UGU DISTRICT MUNICIPALITY

Policy Custodian	**Budget & Treasury Office**
Policy Name	**Funding and Reserves Policy**
Policy Number	**5/2/P**
Status **Date**	**Adopted** **2025/2026 FY**
Approved by	**Council** **C/R 11.1**
Date First Approved	**28 June 2018**
Date Last Approved	**28 May 2026**
Date for Next Review	**2026/2027 FY**

CONTENTS

PREAMBLE

1. Section 8(1) of the Municipal Budget and Reporting Regulations prescribes that a Municipality must have a Funding and Reserve Policy; and
2. Section 168(1) of the MFMA allows the Minister, acting with the concurrence of the Cabinet member responsible for local government, to make regulations or guidelines applicable to municipalities and municipal entities; and
3. The MFMA aims to modernise budget and financial management practices by placing local government finances on a sustainable footing in order to maximize the capacity of municipalities to deliver services to all residents, customers, users and investors; and
4. As the aforementioned provides for a Municipal Funding and Reserve Policy; and
5. Therefore, Ugu District Municipality Council adopts the Municipal Funding and reserve policy as set out in this document.

1. INTRODUCTION

1.1 The Funding and Reserves policy aims to ensure that the Municipality has sufficient funding in order to achieve its objectives through the implementation of its operating and capital budgets.

1.2 This Policy aims to set guidelines towards ensuring financial viability over both the short- and long-term which includes reserves requirements.

2 DEFINITIONS

In this Policy, unless the context otherwise indicates, a word or expression to which a meaning has been assigned in the Act, has the same meaning as in that Act.

‘’Accounting Officer’’ means the Municipal Manager of Ugu District Municipality

‘’Chief Financial Officer’’ means the Chief Financial Officer of Ugu District Municipality

“Council” means the Council of Ugu District Municipality

"MFMA" means the Municipal Finance Management Act, 2003 (Act No 56 of 2003)

"Municipality" means Ugu District Municipality

"GRAP" means Generally Recognised Accounting Practices standards.

3 OBJECTIVES OF THE POLICY

The objectives of this Policy are to:

3.1 Ensure that the Medium-Term Revenue/Expenditure Framework (Annual Budget) of the Municipality is appropriately funded.

3.2 Ensure that cash resources and reserves are maintained at the required levels to avoid unfunded liabilities.

3.3 To achieve financial stability in order to provide sustainable levels of service delivery to the community.

4 REGULATORY FRAMEWORK

The legislative framework governing funding of the Annual Budget is:

4.1 Local Government Municipal Finance Management Act, 2003 (Act No. 56 of 2003); and,

4.2 Local Government: Municipal Budget and Reporting Regulation, Regulation 393, published under Government Gazette 32141, 17 April 2009.

4.3 Budget Policy

4.4 Credit and Debt Collection Policy

5 FUNDING OF THE ANNUAL BUDGET

5.1 An annual budget may only be funded from:

5.1.1 Cash backed accumulated funds from previous years' surpluses and reserves not committed for any other purpose.

5.1.2 Realistically anticipated revenues to be collected.

5.1.3 Borrowed funds only for capital expenditure, and

5.1.4 Grants and subsidies.

5.2 Realistic anticipated revenue projections must take into account:

5.2.1 Projected revenue for the current year based on the previous year's billing information.

5.2.2 Actual revenue collected in previous financial years.

6 OPERATING BUDGET

6.1 The operating budget provides funding to departments for their medium-term expenditure as planned. The Municipality categorizes services rendered to the community according to its revenue generating capabilities in line with the tariffs policy.

6.1.1 Trading services – services that generate surpluses that can be used for cross subsidization to fund other services.

6.1.2 Economic services – services that break even with no surpluses.

6.1.3 Rates and general services – services that are funded by surpluses generated by trading services, and/or other revenues generated such as, interest received, grants and subsidies etc.

6.2 The operating budget is funded from the following main sources of revenue:

6.2.1 Surpluses generated from service charges.

6.2.2 Government grants and subsidies.

6.2.3 Other revenue, interest received etc.

6.2.4 Cash backed accumulated surpluses from previous years not committed for any other purposes.

6.3 The following guiding principles apply when compiling the operating budget:

6.3.1 The annual budget must be balanced and funded.

6.3.2 Growth parameters must be realistic considering the current economic conditions.

6.3.3 Tariff adjustments must be realistic, taking into consideration the general inflation, affordability, bulk increases, and the demand according to the approved Integrated Development Plan (IDP).

6.3.4 Revenue from government grants and subsidies must be in line with allocations gazette in the Division of Revenue Act and provincial gazettes.

6.3.5 Revenue from public contributions, donations or any other grants may only be included in the budget if there are acceptable documentation that guarantees the funds such as:

6.3.5.1 Signed service level agreement.

6.3.5.2 Contract or written confirmation; or

6.3.5.3 Any other legally binding document.

6.3.5.4 Projected revenue from service charges must be realistic based on current and past trends with expected growth considering the current economic conditions. The following factors must be considered for each service when applicable:

6.3.5.4.1 <u>Metered services namely water</u>:

aa) The consumption trends for the previous financial years.

bb) Envisaged water restrictions when applicable; and

cc) Actual revenue collected in previous financial years.

6.3.5.4.2 <u>Sewerage services:</u>

aa) The actual number stands/consumer points receiving the service and the consumption trends per category; and

bb) Actual revenue collected in previous financial years.

6.5.5.2.1 Rebates, exemptions or reductions for service charges are budgeted either as revenue foregone or as expenditure most often (grant) as per directive in MFMA Budget Circular 51 depending on the conditions thereof.

6.5.5.2.2 Other projected income is charged in terms of the approved sundry\ tariffs and fines considering the past trends and expected growth for each category.

6.5.5.2.3 Provision for revenue that will not be collected is made against the expenditure item bad debt and based on actual collection levels for the previous financial year and the projected annual non-payment rate.

6.5.5.2.4 Interest received from actual long-term and or short-term investments are based on the amount reasonably expected to be earned on cash amounts available during the year according to the expected interest rate trends. The actual amount allocated for interest on investments is contributed to the Capital Replacement Reserve.

6.5.5.2.5 Transfers from the accumulated surplus to fund operating expenditure will only be allowed for specific once-off projects and with no recurring operating expenditure resulting there from.

6.5.5.2.6 Transfers from the accumulated surplus to offset the increased depreciation charges as a result of the implementation of GRAP 17 will be phased out over a number of years.

6.5.5.2.7 A detailed salary budget is compiled on an annual basis. All funded positions are budgeted for in total and new and/or funded vacant positions are budgeted for six months only of the total package considering the recruitment process. As a guiding principle, the salary budget should not exceed the parameter (percentage) of the aggregate operating budget component of the annual or adjustments budget, the parameters as may be contained in the budget circular issued by National Treasury from time to time.

6.5.5.2.8 (Depreciation charges are fully budgeted for according to the asset register and to limit the impact of the implementation of GRAP 17 a transfer from the accumulated surplus is made) However the annual cash flow requirement for the repayment of borrowings must fully be taken into consideration with the setting of tariffs.

6.5.5.2.9 To ensure the health of municipal assets, sufficient provision must be made for the maintenance of existing and infrastructure assets based on affordable levels, resulting that maintenance budgets are normally lower than the recommended levels. Therefore, the mere reduction of maintenance budgets to balance annual budgets must carefully be considered. As a guiding principle, repair and maintenance should constitute between 5 and 8% of the carrying value of the property, plant and equipment and should annually be increased incrementally until the required targets are achieved.

6.5.5.2.10 Individual expenditure line items are to be revised each year when compiling the budget to ensure proper control over expenditure. Increases for these line items must be linked to the average inflation rate and macro-economic indicators unless a signed agreement or contract stipulates otherwise.

7 CAPITAL BUDGET

7.1 The capital budget provides funding for the Municipality’s capital programme based on the needs and objectives as identified by the community through the Integrated Development Plan and provides for the eradication of infrastructural backlogs, renewal and upgrading of existing infrastructure, new developments and expansion of bulk infrastructure.

7.2 Capital expenditure may only be incurred on a capital project if:

7.2.1 The funding for the project has been appropriated in the capital budget.

7.2.2 The total cost for the project has been approved by Council.

7.2.3 The future budgetary implications and projected cost covering all financial years until the project is operational has been considered.

7.2.4 The implications of the capital budget on municipal tax and tariff increases been considered.

7.2.5 The sources of funding are available and have not been committed for other purposes.

7.3 Provisions on the capital budget will be limited to availability of sources of funding and affordability. The main sources of funding for capital expenditure are:

7.3.1 Accumulated cash backed internal reserves.

7.3.2 Borrowings.

7.3.3 Government grants and subsidies; and

7.3.4 Public donations and contributions.

7.4 The following guiding principles apply when considering sources of funding for the capital budget:

7.4.1 <u>Government grants and subsidies:</u>

7.4.1.1 Only gazette allocations or transfers as reflected in the Division of Revenue Act or allocations as per provincial gazettes may be used to fund projects.

7.4.1.2 The conditions of the specific grant must be taken into consideration when allocated to a specific project; and

7.4.1.3 Government grants and subsidies allocated to specific capital projects are provided for on the relevant department’s operating budget to the extent the conditions will be met during the financial year.

7.5 In the case of public contributions, donations and/or other grants, such capital projects may only be included in the annual budget if the funding is guaranteed by means of:

7.5.1 Signed service level agreement.

7.5.2 Contract or written confirmation; and/or

7.5.3 Any other legally binding document.

7.6 Public donations, contributions and other grants are provided for on the relevant department's operating budget to the extent the conditions will be met during the financial year.

7.7 The borrowing requirements, to be used as a basis to determine the affordability of external loans over the Medium-Term Income and Expenditure Framework. The ratios to be considered to take up additional borrowings:

7.7.1 Long-term credit rating of BBB;

7.7.2 Interest cost to total expenditure to not exceed 8%;

7.7.3 Long-term debt to revenue (excluding grants) not to exceed 45%;

7.7.4 Collection rate of above 95%;

7.7.5 Percentages of capital charges to operating expenditure less than 18%.

7.8 Allocations to capital projects from cash backed internal reserves will be based on the available funding for each ring-fenced reserve according to the conditions of each reserve as follows:

7.8.1 Infrastructure projects to service new developments and the revenue is received through the sale of stands/land/site must be allocated to the capital reserve for services.

7.8.2 Capital projects of a smaller nature such as office equipment, furniture, plant and equipment etc. must be allocated to the capital reserve from revenue which is funding from the revenue budget for that specific year. A general principle is that these types of capital expenditure should not exceed more than 1% of total operating expenditure.

7.8.2.1 Capital projects to replace and/or upgrade existing assets may be allocated to the capital replacement reserve.

7.8.2.2 Capital projects to upgrade bulk services will be allocated to the capital bulk contributions reserve for each service.

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

7.9.1 Additional personnel cost to staff new facilities once operational.

7.9.2 Additional contracted services, that is, security, cleaning etc.

7.9.3 Additional general expenditure, that is, services cost, stationery, telephones, material etc.

7.9.4 Additional other capital requirements to the operate facility, that is, vehicles, plant and equipment, furniture and office equipment etc.

7.9.5 Additional costs to maintain the assets.

7.9.6 Additional interest and redemption in the case of borrowings.

7.9.7 Additional depreciation charges.

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

8 CASH FLOW MANAGEMENT

8.1 The availability of cash is the most important requirement for financial sustainability and must be closely monitored by the Chief Financial Officer. In doing so the Chief Financial Officer must ensure a minimum cash on hand to cover 90 days' operational expenditure.

8.2 Surplus cash not immediately required for operational purposes must be invested in terms of the Municipality's Cash Banking and Investment Policy to maximise the return on cash.

9 MANAGEMENT OF DEBTORS

9.1 Debt is managed in terms of the Municipal credit control and debt collection policy.

9.2 The provision for bad debts is budgeted as an expense and is based on the projected annual non-payment rate for each service.

10 DONATIONS, GRANTS AND SUBSIDIES.

10.1 Revenue from donations or any other grants may only be included in the budget.
if there is acceptable documentation that guarantees the funds such as:

10.1.1 Signed service level agreement.

10.1.2 Contract or written confirmation; or

10.1.3 Any other legally binding document.

10.2 The conditions of the specific grant must be taken into consideration when allocated to a specific project. Government grants and subsidies allocated to specific capital projects are provided for on the relevant department's operating budget to the extent that the conditions will be met during the financial year.

11 THE CAPITAL REPLACEMENT RESERVE

11.1 All reserves must be *"ring fenced"* and "*cash backed*" as internal reserves within the accumulated surplus, except for provisions as allowed by GRAP.

11.2 Once the Municipality has reached its maximum gearing ability, no further borrowings can be taken up. The Municipality must invest in a capital replacement reserve. This reserve provides internal funding for the Municipality's capital replacement and renewal program. Contributions to the capital replacement reserve through the operating budget will be:

a) Interest received on investments.

b) Proceeds from sale of assets.

12 THE INFRASTRUCTURE IMPROVEMENT

This supplements capital expenditure for the necessary expansions and upgrading of bulk infrastructure. Revenue generated from Infrastructure Improvement Fee is allocated to this reserve for each applicable service. The unspent contributions must be cash backed to ensure availability of cash when the infrastructure upgrades are required.

13 PROVISIONS

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

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

The Municipality has the following provisions:

13.1 Leave provision.

Liabilities for annual leave are recognized as they accrue to employees. An annual provision is made from the operating budget to the leave provision. Due to the fact that not all leave balances are redeemed for cash, only 75% of the leave provision is cash backed.

13.2 Long services awards

Municipal employees are awarded leave days according to years in service at year end. Due to the fact that not all long service leave balances are redeemed for cash, only 75% of the long service leave provision is cash backed.

13.3 Post-employment medical care benefits

The Municipality provides post-retirement medical care benefits by subsidizing the medical aid contributions to retired employees and their legitimate spouses. The entitlement to post-retirement medical benefits is based on employees remaining in service up to retirement age and the completion of a minimum service period. The expected cost of these benefits is accrued over a period of employment.

14 OTHER ITEMS TO BE CASH BACKED

14.1 Unspent conditional grant funding

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

14.2 Consumer Deposits

Consumer deposits are partial security for future payment. Deposits are considered a liability as the deposit is utilized once the agreement is terminated. The funds are owed to consumers and can therefore be utilized to fund the operating or capital budget. Consumer deposits should be retained in cash and be ring-fenced.

15 COMPLIANCE AND ENFORCEMENT

15.1Violation of or non-compliance with this Policy may give a just cause of disciplinary steps to be taken.

15.2 It will be the responsibility of Accounting Officer to enforce compliance with this Policy.

16 POLICY REVIEW

This Policy will be reviewed annually to ensure that it complies with changes in applicable legislation and accounting standards.

17 EFFECTIVE DATE

This Policy shall come to effect upon approval by Council of Ugu District Municipality.

18. RECORDS OF APPROVAL

Meeting	Date	Resolution
Review 2021/2022		
Policy Review Committee	20 January 2022	Recommended to MANCO
MANCO	24 January 2022	Recommended to Portfolio Committee on Finance
Portfolio Committee on Finance	03 February 2022	Recommended to EXCO
EXCO	06 March 2022	Recommended to Council
Council	26 May 2022	Approved
Review 2022/2023		
Policy Review Committee	10 February 2023	Recommended to MANCO
MANCO	24 April 2023	Recommended to Portfolio Committee on Finance
Portfolio Committee on Finance	16 May 2023	Recommended to EXCO
EXCO	17 May 2023	Recommended to Council
Council	25 May 2023	Approved
Review 2023/2024		
Policy Review Committee	14 February 2024	Recommended to MANCO
MANCO	11 March 2024	Recommended to Portfolio Committee on Finance
Portfolio Committee on Finance	20 March 2024	Recommended to Exco
EXCO	20 March 2024	Recommended to Council
Council	23 May 2024	Approved
Review 2024/2025		
Policy Review Committee	18 February 2025	Recommended to MANCO
MANCO	19 May 2025	Recommended to Finance Portfolio Committee
Joint Portfolio Committee on Finance and EXCO	26 May 2025	Recommended to Council
Council	29 May 2025	Approved

Review 2025/2026

Policy Review Committee	Policy Review Committee	Policy Review Committee
MANCO	04 May 2026	Recommended to Portfolio Committee on Finance
Portfolio Committee on Finance	12 May 2026	Recommended to Exco
EXCO	20 May 2026	Recommended to Council
Council	28 May 2026	Approved