FUNDING AND RESERVES POLICY

2025/2026

POLICY NAME	**FUNDING AND RESERVES POLICY**
Original Author(s)	FINANCIAL SERVICES
Policy status	REVIEW
Council Resolution No and Date of approval	
Signature of Speaker	
Signature of MM	

Contents

The approved amendments to this policy are intended to make certain sections clearer, provide more details for readers, users and practitioners, and show links with the budget schedules required in the terms of the Municipal Budget and Reporting Regulations that are used in the Medium Term Revenue and Expenditure (MTREF) budget report that is submitted to council for approval of the annual budget.

1. INTRODUCTION AND OBJECTIVE

The Council sets itself the objective of becoming a financially sustainable municipality with basic levels of service delivery to the entire community.

This policy aims to set standards and guide lines towards ensuring financial viability over both the short- and long term and includes funding as well as reserves requirements.

2. SECTION A: FUNDING POLICY

2.1. LEGISLATIVE REQUIREMENTS

In terms of Sections 18 and 19 of the Municipal Finance Management Act (Act No 56 of 2003) (MFMA), an annual budget may only be funded from:

- Realistically anticipated revenues to be collected;
- Cash backed accumulated funds from previous years' surpluses not committed for other purposes and
- Borrowed funds, but only for capital projects.

Furthermore, spending on a capital project may only be commenced once the funding sources have been considered, are available and have not been committed for other purposes.

In determining whether the budget is funded and in addition ensuring long term financial sustainability, the municipality will use analytical processes, including those specified by National Treasury from time to time.

2.2. STANDARD OF CARE

Each functionary in the budgeting and accounting process must do so with judgment and care that the objectives of this policy are achieved.

2.3. STATEMENT OF INTENT

The municipality will not pass a budget which is not funded or where any of the indicators as listed in this document are negative, unless acceptable reasons can be provided for non-compliance and provided that the requirements of the MFMA must at all times be adhered to.

2.4. CASH MANAGEMENT

Cash must be managed in terms of the municipality's Cash, Liability and Investment Management Policy.

2.5. LIABILITY MANAGEMENT

Debt must be managed in terms of the municipality's Cash, Liability and Investment Management Policy, together with any requirements in this policy.

2.6. FUNDING THE OPERATING BUDGET

2.6.1. INTRODUCTION

The municipality's objective is that the user of municipal resources must pay for such usage in the period in which it will occur.

The municipality recognizes the plight of the poor, and in line with national and provincial objectives, commits itself to subsidizing services to the poor. This may necessitate cross-subsidization in some tariffs to be calculated in the budget process.

2.6.2. GENERAL PRINCIPLE WHEN COMPILING THE OPERATING BUDGET

The following specific principles apply when compiling the budget:

a) The Operating Budget should be cash funded.
b) The Operating Budget is funded from the following main sources of revenue:

i) Property Rates;

ii) Service Charges;

iii) Government Grants and Subsidies; and

c) Other revenue, fines, interest received etc.

d) Growth parameters must be realistic and be based on historic patterns adjusted for current reliable information[1].

e) Tariff adjustments must be fair, taking into consideration general inflation indicators as well as the geographic region's ability to pay.

f) Within the budget, grants recognized as revenue must equal the total expected expenditure from grants inclusive of capital expenditure and VAT, as per directives given in various MFMA Circulars.

g) Revenue from public contributions, donations or any other grants may only be included in a budget (Adjustment or Original budget) if there is acceptable documentation that guarantees the funds.

h) Projected revenue from service charges must be reflected as net (i.e. all billing less revenue foregone, including free basic services, discounts and rebates).

i) Projected revenue from property rates must include all rates to be levied. All rebates and discounts must be budgeted for as revenue foregone.

j) The cash flow budget will reflect cash movements on the budgeted statement of financial position as well as cash items on the budgeted statement of financial performance.

k) Depreciation must be fully budgeted for in the operating budget.

l) A detailed salary budget is compiled on an annual basis. All funded positions are budgeted for in total as well as new and/or funded vacant positions. .

m) Individual expenditure line items are to be revised each year when compiling the budget to ensure proper control over expenditure.

[1] Refer also to the Rates Policy, Section 3. principles

2.7. FUNDING THE CAPITAL BUDGET

2.7.1. INTRODUCTION

The municipality's objective is to maintain, through proper maintenance and replacement measures, existing levels of service and to improve and implement services which are neglected or non – existent.

In order to achieve this objective, the municipality must annually, within financial means, budget for the replacement of redundant assets as well as acquiring new assets.

2.7.2. FUNDING SOURCES FOR CAPITAL EXPENDITURE

The capital budget can be funded by way of transfers and grants, public contributions and donations, borrowing and internally generated funds.

Proceeds from the sale of assets must mainly be used to fund the capital replacement reserve and infrastructure type projects.

Internally Generated Funds

The capital budget may be financed from internally generated funds such as the capital replacement reserve and surplus cash resources. The allocations of the funding sources from internally generated funds will be determined during the budget process.

Transfers and Grants (Including Public Contributions and Donations)

Grants for capital expenditure have become a common practice, especially in order to extend service delivery to previously disadvantaged areas.

While such grants are welcomed, care should be taken that the acceptance of grant funding does not place an unreasonable burden on the residents for future operating and maintenance costs which may be higher than their ability to pay.

The Accounting Officer will annually evaluate the long-term effect of capital grants on future tariffs, and if deemed necessary, report on such to Council.

Borrowings

The municipality may only raise long-term borrowings in accordance with its Cash, Liability and Investment Management Policy.

The Accounting Officer must put accounting measures in place to ensure that no unspent portions of loans are utilized for operating purposes.

For budgeting purposes any difference between proposed capital spending from loans and proposed loans raised must be included in the cash surplus for the year, i.e. any unspent borrowings at year end must be cash-backed in the 'Cash backed reserves reconciliation'.

Repaying long-term liabilities will impact directly on future tariffs that will be charged to consumers. For this reason, Council will give priority to borrowing for revenue-generating assets only. Provision for acquiring non-revenue generating assets will be made by way of utilizing other funding sources.

2.8. FUNDING COMPLIANCE MEASUREMENT

2.8.1. INTRODUCTION

The municipality must ensure that the annual budget or any subsequent adjustments budget complies with the requirements of the MFMA and this policy.
For this purpose, a set of indicators must be used as part of the budget process and be submitted with the budget. These indicators will include all indicators as recommended by National Treasury as well as any additional indicators detailed in this policy.

If any of the indicators are negative during the compilation or approval process of the budget, the budget may not be approved, unless those negative indicators can be reasonably explained and any future budget projections address the turn-around of these indictors to within acceptable levels[2].

2.8.2. CASH AND CASH EQUIVALENTS AND INVESTMENTS

A positive cash/cash equivalents position should be maintained throughout the year. In addition, the forecasted cash position at year-end must at least be the amount as calculated in the Reconciliation of Cash Requirements as determined by this policy and attached to this policy as Appendix "A"[3].

2.8.3. CASH PLUS INVESTMENTS LESS APPLICATION OF FUNDS

The overall cash position (cash/cash equivalents and investments) of the municipality must be sufficient that it can:

- Provide for the cash-backing of:

[2] Indicators may include those referred to in the following budget schedules:
SA8: Performance indicators and benchmarks
SA10: Funding measurement
[3] A surplus balance on budget schedule A8: Cash backed reserves/accumulated surplus reconciliation

- unspent conditional transfers and grants;
- unspent conditional public contributions;
- unspent borrowing;
- the cash portion of statutory funds such as the Housing Development Fund;
- VAT due to SARS;
- secured investments (whether long- or short-term);
- reserves as approved by the municipality and those portions of provisions as indicated elsewhere in this policy; and

Take into account other working capital requirements, by providing a minimum of one month's operational expenditure excluding debt impairments, depreciation and other non-cash expenses should be available for liquidity cover.

2.8.4. INDICATORS

2.8.4.1. MONTHLY AVERAGE PAYMENT COVERED BY CASH AND CASH EQUIVALENTS ("CASH COVERAGE")[4]

This indicator shows the level of risk should the municipality experience financial stress.

2.8.4.2. SURPLUS/DEFICIT EXCLUDING DEPRECIATION OFFSETS[5]

It is probable that the operating budget including depreciation charges on assets funded by grants and public contributions, as well as on revalued assets, could result in a deficit.

It is not the intention that residents be burdened with tariff increases to provide for such depreciation charges. In order to ensure a

[4] Supporting Table SA10 Funding measurement: indicator no. 3
[5] Supporting Table SA10 Funding measurement: indicator no. 4

"balanced" budget but excluding such depreciation charges, the depreciation charges maybe offset against the net surplus / deficit.

2.8.4.2 PROPERTY RATES/SERVICE CHARGE REVENUE PERCENTAGE INCREASE LESS MACRO INFLATION TARGET[6]

The intention of this indicator is to ensure that tariff increases are in line with macro-economic targets, but also to ensure that revenue increases for the expected growth in the geographic area are realistically calculated.

The formula to be used is as follows:

	DESCRIPTION	PROPERTY RATES	SERVICE CHARGES	TOTAL
A	Revenue of budget year	R XX	R XX	R XX
B	Less: Revenue of prior year	R XX	R XX	R XX
C	**=Revenue increase/decrease**	**R XX**	**R XX**	**R XX**
D	% Increase/(Decrease)	C/B %	C/B %	C/B %
E	Less: Upper limit of macro Inflation target	%	%	%
F	**=Growth in excess of inflation target**	**%**	**%**	**%**
G	Less: Expected growth %	%	%	%
H	**=Increase attributed to tariff Increase above macro inflation target**	**%**	**%**	**%**

[6] Supporting Table SA10 Funding measurement: indicator no. 5

In the event that the percentage in (h) above is greater than zero, a proper motivation must accompany the budget at submission, or the budget must be revised.

2.8.4.3. CASH COLLECTION PER CENTRATE[7]

The object of the indicator is to establish whether the projected cash to be collected is realistic and complies with section 18 of the MFMA.

The collection rate for calculating the provision for impairment of receivables must be based on past and present experience. Past experience refers to the collection rates of the prior years and present experience refers to the collection rate of the current financial year as from 1 July.

It is not permissible to project a collection rate higher than the current rate. Any improvement in collection rates during the budget year may be appropriated in an Adjustments Budget.

2.8.4.4. DEBT IMPAIRMENT EXPENSE AS A PERCENTAGE OF BILLABLE REVENUE[8]

This indicator provides information as to whether the contribution to the provision for impairment of receivables is adequate. In theory it should be equal to the difference between 100per cent and the cash collection rate, but other factors such as past performance can have an influence on it. Excessive differences should be motivated and/or explained in the MTREF budget report.

[7] Supporting Table SA10 Funding measurement: indicator no. 6
[8] Supporting Table SA10 Funding measurement: indicator no. 7

2.8.4.5. BORROWING AS A PERCENTAGE OF CAPITAL EXPENDITURE (EXCLUDING GRANTS AND CONTRIBUTIONS)[9]

This indicator provides information as to compliance with the MFMA in determining borrowing needs. The Accounting Officer must ensure compliance with the municipality's liability management.

2.8.4.6. GRANT REVENUE AS A PERCENTAGE OF GRANTS AVAILABLE[10]

The percentage attained should never be less than 100per cent and the recognition of expected unspent grants at the current year-end as revenue in the next financial year must be substantiated in a report.

2.8.4.7. CONSUMER DEBTORS CHANGE (CURRENT- AND NON-CURRENT)[11]

The object of the indicator is to determine whether budgeted reductions in outstanding debtors are realistic.

Any unacceptably high increase in either current or non–current debtors' balances should be investigated and reported.

2.8.4.8. REPAIRS AND MAINTENANCE EXPENDITURE LEVEL[12]

Property Plant and Equipment should be maintained properly at all times in order to ensure sustainable service delivery.
The budget should allocate sufficient resources to maintain assets and care should be exercised not to allow a declining maintenance

[9] Supporting Table SA10 Funding measurement: indicator no. 8
[10] Supporting Table SA10 Funding measurement: indicator no. 10
[11] Supporting Table SA10 Funding measurement: indicator no. 11 and 12
[12] Supporting Table SA10 Funding measurement: indicator no. 13

program in order to fund other less important expenditure requirements.

Similarly, if the maintenance requirements become excessive, it could indicate that a capital renewal strategy should be implemented or reviewed.

As a general benchmark the maintenance budget infrastructure assets should be 8 per cent of the asset values (write down values). Currently the ratio is below this and the benchmark should be achieved within the next ten years.

Where the budgeted amounts for repairs and maintenance reflected on Table A9 are less than 8 per cent of the asset value (write down value) of the municipality's Plant Property and Equipment (PPE) as reflected in the municipality's annual financial statements, the municipality must provide a detailed explanation and assurance that the budgeted amount is adequate to secure the ongoing health of the municipality's infrastructure supported by reference to its asset management plan or disclosure of determination of the repairs and maintenance per asset class in the MTREF budget report.[13]

Should the municipality receive an audit qualification related to its assets register, where the budgeted amounts for repairs and maintenance reflected on TableA9 are less than 10 per cent of the municipality's operating expenditure on Table A4, the municipality must provide a detailed explanation and assurance that the budgeted amount is adequate to secure the ongoing health of the municipality's infrastructure supported by reference to its asset management plan.[14]

[13]Based on MFMA Circular 55, paragraph 4.2
[14] MFMA Circular 55, paragraph 4.2

2.8.4.9. ASSET RENEWAL/REHABILITATION EXPENDITURE LEVEL[15]

This indicator supports further the indicator for repairs and maintenance.

The Accounting Officer must, as part of the capital budget, indicate whether each project is a new asset or a replacement/renewal asset in order to determine whether the renewal program is sufficient or needs revision.

Where the municipality allocates less than 40 per cent of its Capital Budget (as reflected on Table A8) to the renewal of existing assets it must provide a detailed explanation and assurance that the budgeted amount is adequate to secure the ongoing health of the municipality's infrastructure supported by reference to its asset management plan.[16]

3. SECTION B: RESERVES POLICY

3.1. INTRODUCTION

Fund accounting historically formed the major component of municipal finance in the Institute for Municipal Finance Officers (IMFO) standards.

After the change to General Recognised Accounting Practices (GRAP), fund accounting is no longer allowed.

However, the municipality recognises the importance to itself, its creditors, financiers, staff and the general public of providing for a measure of protection for future losses, as well as providing the necessary cash resources for future capital replacements and other current and non-current liabilities.

[15] Supporting Table SA10 Funding measurement: indicator no. 14
[16] MFMA Circular 55, paragraph 4.2

This policy therefore aims to provide for a measure of protection by creating certain reserves.

3.2. LEGAL REQUIREMENTS

There are no specific legal requirements for the creation of reserves, except for the Housing Development Fund. The GRAP Standards themselves do not provide for reserves.

The GRAP "Framework for the Preparation and Presentation of Financial Statements" states in paragraph 91 that such reserves may be created, but "Fund Accounting" is not allowed and any such reserves must be a "legal" reserve, i.e. created by law or Council Resolution. According to Generally Recognized Accounting Practices (GRAP), such reserves may only be created if such reserves are cash backed.

3.3. TYPES OF RESERVES

Reserves can be classified into two main categories being "cash funded reserves" and "non – cash funded reserves".

3.3.1. CASH FUNDED RESERVES

In order to provide for sufficient cash resources for future expenditure, the municipality hereby approves the establishment of the following reserves:

(a) Capital Replacement Reserve (CRR)

The CRR is to be utilized for future capital expenditure from own funds and may not be used for maintenance or other operating expenditure.

The CRR must be cash–backed and the Accounting Officer is hereby delegated to determine the contribution to the CRR during the compilation of the annual financial statements. The cash proceeds on the sale of immovable assets such as land and buildings and augmentation fees, will be transferred to the CRR in order to build resources for the acquisition of future assets.

3.3.2. NON – CASH FUNDED RESERVES

On occasion it is necessary to create non – cash funded reserves. The Accounting Officer must create any reserves prescribed by the accounting standards, such as the Revaluation Reserve and Valuation Reserve, if required.

The Accounting Officer is delegated to create reserves for future depreciation offsetting, in the absence of a standard similar to IAS 20.

3.4. ACCOUNTING FOR RESERVES

3.4.1. OTHER RESERVES

The accounting for all other reserves must be processed through the Statement of Financial Performance. The required transfer to or from the reserves must be processed in the Statement of Net Assets to or from the accumulated surplus.

It is a condition of GRAP and this policy that no transactions may be directly appropriated against these reserves.

4. SECTION C: CORPORATE GOVERNANCE (OVERSIGHT)

4.1. Compliance with the various stipulations as documented in this Funds and Reserves Policy needs to be monitored by the Chief Financial Officer and reported on to the Accounting Officer on a monthly basis and to the Finance/Audit Committee on a quarterly basis.

4.2. Where compliance has been breached the Chief Financial Officer must present an action plan to correct the non-compliance. The Finance Committee must monitor the successful implementation of the corrective action plans and report progress to Council.

5. SECTION D: TRANSITIONAL ARRANGEMENT

5.1. Upon adoption of this policy by the Council, the Accounting Officer in conjunction with the Chief Financial Officer must determine the current performance levels of the municipality against this Policy and present a plan of action towards achieving and maintaining the stipulation as set out in this policy thereby utilizing a more blended funding mix for capital infrastructure investment.

5.2. The Council must approve an appropriate timeframe within which the municipality must achieve the approved stipulations as set out in this Policy. The period between the date of the policy adoption by Council and the target date for compliance shall be known as the Transitional Period.

5.3. The Finance Committee must report progress during the approved Transitional Period to the Council.

6. SECTION E: REVIEW OF THE POLICY

This Funding and Reserves Policy is the only policy of the municipality and replaces any past policies in this regard. Any revision of this policy must be approved by Council.

This policy must be reviewed and submitted for consideration by Council on an annual basis. Such submission must be accompanied with a full description of the reasons for the change to the policy.

APPENDIX A

RECONCILIATION OF CASH REQUIREMENTS

Cash flow from operating activities	R XX
Add : Depreciation from own funds	R XX
Add : Contribution to provisions	R XX
Add : Contribution to CRR	R XX
Add : Contribution to Employee Benefits reserve	R XX
Add : Contribution to Valuation reserve	R XX
Add : Unspent conditional grants	R XX
Add : Unspent public contributions	R XX
Add : Unspent borrowings	R XX
Add : VAT due to SARS	R XX
Add : Secured investments	R XX
Add : Cash portion of Statutory Reserves	R XX
Add : Working Capital Requirements	R XX
= Minimum Cash Surplus Requirements for the year	R XX