of households identified as indigent or poor, the consumption patterns in respect of basic services and the growth patterns within the various geographic areas.

4.2 Eskom bulk tariff increases

In terms of the Multi Year Price Determination (MYPD) for Eskom's tariffs approved by the National Energy Regulator of South Africa (NERSA), a tariff increase of 9.4 per cent has been approved for the 2016/17 financial year. However NERSA has not yet approved and published guidelines on municipal electricity price increase for the 2016/17 financial year.

Municipalities are urged to examine the cost structure of providing electricity services and to apply to NERSA for electricity tariff increases that reflect the total cost of providing the service so that they work towards achieving financial sustainability.

5. Funding choices and management issues

Municipalities should carefully consider the costs associated with service delivery while keeping in mind affordability and inflation when setting revenue raising measures. Once again, approving tariffs that are far below levels representing the cost of providing the services would negatively impact on the financial sustainability of municipalities.

5.1 Employee related costs

The South African Local Government Bargaining Council recently entered into a three-year *Salary and Wage Collective Agreement* for the period 01 July 2015 to 30 June 2018. The agreement reached is as follows:

- *2015/16 Financial Year – 7 per cent*
- *2016/17 Financial Year – average CPI (Feb 2015 – Jan 2016) + 1 per cent*
- *2017/18 Financial Year – average CPI (Feb 2016 – Jan 2017) + 1 per cent*

Municipalities are advised to use this Salary and Wage Agreement preparing their 2016/17 MTREF budgets.

5.2 Remuneration of councilors

Municipalities are advised to budget for the actual costs approved in accordance with the gazette on the Remuneration of Public Office Bearers Act: Determination of Upper Limits of Salaries, Allowances and Benefits of different members of municipal councils published on 21 December 2015 by the Department of Cooperative Governance.

5.3 Cost containment measures

In the 2016 State of the Nation Address by the President, the cost containment measures announced by the Minister of Finance in 2013 were re-emphasised. It was highlighted that excessive and wasteful expenditure has been reduced, but there is still more to be done to cut wastage. In addition the President announced some new measures which include, amongst others:

- Curtailment of overseas trips and the submission of strong motivations by those requesting permission to travel i.e. the benefit to the country needs to be proved; and
- Institution of further restrictions on conferences, catering, entertainment and social functions.

The Minister of Finance announced further measures in his budget speech on 24 February 2016. The Mayors of municipalities were urged to join in eliminating wasteful expenditure in government.

The advice provided in MFMA Budget Circular (No. 58, 66, 70, 72, 74 and 75) on cost containment measures and elimination of non-priority spending is still applicable to municipalities. A separate MFMA Circular will be issued on cost containment measures. In addition National Treasury is firstly in a process of reviewing the National Treasury instruction on cost containment measures which was issued to accounting officers of departments and secondly, determining its applicability to local government. Once the process has been concluded, a Regulation on cost containment measures applicable to local government will be issued.

Municipalities were advised in MFMA Circular No. 70 to align their budgeting policies to the cost containment measures to the extent possible as approved by Cabinet in 2013. Municipalities are requested to table the cost containment measures in council and to submit evidence thereof to the National and Provincial Treasuries together with the budget documentation in terms of the MFMA.

5.4 2016/17 MTREF budget assessment

The National Treasury has continuously advised municipalities in previous budget circulars on financial management issues to be considered when compiling budgets. The 2016/17 MTREF budget assessment will critically consider the following:

- Cost reflective tariffs;
- Appropriateness of budget assumptions;
- Provision for asset renewal and maintenance;
- Credibility and level of funding of the budget (funded or not funded); and
- Alignment of the budgets to municipality's plans.

Therefore municipalities must ensure that their 2016/17 MTREF addresses the items listed above and further submit the methodology applied in setting tariffs when submitting budget documentation to the National Treasury in terms of the MFMA.

6. Conditional Grant Transfers to Municipalities

6.1 Overspending of conditional grants

Expenses incurred against conditional grants should be made in line with the allocations stated in the Division of Revenue Act (DoRA) as required by the Municipal Budget and Reporting Regulations (MBRR) in supporting tables SA 18 and 19. Municipalities must therefore adopt their annual budget in line with the allocations made in the DoRA.

In instances where municipalities overspent against their budgeted programmes, own revenue source should be used against such expenditure items. This implies that a debtor cannot be raised against the transferring national officer's future allocations.

6.2 Criteria for the rollover of conditional grant funds

The criteria published in MFMA Budget Circular No. 75 are still applicable when considering rollover requests. Municipalities must submit the required information or application to National Treasury by 31 August 2016, if not, the application will not be considered.

When considering rollover requests from municipalities, all unspent cash backed grants should be classified only as "Cash and cash equivalents". This number must also reconcile with the cash flow statements. All conditional grants must be spent in line with the conditions for which they are set for. They must not be invested.

6.3 Payment procedure on conditional grants

Conditional grants are paid in line with the approved payment schedule and are captured and authorised three days in advance. These payments include revised payment schedules, amended payment schedules, and withheld payments and rollovers credit payments.

7. The Municipal Budget and Reporting Regulations

National Treasury has released Version 2.8 of Schedule A1 (the Excel Formats). This version incorporates minor changes (see Annexure A). Therefore **ALL** municipalities **MUST** use this version for the preparation of their 2016/17 Budget and MTREF.
Download Version 2.8 of Schedule A1 by clicking HERE

> The Municipal Budget and Reporting Regulations, formats and associated guides are available on National Treasury's website at:
> http://mfma.treasury.gov.za/RegulationsandGazettes/Pages/default.aspx

7.1 Assistance with the compilation of budgets

If municipalities require advice with the compilation of their respective budgets, specifically the budget documents or Schedule A1, they should direct their enquiries to their respective provincial treasuries or to the following National Treasury official as follows:

	Responsible NT officials	**Tel. No.**	**Email**
Eastern Cape	Templeton Phogole Matjatji Mashoeshoe	012-315 5044 012-315 6567	Templeton.Phogole@treasury.gov.za Matjatji.Mashoeshoe@treasury.gov.za
Free State	Vincent Malepa Cethekile Moshane Katlego Mabiletsa	012-315 5539 012-315 5079 012-395 6742	Vincent.Malepa@treasury.gov.za Cethekile.moshane@treasury.gov.za Katlego.Mabiletsa@treasury.gov.za
Gauteng	Kgomotso Baloyi Nomxolisi Mawulana	012-315 5866 012-315 5460	Kgomotso.Baloyi@treasury.gov.za Nomxolisi.Mawulana@treasury.gov.za
KwaZulu-Natal	Bernard Mokgabodi Johan Botha	012-315 5936 012-315 5171	Bernard.Mokgabodi@treasury.gov.za Johan.Botha@treasury.gov.za
Limpopo	Una Rautenbach Sifiso Mabaso	012-315 5700 012-315 5952	Una.Rautenbach@treasury.gov.za Sifiso.Mabaso@treasury.gov.za
Mpumalanga	Jordan Maja Anthony Moseki	012-315 5663 012-315 5174	Jordan.Maja@treasury.gov.za Anthony.Moseki@treasury.gov.za
Northern Cape	Willem Voigt Mandla Gilimani	012-315 5830 012-315 5807	Willem.Voigt@treasury.gov.za Mandla.Gilimani@treasury.gov.za
North West	Sadesh Ramjathan	012-315 5101	Sadesh.Ramjathan@treasury.gov.za

	Makgabo Mabotja	012-315 5156	Makgabo.Mabotja@treasury.gov.za
Western Cape	Vuyo Mbunge Kevin Bell	012-315 5661 012-315 5725	Vuyo.Mbunge@treasury.gov.za Kevin.Bell@treasury.gov.za
Technical issues with Excel formats	Elsabe Rossouw	012-315 5534	lgdataqueries@treasury.gov.za

National Treasury, together with the provincial treasuries, will undertake a compliance check and, where municipalities have not provided complete budget information, the municipal budgets will be returned to the mayors and municipal managers of the affected municipalities for the necessary corrections. Municipal managers are reminded that the annual budget must be accompanied by a 'quality certificate' in accordance with the format as set out in item 31 of Schedule A in the Municipal Budget and Reporting Regulations.

The National Treasury needs to emphasise that where municipalities have not adhered to the Municipal Budget and Reporting Regulations, ***those municipalities will be required to go back to the municipal council and table a complete budget document aligned to the requirement of the Municipal Budget and Reporting Regulations***.

Municipalities with municipal entities are once again reminded to prepare consolidated budgets and in-year reports for both the parent municipality and its entity or entities in that they are to produce:

- An annual budget, adjustment budget and monthly financial statements for the parent municipality in the relevant formats; and
- A consolidated annual budget, adjustments budget and monthly financial statements for the parent municipality and all its municipal entities in the relevant formats.

> The A Schedule that the municipality submits to National Treasury must be a consolidated budget for the municipality (plus entities) and not the budget of the parent municipality only.

8. Budget process and submissions for the 2016/17 MTREF

8.1 Submitting budget documentation and schedules for 2016/17 MTREF

To facilitate oversight of compliance with the Municipal Budget and Reporting Regulations, accounting officers are reminded that:

- Section 22(b)(i) of the MFMA requires that ***immediately*** after an annual budget is tabled in a municipal council, it must be submitted to the National Treasury and the relevant provincial treasury in both printed and electronic formats. If the annual budget is tabled to council on 31 March 2016, the final date of submission of the electronic budget documents and corresponding electronic returns is **Friday, 01 April 2016**. The deadline for submission of hard copies including council resolution is **Friday, 8 April 2016**.
- Section 24(3) of the MFMA, read together with regulation 20(1), requires that the approved annual budget must be submitted to both National Treasury and the relevant provincial treasury ***within ten working days*** after the council has approved the annual budget. If the council only approves the annual budget on 30 June 2016, the final date for such a submission is **Thursday, 14 July 2016**, otherwise an earlier date applies.

The municipal manager must submit:

- the budget documentation as set out in Schedule A (version 2.8) of the Municipal Budget and Reporting Regulations, including the main Tables (A1 - A10) and ALL the supporting tables (SA1 – SA37) in both printed and electronic formats;
- the draft service delivery and budget implementation plan in both printed and electronic format;
- the draft integrated development plan;
- the council resolution;
- signed Quality Certificate as prescribed in the Municipal Budget and Reporting Regulations;
- **schedules D, E and F specific for the entities**;
- signed budget locking certificate as found on the website;
- service level standards; and
- *m*SCOA implementation plan and progress to date.

Municipalities are required to send electronic versions of documents and the A1 schedule to lgdocuments@treasury.gov.za.

If the budget documents are too large to be sent via email (exceeds 4MB) please submit to lgbigfiles@gmail.com. Any problems experienced in this regard can be addressed with Elsabe Rossouw at Elsabe.Rossouw@treasury.gov.za.

All new municipalities must submit the 2016/17 MTREF as soon as it is adopted by the newly elected council.

Municipalities are required to send printed submissions of their budget documents and council resolution to:

For couriered documents	***For posted documents***
Ms Linda Kruger	Ms Linda Kruger
National Treasury	National Treasury
40 Church Square	Private Bag X115
Pretoria, 0002	Pretoria, 0001

In addition to the above mentioned budget documentation, metropolitan municipalities must submit the Built Environment Performance Plan (BEPP) tabled in council on 31 May 2016 to Yasmin.coovadia@treasury.gov.za. If the BEPP documents are too large to be sent via email (exceeds 4MB) please submit to yasmin.coovadia@gmail.com or send to Yasmin Coovadia via Dropbox; any problems experienced in this regard can be addressed with Yasmin.Coovadia@treasury.gov.za. Hard copies of the BEPP may be sent to Yasmin Coovadia, National Treasury, 3rd floor 40 Church Square, Pretoria, 0002 or Private Bag X115, Pretoria, 0001.

8.2 Budget reform returns to the Local Government Database for publication

For publication purposes, municipalities are still required to use the Budget Reform Returns to upload budget and monthly expenditure to the National Treasury Local Government Database. All returns are to be sent to lgdatabase@treasury.gov.za.

Municipalities are requested to submit returns for both the draft budget and the final adopted budget.

This will assist the National and provincial treasuries with the annual benchmark process. The aligned electronic returns may be downloaded from National Treasury's website at the following link: http://mfma.treasury.gov.za/Return_Forms/Pages/default.aspx.

8.3 Municipal Standard Chart of Accounts (*m*SCOA)[1]

The *m*SCOA Regulations apply to all municipalities and municipal entities with effect from 1 July 2017 and only seven months remain for preparation and implementation readiness as the 2017/18 MTREF budgets will all have to be aligned to *m*SCOA. It is critical for municipalities to start budgeting on *m*SCOA by September 2016 to go live on 01 July 2017.

Municipalities are reminded that the current reporting requirements will remain in place until the National Treasury considers the implementation of the *m*SCOA and the new reporting reforms are no longer a risk. Those who do not adhere to the prescribed reporting according to the MBRR and the submission of the Budget reform returns to the National Treasury Local Government database will be regarded as non-compliant for publication purposes (refer to paragraph 8.2).

> Municipalities that are implementing the *m*SCOA must use the latest version of the *m*SCOA classification framework at the link below when compiling the 2016/17 MTREF.
>
> http://mfma.treasury.gov.za/RegulationsandGazettes/MunicipalRegulationsOnAStandardChartOfAccountsFinal/Pages/default.aspx

The MBRR Schedules will remain as is until further notice.

8.4 General

Municipalities use external service providers' e-mails as a result of weak or poor Information and Communication Technology (ICT). The affected municipalities are urged to use official e-mail addresses linked to the institution; therefore they must address the ICT challenges experienced.

Contact

national treasury
Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

Post	Private Bag X115, Pretoria 0001
Phone	012 315 5009
Fax	012 395 6553
Website	http://www.treasury.gov.za/default.aspx

JH Hattingh
Chief Director: Local Government Budget Analysis
07 March 2016

[1] The Minister of Finance promulgated the Municipal Regulations on a Standard Chart of Accounts in government gazette Notice No. 37577 on 22 April 2014.

Annexure A – Changes to Schedule A1 – the 'Excel formats'

As noted above, National Treasury has released Version 2.8 of Schedule A1 (the Excel Formats). It incorporates the following changes:

No.	Sheet/ Table	Amendment	Reason
1	A10	Cost of free basic services	Improve reporting of services provided including informal settlements.
2	SA1	Revenue foregone	Improve reporting on revenue foregone and cost of free basic services.
3	SA9	Provision of free basic services	To provide detailed breakdown of free basic services which links to A10.

Annexure B – Previous MFMA Circulars

Budget management issues dealt with in previous MFMA Circulars

Municipalities are reminded to refer to MFMA Circulars 48, 51, 54, 55, 66, 67 and 70 with regards to the following issues:

1. *Mayor's discretionary funds and similar discretionary budget allocation* – National Treasury regards allocations that are not designated for a specific purpose to be bad practice and discourage them (refer to MFMA Circular 51).
2. *Unallocated ward allocations* – National Treasury does not regard this to be a good practice, because it means that the tabled budget does not reflect which ward projects are planned for purposes of public consultation and council approval (refer to MFMA Circular 51).
3. *New office buildings* – Municipalities are required to send detailed information to National Treasury if they are contemplating building new main office buildings (refer to MFMA Circular 51).
4. *Virement policies of municipalities* – Municipalities are reminded of the principles that must be incorporated into municipal virements policies (refer to MFMA Circular 51).
5. *Providing clean water and managing waste water* – Municipalities were reminded to include a section on 'Drinking water quality and waste water management' in their budget document (refer to MFMA Circular 54).
6. *Renewal and repairs and maintenance of existing assets* – Allocations to repairs and maintenance, and the renewal of existing infrastructure must be prioritised. Municipalities must provide detailed motivations in their budget documentation if allocations do not meet the required benchmarks set out in MFMA Circular 55 and 66.
7. *Credit cards and debit cards linked to municipal bank accounts are not permitted* – On 02 August 2011 National Treasury issued a directive to all banks informing them that as from 01 September 2011 they are not allowed to issue credit cards or debit cards linked to municipal bank accounts (refer to MFMA Circular 55).
8. *Water and sanitation tariffs must be cost reflective* - refer to MFMA Circular 66.
9. *Solid waste tariffs* – refer to MFMA Circular 70.
10. *Variances between 4th Quarter section 71 results and annual financial statements* – refer to Circular 67.
11. *Additional In-Year reporting requirements* – refer to MFMA Circular 67.
12. *Appropriation statement (reconciliation: budget and in-year performance)- reference is made to circular 67.* It came to the attention of National Treasury that a number of municipalities did not include the appropriation statement as part of their 2012/13 or 2013/14 annual financial statement. In terms of the Standards of GRAP 24 on the Presentation of Budget Information in Financial Statements, municipalities are required to present their original and adjusted budgets against actual outcome in the annual financial statements. This is considered an appropriation statement and the comparison between the budget and actual performance should be a mirror image of each other as it relates to the classification and grouping of revenue and expenditure as has been the case in a national and provincial context. This statement is subject to auditing and accordingly supporting documentation would be required to substantiate the compilation of this statement.
13. *Eliminating non-priority spending* – The 2013 MTBPS emphasised the need for government to step-up its efforts to combat waste, inefficiency and corruption (refer to MFMA circular 70).
14. *Council oversight over the budget process* – refer to MFMA Circular 70.

Conditional grant issues dealt with in previous MFMA Circulars

Municipalities are reminded to refer to MFMA Circulars 48, 51, 54, 55 and 67 with regards to the following issues:

1. *Accounting treatment of conditional grants*: Municipalities are reminded that in accordance with accrual accounting principles, conditional grants should only be treated as 'transfers recognized' revenue when the grant revenue has been 'earned' by incurring expenditure in accordance with the conditions of the grant.
2. *VAT on conditional grants:* SARS has issued a specific guide to assist municipalities meeting their VAT obligations – ***VAT 419 Guide for Municipalities***. To assist municipalities accessing this guide it has been placed on the National Treasury website at: http://mfma.treasury.gov.za/Guidelines/Pages/default.aspx
3. *Interest received and reclaimed VAT in respect of conditional grants:* Municipalities are reminded that in MFMA Circular 48, National Treasury determined that:
    - Interest received on conditional grant funds must be treated as 'own revenue' and its use by the municipality is not subject to any special conditions; and
    - 'Reclaimed VAT' in respect of conditional grant expenditures must be treated as 'own revenue' and its use by the municipality is not subject to any special conditions.
4. *Appropriation of conditional grants that are rolled over* – As soon as a municipality receives written approval from National Treasury that its unspent conditional grants have been rolled-over it may proceed to spend such funds (refer to MFMA Circular 51 for other arrangements in this regard).
5. *Pledging of conditional grant transfers* – the 2015 Division of Revenue Bill contained a provision that allows municipalities to pledge their conditional grants. The end date for the pledges is extended to 2017/18. The process of application as set out in MFMA Circular 51 remains unchanged.
6. *Separate reporting for conditional grant roll-overs* – National Treasury has put in place a separate template for municipalities to report on the spending of conditional grant roll-overs. Municipalities are reminded that conditional grant funds can only be rolled-over once, so if they remain unspent in the year in which they were rolled-over they MUST revert to the National Revenue Fund.
7. *Payment schedule* – National Treasury has instituted an automated payment system of transfers to municipalities in order to ensure appropriate safety checks are put in place. Only the primary banking details verified by National Treasury will be used for effecting transfers.
8. *Conditional grant transfers/payments, the responsibilities of transferring and receiving authorities and the criteria for the rollover of conditional grants –* It is important that the transfers made to municipalities' are transparent, and properly captured in the municipalities' budgets. MFMA Circular no: 67 in this regard refers. The criterion for the rollover of conditional grants is stipulated in MFMA Circular no: 51.

MBRR issues dealt with in previous MFMA Circulars

Municipalities are reminded to refer to MFMA Circulars 48, 51, 54, 55 with regards to the following issues:

1. *Budgeting for revenue and 'revenue foregone'* – The 'realistically anticipated revenues to be collected' that must be reflected on the Budgeted Statement of Financial Performance (Tables A2, A3 and A4) must exclude 'revenue foregone'. The definition

of 'revenue foregone' and how it is distinguished from 'transfers and grants' is explained in MFMA Circular 51.

2. *Preparing and amending budget related policies* – Information on all budget related policies and any amendments to such policies must be included in the municipality's annual budget document (refer to MFMA Circular 54).
3. *2013/14 MTREF Funding Compliance Assessment* – All municipalities were required to perform the funding compliance assessment outlined in *MFMA Funding Compliance Guideline* and to include the relevant information outlined in MFMA Circular 55 in their 2015/16 budgets (refer to MFMA Circular 55).
4. *Tabling a funded budget* - It is critical that municipalities adopt and implement funded budgets as per Section 18 of the MFMA. Tables A7 and A8 which if completed correctly by the municipality, it will provide most of the information required to evaluate whether a municipality's operating and capital budgets are **funded** or not.

Ms Shafeeqa Davids
Fiscal Policy
Email: Shafeeqa.Davids@westerncape.gov.za
tel.: +27 21 483 9192/8454 fax: +27 21 483 7724

Reference: PTR 14/2/5

TO: THE MUNICIPAL MANAGERS
THE CHIEF FINANCIAL OFFICERS

MUNICIPAL ELECTRICITY TARIFF GUIDELINE INCREASE FOR 2016/17

Purpose

The purpose of this memorandum is to provide clarity and advice to municipalities on the municipal electricity tariff which should be applied in light of the recent NERSA Guidelines.

Background

The Energy Regulator, on an annual basis, approves a percentage guideline increase and reviews the municipal tariff benchmarks. On 10 November 2015 NERSA received Eskom's Regulatory Clearing Account (RCA) application for the first year (2013/14) of the third Multi-Year Price Determination (MYPD3) period. The Energy Regulator made its determination on Eskom's RCA on 1 March 2016. NERSA granted Eskom an average increase of 9.4 per cent to Eskom's RCA application for the first year (2013/14) of the MYPD3 control period. Furthermore, the Eskom Retail Tariff Structural Adjustment (ERTSA) application was approved on 7 March 2016, leading to a bulk increase of 7.86 per cent for municipalities. This is due to the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) ('the MFMA') time lag (the municipalities' implementation date is 1 July whereas Eskom's financial year starts on 1 April).

NERSA Calculation for the Municipal Tariff Guideline

There are certain factors that need to be taken into account in determining the expected tariff increase for electricity in the municipal space. NERSA has developed a set of assumptions regarding certain cost item increases. These assumptions are as follows:

- The bulk purchases expected increase is provided in Eskom's standard tariff submission for the upcoming financial year (7.86%)[1];
- Consumer Price Index (CPI)- 6.6%;
- salary increases – CPI plus 1%[2]; and
- Repairs and maintenance, capital charges and other costs will increase by CPI[3].

NERSA has developed a formula to determine the weighted average expected increase municipalities will incur in the provision of the service. From a sample analysis used by NERSA it was estimated that approximately 70 per cent of the municipal cost of providing electricity relates to bulk purchases. NERSA has implemented scenario 3 of their 2013 consultation paper.

NERSA, Scenario 3

Bulk purchases	**Salaries & Wages**	**Repairs and Maintenance**	**Capital Charges**	**Other Costs[4]**
70%	10%	6%	4%	10%

The formula for calculating the guideline:

MG = (B x BPI) + (S x SI) + (R x RI) + (C x CCI) + (OC x OCI)

Where:

- MG = % Municipal Guideline Increase
- B = % Bulk purchases
- BPI =% Bulk purchase increase
- S = % Salaries
- SI = % increase
- R = % Repairs
- RI = % Repairs increase
- C = % Capital charges
- CCI = % Capital charges increase
- OC = % Other costs
- OCI= % Other costs increase

1 NERSA consultation paper 7 March 2016.

2 As indicated in Circular No. 6/2012: Salary and Wage Collective Agreement.

3 NERSA consultation paper 2013.

4 Charges allocated from and to municipal departments, general expenses (costs related to the Municipal Electricity Department but not indicated on the D-forms).

Cost Item	Municipal % of Total Cost	Expected % increase	Weighted Average Increase
Bulk purchases	70%	7.86%	5.893%
Salaries	10%	7.6%	0.760%
Repairs and Maintenance	6%	6.6%	0.396%
Capital Charges	4%	6.6%	0.198%
Other Costs	10%	6.6%	0.396%
Municipal Electricity Increase			**7.64%**

Municipalities are therefore advised to apply municipal electricity tariff increases taking into account proportional cost of the above costs items in relation to the applicable weighted average increase.

In summary, the bulk tariff at which municipalities will buy electricity from Eskom is increased by 7.86 per cent and municipal guideline increase for consumers are 7.64 per cent.

Municipalities should to the extent where it is possible incorporate the above guidelines for the finalisation of the draft budgets, failing which it should be corrected prior to the adoption of the final budgets.

Kind regards

MR ML BOOYSEN
ACTING CHIEF DIRECTOR: PUBLIC POLICY SERVICES
DATE: 18 March 2016

Mr Grant Easton
Municipal Manager
Knysna Municipality
P.O. Box 21
KNYSNA
6570

Date:
15 March 2016

Enquiries:
Tel +27 44 801 2264

Dear Mr Easton

2016/17 ESKOM STANDARD TARIFF INCREASES

On 7 March 2016, the National Energy Regulator of South Africa (Nersa) approved the 2016/17 average price increase to the standard tariffs of 9.4%. The standard tariff increase of 9.4% recovers the 2016/17 multi-year price determination (MYPD3) allowed revenue plus an additional R10.257billion from the 2013/14 Regulatory Clearing Account (RCA) balance.

The RCA is a globally accepted regulatory principle that provides an MYPD3 risk mechanism to cater for changes in the previous decision. Through the RCA, Nersa may allow Eskom the recovery of variances between the MYPD decision's forecasted costs and Eskom's actual costs.

Nersa approved the 2016/17 Eskom schedule of standard tariffs with the following increases

Effective 1 April 2016, non-local authority tariff increases

9.4% for Urban and rural tariffs – all rates except the affordability subsidy charge

Homelight tariff

- 7.2% Homelight 20A Block 1 rate
- 9.0% Homelight 20A Block 2 rate

8.61% Affordability subsidy charge

As per the MYPD3 decision, to cater for affordability the Homelight 20A increases are 7.2% for Block 1 and 9.0% for Block 2.

The increase to the affordability subsidy charge is 8.61% to recover the incremental subsidy due to the lower Homelight 20A tariff increase.

Effective 1 July 2016, local authority tariff increase

7.86% for all local-authority tariffs

The local authority tariff increase of 7.86% is effective from 1 July 2016 through to 30 June 2017. During the April to June 2016 three month period, the 2015/16 local authority tariffs are applicable.

Due to the higher than 9.4% local authority revenue recovery during April to June, a lower 7.86% local authority tariff increase is applicable from 1 July 2016 to 30 June 2017.

It is important to note that the tariff increases are applied on the 2015/16 tariff rates and if a customer, on a year-on-year basis, changes the way they use electricity (time-of-use, season and volume differences), the customer's electricity cost changes may be different from the tariff increase.

For the Eskom schedule of standard prices, tariff rates and tariff analysis tools, visit the website www.eskom.co.za\tariffs .

Yours sincerely

____
Abduragmaan Jacobs
KEY CUSTOMER RELATIONS MANAGER (WESTERN CAPE OPERATING UNIT)

24th March 2016
……………………………………
Date

ANNEXURE 1

MUNICIPAL TARIFF GUIDELINE INCREASE, BENCHMARKS AND PROPOSED TIMELINES FOR MUNICIPAL TARIFF APPROVAL PROCESS FOR THE 2016/17 FINANCIAL YEAR

Consultation Paper

07 March 2016

Table of Contents

Abbreviations and Acronyms

A	Ampere
BP	Bulk Purchase
BPI	Bulk Purchase Increase
CC	Capital Charges
c/kWh	Cents per kilowatt-hour
CCI	Capital Charges Increase
CPI	Consumer Price Index
D-forms	Distribution Forms
EPT	Electricity Pricing and Tariffs
ERA	Electricity Regulation Act, 2006 (Act no.4 of 2006)
ERTSA	Eskom Retail Tariff Structural Adjustment
IBT	Inclining Block Tariff
kVA	Kilovolts-Amps
kWh	Kilowatt-hour
LF	Load Factor
MD	Maximum Demand
MFMA	Municipal Finance Management Act, 2003 (Act no.56 of 2003)
MWh	Megawatt-hour
MYPD	Multi-Year Price Determination
NERSA	National Energy Regulator of South Africa
OC	Other Costs
OCI	Other Costs Increase
R	Repairs
RCA	Regulatory Clearing Account
RI	Repairs Increase
S	Salaries
SI	Salaries Increase
TOU	Time-of-Use
V	Volt

1. EXECUTIVE SUMMARY

The National Energy Regulator (NERSA) is the regulatory authority over the energy sector in South Africa and its mandate includes the regulation of the electricity supply industry. In terms of section 4(ii) of the Electricity Regulation Act, 2006 (Act No. 4 of 2006) ('the ERA'), the Energy Regulator must regulate electricity prices and tariffs.

The Energy Regulator, on an annual basis, approves a percentage guideline increase and reviews the municipal tariff benchmarks. The guideline assists the municipalities in the preparation of their budgets and tariff adjustment applications. The benchmarks are revised and used in the evaluation of the municipal tariff applications. These benchmarks are developed per tariff category.

On 10 November 2015 NERSA received Eskom's Regulatory Clearing Account (RCA) application for the first year (2013/14) of the third Multi-Year Price Determination (MYPD3) period. The RCA is an account in which all variances in Eskom's allowed expenses are deposited. The balance in the RCA account can either be in Eskom's or the customers' favour. NERSA applies a prudency test to all the costs presented by Eskom in their application.

The Energy Regulator made its determination on Eskom's RCA on 01 March 2016. Subsequently, the determination on Eskom's Retail Tariff Structural Adjustment (ERTSA) was approved on 07 March 2016.

The municipal tariff guideline increase is developed based on Eskom's approved bulk price increase of electricity to municipalities and the increase on the municipalities' cost structures. Hence the approval of the municipal guideline increase subsequent to the determination of ERTSA. It should be noted that it is for this reason that the consultation on the guideline increase and benchmarks for the 2016/17 financial year will be taken into consideration in March/ April 2016.

The Energy Regulator is requesting the stakeholders to comment on the guideline increase, the benchmarks and the proposed timelines as set out in this consultation paper. The comments should be addressed to: **Ms Tabisa Nkopo** or **Ms Nthabiseng Mapitsing** at **The National Energy Regulator, Kulawula House, 526 Madiba Street, Arcadia, Pretoria** or emailed to: **municguideline@nersa.org.za**. The deadline for the submission of comments is 07 April 2016.

NERSA will not hold a public hearing on the key issues highlighted in the consultation paper, but will follow the notice and comment procedure in terms of Section 4 (3) of the Promotion to Administration Justice Act, 2000 (Act No. 3 of 2000). This is due to the fact that in the past, few to no presenters attended the public hearing to make representations to NERSA.

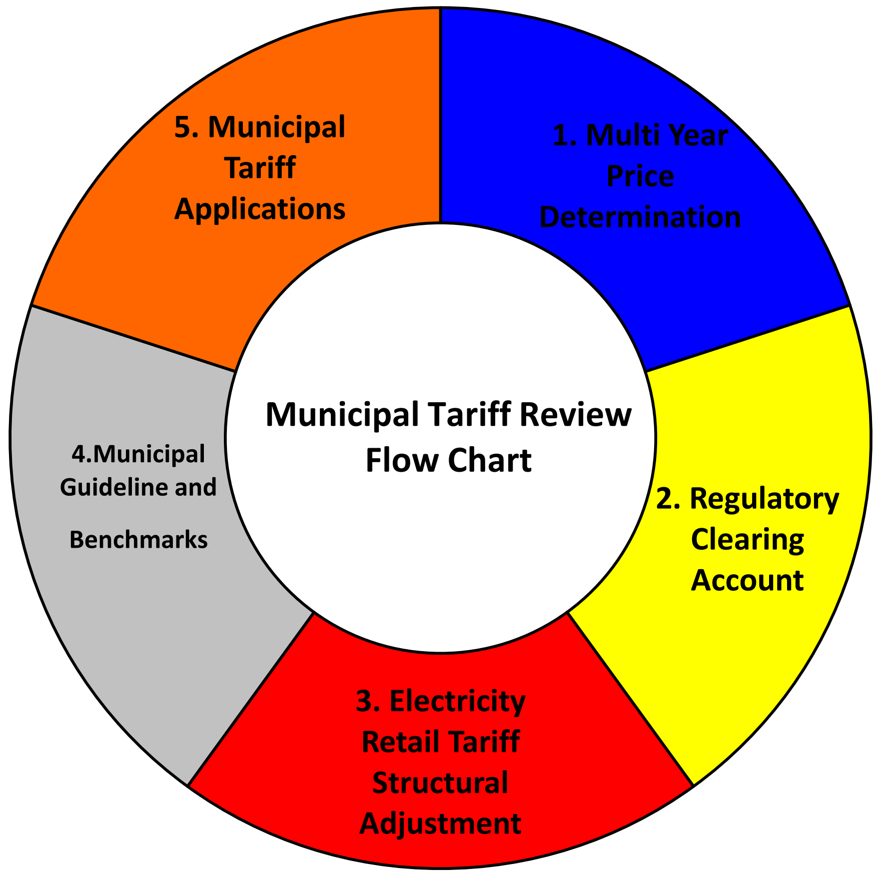
2. BACKGROUND

The consultation paper incorporates price or tariff adjustments by municipal distributors, the municipal tariff benchmarks, tariff applications and the approval processes. Eskom generates approximately 95% of the energy that is consumed in the country and the municipal distributors purchase their energy from Eskom. All municipalities are informed about the approved guideline percentage increase. This is not an automatic increase for the municipalities and private distributors. As a result, NERSA allows licensees to submit their proposed price adjustments or tariff increases annually for approval by the Energy Regulator.

Benchmarks are based on five tariff/customer categories and the corresponding average consumption levels. NERSA acknowledges that these are average consumption levels and that there may also be other tariff classes at various municipalities that will cater for other customer classes or consumption levels. Where such circumstances exist, the municipality's tariff applications will be treated on a case-by-case basis.

According to the NERSA timelines, the municipal tariff guideline and benchmarks will be approved in April 2016. Municipalities are required to submit their tariff applications to NERSA as soon as possible upon receipt of the municipal tariff guideline letter.

2.1. The municipal tariff review flow chart



2.2. Issues considered in the analysis of the municipal tariff review

NERSA approved a Cost of Supply (COS) study framework as it is a requirement of the Electricity Pricing Policy (EPP). The municipalities purchase power at the bulk supply tariff and sell it to end users at a tariff that is associated with a specific customer category. The tariff rates for customers in each tariff category are computed to reflect the cost of electricity supply to that category of customers. Therefore, municipalities are urged to perform cost of supply studies so that the revenue earned by the municipalities per tariff category is aligned with the cost to supply electricity.

The following factors, among others, will be taken into account when determining the average cost to supply:

a) bulk purchases;
b) bad debts;
c) reasonable energy losses;
d) direct and indirect charges;
e) salaries and wages; and
f) capital charges.

Furthermore, the municipalities' overall financial and technical performance will be reviewed prior to a final decision on the overall tariff increase. Indicators to be considered in this regard mainly include:

a) percentage surplus;
b) percentage energy losses;
c) percentage power costs;
d) repairs and maintenance;
e) bad debt provision; and
f) average selling price/average purchase price ratio.

2.3. Submission of D-form information

NERSA held workshops and one-on-one interactions with municipalities per province in order to assist municipalities with the completion of the Distribution forms (D-forms). This process ran parallel with the submission of the D-forms. Access to the D-form templates can be obtained through the NERSA website (www.nersa.org.za). The closing date for the submission of the D-forms is 31 October annually. Municipalities that have been contacted by NERSA regarding inaccurate or outstanding data are required to ensure that accurate information is submitted timeously to NERSA, in order to ensure that proper analysis is done and the approval of the tariff applications is achieved. The distribution forms that are primarily used for the tariff approval process are D1 (Financial information), D2 (Market information) and D3 (Human Resources information).

These forms contain information regarding the financial position, efficiency levels of the municipality, data regarding the customer's consumption patterns and the number of customers per tariff category. This information assists NERSA in the analysis of the tariffs and in determining the revenues that the municipality collects from the various tariff categories.

NERSA will not consider any municipal tariff applications without the submission of appropriate and accurate D-form information.

3. DETERMINATION OF THE MUNICIPAL TARIFF GUIDELINE

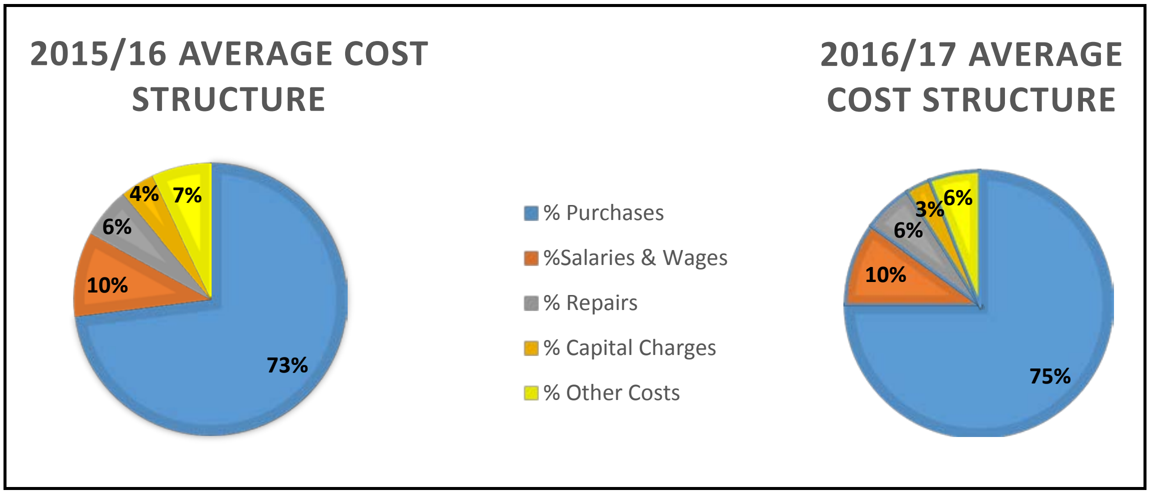
The following issues and assumptions were made when developing the percentage guideline increase for 2016/17.

On 01 March 2016 NERSA granted Eskom an average increase of 9.4% to Eskom’s RCA application for the first year (2013/14) of the MYPD3 control period. Furthermore, the ERTSA application was approved on 07 March 2016, leading to a bulk increase of 7.86% for municipalities. This is due to the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (‘the MFMA’) time lag (the municipalities' implementation date is 01 July whereas Eskom's financial year starts on 01 April).

The following issues were considered when developing the percentage guideline increase for 2016/17:

a) The 2013/14 D-form information was used to determine whether there would be changes to the municipality’s cost structures.
b) A stratified random sampling amounting to 126 D-forms was done.
c) The chosen sample would be useful in determining whether the weights of the cost drivers that have been developed need to be revised or maintained.

The pie chart below indicates the findings from the analysis done from the various sized municipalities.



The data from the computed various sized municipalities indicated a change in the weights of the cost structures. The municipal bulk purchases have increased from 73% to 75%; this increase results from Eskom's cumulative electricity prices. The average percentage for salaries and wages has been maintained at 10% in order for municipalities to incorporate the recruitment of skilled staff, additional staff and the allowance for paying scarce skills allowance. NERSA requires municipalities to spend 6% of their total ring-fenced electricity revenue on repairs and maintenance to ensure a sustainable electricity supply system. The capital charges and other costs weights decreased from 4% to 3% and 7% to 6% respectively, due to increase in the weight of bulk purchases.

Municipalities must submit their specific cost drivers should they be different from the ones presented by NERSA in the consultation paper. This will assist NERSA in considering municipalities on a case-by-case basis based on their actual cost structures.

Stakeholder Comment # 1
Stakeholders are invited to comment on the changes in the breakdown of the cost weighting that NERSA has taken into consideration when developing the guideline.

In developing the guideline, the following assumptions on cost increases were made:

a) Bulk purchases will increase by 7.86% as indicated in the Eskom standard tariff submission for the 2016/17 financial year.
b) Consumer Price Index (CPI) – 6.6%[1].
c) Salary increases – CPI plus 1%[2] .
d) Repairs and maintenance, capital charges and other costs will increase by CPI.

3.1. The formula for calculating the guideline increase:

MG = (BP x BPI) + (S x SI) + (R x RI) + (CC x CCI) + (OC x OCI)

= (75 x 0.07857) + (10 x 0.076) + (6 x 0.066) + (3 x 0.066) + (6[3] x 0.066)

= 5.893 + 0.760 + 0.396 + 0.198 + 0.396

= <u>7.64%</u>

Where:

- MG = % Municipal Guideline Increase
- BP = % Bulk purchases
- BPI =% Bulk purchase increase
- S = % Salaries
- SI = % Salaries increase
- R = % Repairs
- RI = % Repairs increase
- C = % Capital charges
- CCI = % Capital charges increase
- OC = % Other costs
- OCI= % Other costs increase

[1] As indicated in the National Treasury (Budget Review) 2016
[2] As indicated in Circular No. 31/2015: Salary and Wage Collective Agreement
[3] The 'capital charges and other costs' has been reduced due to increase in the weight of bulk purchase.

Table 3: Calculation of the guideline for the 2016/17 financial year

COST LINE ITEM	REVISED MUNIC % OF TOTAL COST	EXPECTED INCREASE %	WEIGHTED AVERAGE EXPECTED INCREASE %
Purchases	75	7.857	5.893
Salaries and wages	10	7.6	0.760
Repairs & Maintenance	6	6.6	0.396
Capital charges in total	3	6.6	0.198
Other Costs[4]	6	6.6	0.396
% increase			**7.64**

Municipalities applying for an increase that is above the guideline will have to justify their increases to the Energy Regulator and the approval will be based on the following requirements:

a) a detailed plan on the additional funds requested needs to be presented to NERSA as part of the motivation for the above-guideline increase (the municipality must provide a detailed revenue analysis whereby it indicates the revenue when using the approved guideline percentage increase versus the actual required revenue and the list of items, i.e. repairs and maintenance, where the extra funds will be allocated);
b) the approved funds must be ring-fenced to ensure that the extra funds are strictly utilised for the identified projects;
c) municipalities must report to NERSA on a six-monthly basis on how the additional funds are utilised; and
d) funds not utilised for the purpose for which they were approved will be clawed back in the following financial year.

4. THE MUNICIPAL ELECTRICITY TARIFF BENCHMARKS

4.1. The municipal electricity tariff benchmarks for the 2015/16 financial year

The existing benchmarks are based on five assumed tariff/customer categories, as set out below.

[4] Charges allocated from and to municipal departments, general expenses (costs related to the Municipal Electricity Department but not indicated on the D-forms).

4.1.1 Current benchmarks

- **Domestic (Block 1 – 4)**

Table 1: Average Domestic Benchmarks

Domestic Inclining Block Tariffs (IBTs)			
Block 1 (0 – 50 kWh) (c/kWh)	Block 2 (51 – 350 kWh) (c/kWh)	Block 3 (351 – 600 kWh) (c/kWh)	Block 4 (>600 kWh) (c/kWh)
72 – 79	**93 – 100**	**134 – 141**	**160 – 166**

The alternative domestic Inclining Block Tariff (IBT) structures and benchmarks are as indicated below.

- **Domestic Low**

Table 2: Average Domestic Low

Domestic Inclining Block Tariffs (IBTs)	
Block 1 (0 –350 kWh) (c/kWh)	Block 2 (351 – 600 kWh) (c/kWh)
91 – 96	**132 – 138**

- **Domestic High**

Table 3: Domestic High

Domestic Inclining Block Tariffs (IBTs)	
Block 1 (0 - 350 kWh) (c/kWh)	**Block 2** (351 - 600 kWh) (c/kWh)
89 – 94	**130 – 136**
Basic Charge (R/month)	

- **Domestic Non-IBT Benchmark**

Table 4: Average Domestic Non-IBT Benchmarks

Domestic Non - Inclining Block Tariffs (IBTs)	
Domestic Low 400 kWh (c/kWh)	Domestic High 800 kWh (c/kWh)
101 – 107	**126 – 131**

4.2. Commercial Benchmarks

4.2.1 Commercial Benchmarks Prepaid and Conventional Single Phase

- **Commercial Prepaid Single Phase**

Table 5: Average Benchmarks for Commercial Prepaid Single Phase

Commercial – Prepaid (2000 kWh)
c/kWh
167 – 174

- **Commercial Conventional Single Phase - Low**

Table 6: Average benchmark for Commercial Low

Commercial – Low (2000 kWh)
c/kWh
155 – 160

- **Commercial Conventional Single Phase - Medium**

Table 7: Average benchmark for Commercial Medium

Commercial – Medium (3000 kWh)
c/kWh
150 - 156

- **Commercial Conventional Single Phase - High**

Table 8: Average benchmark for Commercial High

Commercial – High (7000 kWh)
c/kWh
132 - 138

4.3.1 Commercial Benchmarks Prepaid and Conventional Three Phase

- **Commercial Prepaid Three Phase**

Table 9: Average Benchmarks for Commercial Prepaid Three-Phase

Commercial – Prepaid (5500 kWh)
c/kWh
167 – 174

- **Commercial Conventional Three Phase – Low**

Table 10: Average benchmark for Commercial Low

Commercial – Low (5500 kWh)
c/kWh
117 – 122

- **Commercial Conventional Three Phase – Medium**

Table 11: Average benchmark for Commercial Medium

Commercial-Medium (11500 kWh)
c/kWh
111 – 116

- **Commercial Conventional Three Phase – High**

Table 12: Average benchmark for Commercial High

Commercial (22000 kWh)
c/kWh
108 – 113

4.3. Agriculture Benchmarks

- **Agriculture Low**

Table 13: Average benchmark for Agriculture Low

Agriculture – Low (2000 kWh)
c/kWh
180 – 185

- **Agriculture Medium**

Table 14: Average benchmark for Agriculture Medium

Agriculture – Medium (3000 kWh)
c/kWh
171 – 176

- **Agriculture High**

Table 15: Average benchmark for Agriculture – High

Agriculture – High (7000 kWh)
c/kWh
146 – 151

4.4. Industrial Benchmark

- **Industrial Low**

Table 16: Average benchmark for Industrial – Low

Industrial – Low (43800 kWh)
c/kWh
151 – 159

- **Industrial Medium**

Table 17: Average benchmark for Industrial – Medium

Industrial – Medium (98 550 kWh)
c/kWh
148 – 154

- **Industrial High**

Table 18: Average benchmark for Industrial – High

Industrial- High (730 000 kWh)
c/kWh
134 – 139

4.4.1 Time-of-Use Benchmark

Table 19: Average benchmarks for Industrial TOU

Industrial (Based on Eskom's Nightsave) 43 800 kWh (c/kWh)	Industrial (Based on Eskom's Megaflex)) 43 800 kWh (c/kWh)
185 – 191	122 – 128

5. THE FINANCIAL BENCHMARKS

The table below indicates the weights of the financial benchmarks for the 2016/17 financial year. The municipalities that operate within these benchmarks are considered to run a sustainable and efficient electricity business.

Financial benchmarks

	Current Benchmarks	Revised Benchmarks	Financial Benchmarks (Acceptable Range)[5]
Percentage Power cost	73%	75%[6]	58% - 78%
Percentage Surplus	15%	15%[7]	10% - 20%
System losses	10%	10%[8]	5% - 12%
Average Sales Price/Average Purchase Price ratio	1:1.58	1:1.58	1:1.58 – 1:1.62
Repairs & Maintenance	Minimum of 6%		
Debt collection rate	95%		

[5] The acceptable ranges are NERSA's allowable ranges.

[6] In accordance with the municipal cost structure as indicated in the municipal tariff guideline consultation paper.

[7] The applicable financial benchmark for municipalities.

[8] The applicable technical benchmark for municipalities.

- The municipalities are encouraged to improve their debt collection rate, as this will assist them in collecting revenue that will enable them to be efficient and effective, as well as sustainable.

<u>Stakeholder Comment # 2</u>
Stakeholders are invited to comment on whether NERSA should consider other indicators when determining the efficiency of the municipality.

6. MUNICIPAL TARIFFS ABOVE THE NERSA BENCHMARKS

Municipalities applying for tariffs that are outside the approved benchmarks must justify such increases and the following information must be submitted:

- the total number of customers per tariff category – municipalities that do not have an appropriate customer base must submit the full detail of its customer profile, as well as the associated revenues;
- expected revenues per tariff category;
- the forecasted total sales;
- the average maximum demand per tariff (where applicable);
- the actual consumption; and
- the load profile in percentages (both summer and winter, where applicable).

The municipalities are encouraged to develop time-of-use tariffs in order to enable the customer to benefit from shifting their load. This will also enable municipalities to charge their customers prices that are similar to what Eskom is charging them.

7. THE PROPOSED MUNICIPAL ELECTRICITY TARIFF BENCHMARKS FOR 2016/17

7.1 The revised benchmarks

The benchmarks for the 2016/17 financial year have been developed as follows for the different tariff categories.

7.1.1 Domestic Benchmarks (Block 1 – 4)

- Block 1 – The 2015/16 benchmarks were increased by CPI[9] of 6.6%.
- Block 2 – The 2015/16 benchmarks were increased by CPI plus 1% (6.6 % + 1%[10]).
- Block 3 and 4 – The 2015/16 benchmarks were increased by the municipal tariff guideline increase of 7.64%11.

Table 20: Average Domestic Benchmarks

Domestic Inclining Block Tariffs (IBTs)			
Block 1 0-50 kWh c/kWh	Block 2 51-350 kWh c/kWh	Block 3 350-600 kWh c/kWh	Block 4 >600 kWh c/kWh
77 - 84	101 - 108	144 - 152	173 - 179

7.1.2 The alternative domestic IBT benchmarks were developed as follows:

- Domestic Low & High
  - Block 1 – The 2015/16 benchmarks were increased by 7.10%.
  - Block 2 – The 2015/16 benchmarks were increased by the municipal tariff guideline increase of 7.64%.

[9] The 6.6% is the current CPI as indicated in the Budget Review 2016.
[10] The second block has been increased by 7.10% to align it to the Eskom Homelight tariffs.
[11] The 7.64% is in accordance with the municipal tariff guideline increase for the 2016/17 financial year.

- **Domestic Low**

Table 21: Average Domestic

Domestic Inclining Block Tariffs (IBTs)	
Block 1 (0 – 350kWh) c/kWh	Block 2 (351 – 600 kWh) c/kWh
98 - 103	142 - 149

- **Domestic High**

Table 22: Average Domestic High

Domestic Inclining Block Tariffs (BTs)	
Block1 (0 -350 kWh) c/kWh	Block 2 (351 – 600 kWh) c/kWh
95 - 101	140 - 146
Basic Charge (R/month)	

7.1.3 The domestic tariffs Non-IBT

- This tariff is developed for those municipalities that are unable to implement IBTs.
- The 2015/16 domestic Non-IBT tariff benchmarks were increased by the municipal tariff guideline increase of 7.64%.

Table 23: Average Domestic Non-IBT

Domestic Inclining Block Tariffs (IBTs)	
Domestic Low (400 kWh) c/kWh	Domestic High (800 kWh) c/kWh
108 - 115	136 - 141

7.2 Commercial Benchmarks

7.2.1 Commercial Benchmarks Prepaid and Conventional Single Phase

The commercial single phase tariffs for the 2015/16 benchmark were increased by the municipal tariff guideline increase of 7.64%.

- **Commercial Prepaid Single Phase**

Table 24: Average Benchmarks for Commercial Prepaid Single

Commercial – Prepaid (2000 kWh)
c/kWh
180 - 187

- **Commercial Conventional Single Phase – Low**

Table 25: Average benchmark for Commercial

Commercial – Low (2000 kWh)
c/kWh
167 - 172

- **Commercial Conventional Single Phase - Medium**

Table 26: Average benchmark for Commercial Medium

Commercial – Medium (3000 kWh)
c/kWh
161 - 168

- **Commercial Conventional Single Phase - High**

Table 27: Average benchmark for Commercial -

Commercial - High (7000kWh)
c/kWh
142 - 149

7.2.2 Commercial Benchmarks Prepaid and Conventional Three Phase

- The commercial three-phase prepaid tariff for the 2015/16 benchmark were increased by the municipal tariff guideline increase of 7.64%.

  - **Commercial Prepaid Three-Phase**

Table 28 : Average Benchmarks for Commercial Prepaid Three-Phase

Commercial – Prepaid (5500 kWh)
c/kWh
180 - 187

- The commercial conventional three phase tariffs have been revised as comments received from municipalities indicated they were too low. The benchmark is developed by benchmarking against the 2015/16 average energy rates for municipalities.

  - **Commercial Conventional Three Phase – Low**

Table 29: Average benchmark for Commercial Three Phase – Low

Commercial - Low (5500 kWh)
c/kWh
142 - 148

  - **Commercial Conventional Three Phase – Medium**

Table 30: Average benchmark for Commercial Three Phase – Medium

Commercial - Medium (11500 kWh)
c/kWh
135 - 141

- **Commercial Conventional Three Phase – High**

Table 31: Average benchmark for Commercial High

Commercial - High (22000 kWh)
c/kWh
132 - 138

7.3 Agriculture Benchmarks

➢ The agriculture tariffs for the 2015/16 benchmarks were increased by the municipal tariff guideline increase of 7.64%.

- **Agriculture Low**

Table 32: Average benchmark for Agriculture – Low

Agriculture - Low (2000 kWh)
c/kWh
194 - 200

- **Agriculture Medium**

Table 33 : Average benchmark for Agriculture – Medium

Agriculture - Medium (3000 kWh)
c/kWh
184 - 190

- **Agriculture High**

Table 34: Average benchmark for Agriculture – High

Agriculture - High (7000 kWh)
c/kWh
157 - 163

7.4 Industrial Benchmark

- The industrial tariffs for the 2015/16 benchmarks were increased by the municipal tariff guideline increase of 7.64%.

  - **Industrial Low**

Table 35: Average benchmark for Industrial – Low

Industrial - Low (43 800 kWh)
c/kWh
163 - 171

  - **Industrial Medium**

Table 36: Average benchmark for Industrial – Medium

Industrial - Medium (98 550 kWh)
c/kWh
160 - 166

  - **Industrial High**

Table 37: Average benchmark for Industrial – High

Industrial - High (730 000kWh)
c/kWh
144 - 150

7.5 Industrial Time-of-Use

- The benchmarks for the municipalities that buy at Eskom's Megaflex tariff have been adjusted by the guideline increase of 7.64%.

Table 38: Average benchmarks for Industrial Time-Of Use (TOU) Megaflex

Industrial TOU (43 800 kWh) (Based on Eskom's Megaflex)
c/kWh
131 - 138

- The benchmarks for the municipalities that buy at Eskom's Nightsave tariff have been adjusted by the guideline increase of 7.64%.

Table 39: Average benchmarks for Industrial Time-Of Use (TOU) Nightsave

Industrial TOU (43 800 kWh) (Based on Eskom's Nightsave)
c/kWh
199 - 206

8. TIMELINES FOR MUNICIPAL TARIFF APPROVAL PROCESS AND GUIDELINE DETERMINATION

Municipalities are bound by among other legislation, the MFMA and Municipal Systems Act (MSA). According to the MFMA budgetary process, a budget circular to all municipalities is issued by National Treasury by the end of November annually. This circular takes into account NERSA's approved guideline increase.

It is anticipated that municipalities will compile and submit tariff applications for NERSA's consideration from April 2016. In line with the MFMA requirements stated below, NERSA will attempt to complete and finalise the municipal tariff approval process by 15 March 2015.

Section 43 of the MFMA states that:

(1) If a national or provincial organ of state in terms of a power contained in any national or provincial legislation determines the upper limits of a municipal tax or tariff, such determination takes effect for municipalities on a date specified in the determination.

(2) Unless the Minister on good grounds approves otherwise, the date specified in a determination referred to in subsection (1) may -

a) If the determination was promulgated on or before 15 March in a year, not be a date before 1 July in that year; or

b) If the determination was promulgated after the 15 March in a year, not be a date before 1 July in the next year.

The table below shows the timelines and processes leading to the approval of municipal electricity tariffs.

Table 40: Approval of the Municipal Tariff Guideline and Benchmarks

ACTIVITY/TASK	DATE
Modelling of municipal tariff guideline and benchmarks	Oct –Nov 15
Publishing of the municipal guideline, benchmarks and proposed timelines consultation paper on NERSA's website	08 March 16
Workshop and consultations with key stakeholders (NT, AMEU, SALGA)	March 16
Closing date for stakeholder comments	08 April 16
NERSA's decision of the municipal guideline increase, benchmarks and proposed timelines	April 16
Communicate approved guideline, benchmarks and proposed timelines to municipalities	April 16

Table 41: Municipal Tariff Review Process for the 2016/17 Financial Year

Municipalities compile and submit tariff applications for consideration by NERSA	April – May 16
NERSA's consideration and approval of tariff applications and communication of NERSA's decision to municipalities	April – Jun 16
Public Hearing[12] for above guideline increase	May – Jun 16
Consideration and approval of applications above the guideline	May – Jun 16

[12] NERSA will hold two Public Hearings for the municipalities applying for above-guideline increases.

Communicate NERSA's decision to licensees	April – Jun 16
Receipt and analysis of tariff review (appeal) applications	April – Jun 16
Consideration and approval of review applications	April – Jun 16
Communicate NERSA's decision to licensees	April – Jun 16

<u>Stakeholder Comment # 5</u>

Stakeholders are invited to comment on the appropriateness of the municipal tariff approval process and timelines with regard to the MFMA prescribed budgetary process.