ANNUAL BUDGET OF

KOUGA LOCAL MUNICIPALITY

2014/15 TO 2016/17

MEDIUM TERM REVENUE AND EXPENDITURE FORECASTS

Copies of this document can be viewed:

- All satellite offices and public libraries within the municipality
- At www.kouga.gov.za

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Part 1 – Annual Budget

1.1 Executive Mayor's Report

It is my privilege to table the second revised Integrated Development Plan as well as the Annual Budget for the 2014/2015 financial year and the two outer years as prescribed in terms of Section 16(2) of the Municipal Finance Management Act.

The Integrated Development Plan, which is being tabled today, is of course a vital document in relation to the municipal budgeting process as it forms the basis of the budget.

With the compilation of this budget the focus has been on service delivery. The needs were prioritised to form the basis for the budget and to match income and resource to these needs.

Endeavours have again been made to distribute the budget as equitably as possible across the various wards, but I would like to emphasise that a simple comparison from ward to ward cannot be made as certain facilities such as the water and sewage treatment plants, pump stations and electrical sub-stations service many other wards and not just those in which they are located.

Again as stated last year efficient and financial discipline will be vital to ensure the long term financial sustainability of this institution and that the scarce resources available are channelled to areas of greatest need.

Expenditure of course has to match revenue and it was not possible to include all requests or wishes that were tabled. It is therefore inevitable that there will be some disappointments.

The Total Budget amount to R652.4 million of which R33.3 million is the Capital Budget and R619 million the Operational Budget.

Our Capital Budget is mainly funded by Grants and various applications is currently at Government Departments to ensure the burden does not fall on our ratepayers when we address the upgrading of infrastructure or developing new infrastructure to unlock capacity and adequately serve our communities.

To this end we have been able to secure funding from the Department of Human Settlements to address bulk infrastructural needs to unlock housing projects. The projects for Hankey are the Augmentation of a pump station and the Waste Water Treatment Works and the construction of a Reservoir with Supply line. In Patensie the Waste Water Treatment Works and Sewerage pump station will be upgraded and a new reservoir and bulk water supply line will be constructed. In Jeffreys Bay the Sewage pump station for both Apiesdraai and Pellsrus will be upgraded with the construction of a new Reservoir with Supply line.

We have successfully also secured funding for infrastructure implementation through Provincial Treasury that focusses directly on water and sanitation with a social impact. We anticipate that we will be able to convert the digester tanks to a full water borne sewerage system in Thornhill and also start the same process in Wavecrest. Coega Development Corporation will be the implementing agent for Provincial Treasury for these projects.

The Municipality has also secured grant funding through the Department of Water Affairs for the Augmentation and Treatment of Raw Borehole Water supply to Wavecrest. We will also receive a further drawdown on the disaster management funding which will be spend mainly on street upgrades and sewer reticulation.

Further to the above the Municipality has also continued with the process on land alienation which will fund ward based capital projects reflected within the Integrated Development Plan.

Our ratepayers and customers are already burdened heavily by high taxes and continuing price increases at just about every level, electricity, fuel and food prices being points in case. Maintaining services at the high levels to which our ratepayers and consumers have become accustomed to, is very expensive.

To this end we have kept our increases for all services between 6 – 8.3 percent, with the exception of Refuse removal and Rates. For Refuse removal the annual tariff increase is 10% higher than the previous year to ensure that it will operate as a trading service as required by National Treasury. The need for tariffs to be cost reflective was highlighted in the previous year budget and remains relevant. On rates we had to incur a 23.25% tariff increase on businesses and a 20.79% increase in residential areas to effectively gain a 7% Rand value increase based on the prior year figures. This is due to our valuation roll dropping by R7.3 billion in total. During the draft budget a 23.25% tariff increase was anticipated for all consumers, but with the supplementary valuation roll and the inclusion of the wind farms we were able to reduce this tariff to 20.79%. It should be noted that the effective increase will differ from household to household as the increase or drop in their annual property valuation will determine the percentage increase to be paid.

Details of the Operational and Capital Budgets are provided in the budget document.

The draft budget tabled in March was of course not the final product and some changes have been made which is reflecting within the budget document.

I therefore submit this Annual Budget 2014/2015 for adoption.

1.2 Municipal Budget

DEFINITION OF A MUNICIPAL BUDGET

A municipal budget is generally a projection of future revenues and expenditure.

A budget is used to control financial transactions and should also be used as a management and planning tool. It is also the tool for implementing the service delivery objectives of the Municipality as set out in their Integrated Development Plan (IDP).

A municipal budget also provides for greater transparency, accountability, flexibility, and predictability within the municipality.

A Municipal budget is divided into a Capital and an Operating Budget:

a) A capital budget is an estimate of the expenses that will be incurred during that financial year to create future benefits, and the sources of finance from which these expenses will be funded. The municipality spends money either to buy fixed assets or to add to the value of an existing fixed asset with a useful life that extends beyond one year. Fixed assets include, inter alia, land and buildings, motor vehicles, furniture, computers, office equipment and machinery.

Example: Land and buildings, pump stations, water purification plants, furniture, etc.

b) An operating budget is an estimate of the operating revenues which will accrue to the municipality through its normal service delivery and the expenditure that will be incurred through the day to day operations of the municipality over the financial year.

Example: The purchase of a photocopier is a capital expenditure and is budgeted for under the capital budget, but the maintenance and other expenses such as the paper and toner for the photocopier is budgeted for under the operating budget.

OBJECTIVE OF A MUNICIPAL BUDGET

The main objective of a municipal budget is to sensibly allocate realistically expected resources to the municipality's service delivery goals or performance objectives identified as priorities in the approved IDP.

The municipal budget is a tool through which the total level of revenue and expenditure are adequately controlled, public resources are appropriately allocated among sectors and programs, and ensure that departments operate as efficiently as possible within the municipality.

WHERE DOES THE MUNICIPALITY'S REVENUE ORIGINATE FROM?

The Municipality collects revenue from various sources. To achieve sustainable service delivery, we have to ensure sustainable income streams to our services. Property rates are an important source of income.

Other sources include tariffs charged for water and sanitation, electricity and refuse removal management. Kouga Local Municipality also receives external funds from National and Provincial Departments by means of conditional (e.g. Municipal Infrastructure Grant) and unconditional grants (e.g. Equitable Share).

WHAT DOES THE MUNCIPALITY SPEND ITS REVENUE ON?

Municipality spends its revenue on the following services:
• Water, electricity, sanitation and refuse removal
• Streets and Storm Water
• Repairs and maintenance to infrastructure
• Relief for the poor
• Fire services
• Parks
• Libraries
• Sport and recreation facilities
• Upgrading and maintenance of beaches

HOW CAN RESIDENTS BE INVOLVED IN THE BUDGET PROCESS?

The Municipality encourages public participation in the budgetary process. A draft budget can be viewed at the Municipal offices, the official Municipal website as well as all public libraries and is open to comment after it is tabled to Council in March each year.

Once the deadline for comments has been met, amendments are considered and the final budget is approved by Council before the end of May each year. New rates and tariffs are implemented at the start of each new financial year, being 1 July.

COUNCIL OVERSIGHT OVER THE BUDGET PROCESS

A municipal council is elected to direct and exercise oversight of how a municipality raises revenue, plans the use of funds through its budget and spends the funds in accordance with the council approved budget.

In terms of section 4(2)(a) of the Municipal Systems Act, 2000 the council has a duty “to use the resources of the municipality in the best interests of the local community”. This duty is extended to individual councillors through the *Code of Conduct for Councillors*, which states:

> *2. General conduct of councillors. – A councillor must –*
> *(a) perform the functions of office in good faith, honestly and in a transparent manner; and*
> *(b) at all times act in the best interests of the municipality and in such a way that the credibility and integrity of the municipality are not compromised.*

Over the last few years, escalating unauthorised, irregular and fruitless and wasteful expenditures has been observed by the Auditor-General in its annual reports on local government audit outcomes. Many municipalities have not dealt effectively with instances of unauthorised, irregular and fruitless and wasteful expenditure. Such matters must be dealt with decisively by council to address fraud and corruption.

When municipal funds are used for inappropriate purposes it is not in the best interests of the municipality or the local community. Those funds should have been used to deliver services to communities.

Therefore, each council has a duty to put in place policies and processes to:
(a) Prevent unauthorised, irregular and fruitless and wasteful expenditure;

(b) Identify and investigate unauthorised, irregular and fruitless and wasteful expenditure; and

(c) Respond appropriately, and in accordance with the law, to confirmed instances of unauthorised, irregular and fruitless and wasteful expenditure.

As part of the 2014/15 budget process, municipalities are strongly advised to ensure that the necessary policies and processes are institutionalized to proactively curb prohibited expenditure, poor policy implementation and planning. This requires decisive response by all councillors and municipal officials.

1.3 Executive Summary

The main objective of a municipal budget is to allocate realistically expected resources to the service delivery goals or performance objectives identified as priorities in the approved Integrated Development Plan.

For 2014/2015 the process followed in compiling these budgets were as follow:

A budget steering committee was established under the guidance of the Executive Mayor in compliance with the Municipal Budget and Reporting Regulations. The Municipal Budget and Reporting Regulations Part 1section 4 states that the Mayor should establish a budget steering committee to provide technical assistance to the Mayor in discharging his responsibilities as set out in section 53 of the Act. This section gives clarity as to the composition of this Committee. It states that it should consist at least of:

- The Councillor responsible for financial matters
- The Municipal Manager
- The Chief Financial Officer
- The senior managers responsible for the three largest votes in the municipality
- The manager responsible for budgeting
- The manager responsible for planning
- Any technical experts on infrastructure

The Executive Mayor established this committee and it consisted of the following individuals:

- Councillor Koerat (Executive Mayor)
- Councillor Stuurman (Mayoral Committee Member responsible for Finance)
- Mr. S. Fadi (Municipal Manager)
- Ms. C. Burger (Chief Financial Officer)
- Mr. V. Felton (Director: Infrastructure, Planning and Development)
- Mr. J. Jansen (Director: Social Services)
- Mr. E. Olivier (Manager: Human Settlements)
- Mr. S. Abrahams (Manager: Budget and Treasury)
- Mr. A. Koegelenberg (Manager: Performance Management Systems)
- Ms. L. Randall (Media Liaison Officer)

The following individuals were attending on invitation:

- Ms. C. Arends (Director: Tourism and Local Economic Development)
- Ms. T. Tom (Director: Administration, Monitoring and Evaluation)
- Relevant managers from various directorates

The Budget Steering Committee met on the following dates during 2014 (excluding meetings held for the adjustment budget):

- 7 February 2014
- 18 February 2014
- 24 February 2014
- 26 February 2014
- 27 February 2014
- 13 March 2014
- 14 March 2014
- 15 May 2014
- 26 May 2014

This budget is prepared based on a mutual commitment and understanding between Council and Management that strict budget control, debt control and overall financial discipline will be maintained in order to achieve the budgeted goals as set out in this budget.

By strict enforcement and execution of the credit control policy, together with an understanding of the prevailing economic climate, Council aims to maintain a rate of payment to meet Council's financial and constitutional obligations. To this end R37 million of outstanding rates income was handed over to lawyers in January 2014 and we have already noted the positive effects of the legal actions. Further an in-depth debtor's book analysis is in progress with a clear strategy developed which is in the process of being implemented. The first point of departure for this strategy is an Equitable Share Registration drive that has started from 27 May 2014 and will continue until 12 June 2014. As our processes unfold progress will be reported to Council.

The Municipality's budget must be viewed in the context of the policies and financial priorities of the National, Provincial and District authorities. Basically, the government spheres are partners in fulfilling the service delivery challenges experienced in Kouga Local Municipality. It is therefore essential that the other government spheres support the municipality by direct allocation of resources and subsidies to enable the municipality to maintain and achieve the long-term capital needs of the community. We have made progress in the last twelve months in this regard, but will still continue to intensify our efforts to secure grant funding for various projects.

In September 2011, National Treasury published the "*Local Government Budgets and Expenditure Review"*.
The *Review* highlights the following areas as requiring particular attention by municipalities:

- ***Revenue management*** – To ensure the collection of revenues, municipalities need to ensure that billing systems are accurate, send out accounts to residents and follow up to collect revenues owed.

- ***Collecting outstanding debts*** – This requires political commitment, sufficient administrative capacity, and pricing policies that ensure that bills are accurate and affordable.
- ***Pricing services correctly*** – The full cost of services should be reflected in the price charged to residents who can afford to pay. Many municipalities offer overly generous subsidies and rebates that result in services being run at a loss, resulting in funds being diverted away from other priorities.
- ***Underspending on repairs and maintenance*** – Often seen as a way to reduce spending in the short term, underspending on maintenance can shorten the life of assets, increase long-term maintenance and refurbishment costs, and cause a deterioration in the reliability of services.
- ***Spending on non-priorities*** – Many municipalities spend significant amounts on non-priority items including unnecessary travel, luxury furnishings, excessive catering and unwarranted public relations projects. Consultants are often used to perform routine tasks. Considering the pressurised economic climate continued spending on non-priority wants cannot be sustained.

National Treasury's MFMA Circular No. 70 was used to guide the compilation of the 2014/15 MTREF (Annexure E)

National Treasury requires municipalities to continue to explore appropriate ways of structuring the tariffs for utility services to encourage more efficient use of these services and to generate resources required for maintenance, renewal and expansion of infrastructure. They also encourage municipalities to keep increases in rates, tariffs and other charges at levels that reflect appropriate balance between the interest of poor households, other customers and ensuring the financial sustainability of the municipality. For this reason municipalities must justify all increases in excess of the 6 per cent upper boundary of the South African Bank's inflation target.

Currently our tariffs is only structured to fund operations and not for the renewal and expansion of infrastructure.

National Treasury advises that priority ought to be given to:

- Ensuring that drinking water and waste water management meets the required quality standards at all times;
- Protecting the poor;
- Ensure that public investments, services, regulations and incentives are focussed in defined spatial areas (spatial targeting) to optimise overall connectivity to access to opportunities;
- Provide clear signals to the private sector;
- Transport, human settlements, bulk infrastructure, economic infrastructure, land use management (e.g. zoning), tax and subsidy incentives;
- Supporting meaningful Local economic development initiatives that foster micro and small business opportunities and job creation;
- Securing the health of their asset base by increasing spending on repairs and maintenance;
- Expediting spending on capital projects that are funded by conditional grants;
- Ensuring that borrowed funds are invested in revenue generated assets as part of the capital programme; and
- To implement cost containment measures.

Municipalities must also ensure that their capital budgets reflect consistent efforts to address the backlogs in basic services and the renewal of the infrastructure of existing network services.

National Treasury also states that municipalities should control unnecessary spending on nice to-have items and non-essential activities. Some examples of non-priority expenditure is,

- excessive sponsorships, e.g. of music festivals and sporting events, including the purchase of tickets to events for councillors and/or officials;
- public relations projects and activities not centred on actual service delivery or are not a municipal function (e.g. celebrations; gala dinners, commemorations, advertising and voter education);
- LED projects that serve the narrow interests of only a small number of beneficiaries or fall within the mandate of other government departments such as Department of Agriculture;
- excessive catering for meetings and other events, including the use of public funds to buy alcoholic beverages;
- arranging workshops and events at expensive private venues, especially ones outside the municipality (as opposed to using the municipality's own venues);
- excessive printing costs instead of maximising the use of the municipality's website;
- excessive luxurious office accommodation and office furnishings;
- foreign travel by mayors, councillors and officials, particularly 'study tours';
- excessive councillor and staff perks such as luxurious mayoral cars and houses, notebooks, IPADS and cell-phone allowances; travel and subsistence allowances
- excessive staff in the office of the mayor – particularly the appointment of political 'advisors' and 'spokespersons';
- all donations to individuals that are not made in terms of the municipality's indigent policy or a bursary scheme for instance donations to cover funeral costs (other than pauper burials which is a district function);
- costs associated with long-standing staff suspensions and the legal costs associated with not following due process when suspending or dismissing staff, as well as payment of severance packages or 'golden handshakes';
- the use of consultants to perform routine management tasks, and the payment of excessive fees to consultants;
- excessive unnecessary spending on personal bodyguards and security to political office bearers; and
- Excessive overtime.

The following budget principles and guidelines directly informed the compilation of the 2014/15 MTREF:

- The priorities and targets in relation to the key strategic focus areas as determined in the IDP.
- The level of property rates and tariff increases to take into account the need to address maintenance and infrastructural backlogs, including the expansion of services.
- The level of property rates and tariff increases to ensure the delivery of services on a financially sustainable basis.
- An assessment of the relative human resources capacity to implement the Budget.
- No budget allocation has been made to programmes and projects, unless the respective programme and project plans have been submitted by the relevant Executive Directors.
- The need to enhance the municipality's revenue base.
- No loan funding is available to support the Capital Budget, in view of financial affordability considerations.

- In accordance with Section 19 of the Municipal Finance Management Act, the affected Executive Directors to submit comprehensive reports in relation to new projects, inter alia, dealing with the total project costs, funding sources, future operating budget implications and associated tariff implications, before Council finally approves the implementation of any new project.
- There will be no budget allocated to national and provincial funded projects unless the necessary grants to the municipality are reflected in the national and provincial budget and have been gazetted as required by the annual Division of Revenue Act

The main challenges experienced remain as during the compilation of the 2014/15 MTREF and can be summarised as follows for the 2014/15 MTREF budget cycle:

- The continued negative effect of the economic downturn;
- Aging and poorly maintained infrastructure;
- Reprioritisation of capital projects and operating expenditure within the financial affordability limits of the Budget, taking the cash position into account;
- The increased cost of bulk water and electricity (due to tariff increases from the Metro and Eskom), which is placing upward pressure on service tariffs to residents. Continuous high tariff increases are not sustainable - as there will be point where services will no-longer be affordable;
- The need to fill critical vacancies, but the current employee remuneration is already high;
- Depleted Capital Replacement Reserve, impacting on the Municipality’s ability to fund capital expenditure from internal sources;
- Allocation of the required operating budget provision for newly created infrastructure and facilities, with a consequential impact on rates and tariff increases;
- Maintaining revenue collection rates at the targeted levels;
- Allocation of the required budget provision for the rehabilitation and maintenance of infrastructure;
- Decrease in the property valuation roll;
- Unfunded mandates continuing to be a cost burden to Council;
- Increase in the prime lending rate in January 2014.

In summary our realistic anticipated income is as follow:

Operational own income	R531,217,119.00
Operational grants and subsidies	R87,846,799.00
Operational Income Budget	**R619,063,918.00**
Capital Grants	R33,340,400.00
Total Income Budget	**R652,404,318.00**

In summary our expenditure is allocated as follow:

Salaries	R213,686,840.00
Repairs and Maintenance	R43,640,066.00
Bulk water and electricity purchases	R190,710,580.00
General Expenses	R248,497,739.00
Capital expenditure	R36,231,400.00
Total Expenditure	**R732,766,625.00**
Total Income less total expenditure (DEFICIT)	**R80,362,307.00**

A line that we have included within the budget documentation is the Depreciation cost of R80.3 million. With now complying with GRAP 17, we are able to accurately reflect the depreciation cost of Assets within the Annual Budget. This line item is seen as a 'non cash flow item'. The purpose of depreciation is to match the cost of a productive asset (that has a useful life of more than a year) to the revenues earned from using the asset. Since it is hard to see a direct link to revenues, the asset's cost is usually allocated to (assigned to, spread over) the years in which the asset is used. Depreciation systematically allocates or moves the asset's cost from the Statement of Financial Position to expense on the Statement of Financial Performance over the asset's useful life. In other words, depreciation is an allocation process in order to achieve the matching principle; it is *not* a technique for determining the fair market value of the asset. By introducing this line item within the operational expenditure budget as a result of the requirements of GRAP 17, it appears as if there is a possible loss of R80.3 million which is not an accurate reflection as this is a non cash flow item as explained above. In future years it will be systematically absorbed into the operational budget to establish an asset replacement fund.

The increase in capital expenditure is marginal. The capital programme for the 2015/16 and 2016/17 financial years will decrease until MIG funding has been secured. It should be noted that the Municipality has reached its prudential borrowing limits and there is very little scope to substantially increase these borrowing levels over the medium-term. The repayment of capital and interest (debt services costs) has substantially increased over the past few years. We have been able to restructure the DBSA loans to have an interest free period of 18 months to delve into the capital amount due to in the long term restore borrowing power.

Refer to Annexure C for the MIG 3 year cycle budget. It is important to note the comments on both the projects for Weston WWTW & Sewer Reticulation and Kruisfontein WWTW upgrade as a budget shortfall is known and application will be made to MIG for budget maintenance, i.e. shifting of funding is likely within the year to complete these two projects directly aligned to the housing needs.

The Capital Budget Consist of:

Project	Amount	Funding source
Erection of hawkers facilities	300 000.00	Grant from CDM
Oyster Bay modular library	900 000.00	Grant from Department of Sports, Arts and Culture
Tokyo Sexwale modular library	900 000.00	Grant from Department of Sports, Arts and Culture
Environmental Health: 6 m3 Mash Truck	780 000.00	Grant from CDM
Environmental Health: Trailer	11 000.00	Grant from CDM
Electrification of Oceanview (181 houses)	2 000 000.00	INEP
Electrification of Pola Park (340 houses)	3 000 000.00	INEP
Weston WWTW	2 230 757.44	MIG
Kruisfontein WWTW upgrade	14 290 698.56	MIG
Patensie Bulk Sewer Infrastructure	6 150 864.00	MIG
Sports facilities	4 251 060.00	MIG
LED (Social Institutions & micro enterprise infrastructure)	1 417 020.00	MIG
	36 231 400.00	

The **tariff increases** for the major income sources are as follow (**Annexure B**):

Rates	23.25% business tariff 20.79% residential tariff
Electricity	8.3% (average increase)
Water	8%
Sewerage	6%
Refuse Removal	10%
EMF	6%
Other	Range mainly between 6–7%

For Electricity we have to apply to NERSA for the approval of our budget and tariffs. All tariffs were approved as applied for, except for the Basic Charges of the three phase Domestic Tariffs and the Time Of Use (TOM) Network Demand Charges which were reduced by NERSA as noted on their letter. This results in the average increase reducing from 8.4% in the draft budget to 8.3%.

On rates we had to incur a 23.25% tariff increase on businesses and a 20.79% increase in residential areas to effectively gain a 7% Rand value increase based on the prior year figures. This is due to our valuation roll dropping by R7.3 billion in total. During the draft budget a 23.25% tariff increase was anticipated for all consumers, but with the supplementary valuation roll and the inclusion of the wind farms we were able to reduce this tariff to 20.79%. It should be noted that the effective increase will differ from household to household as the increase or drop in their annual property valuation will determine the percentage increase to be paid.

Below is examples of the rand and cent value of 20.79% increase on different households:

	Tariff in 2013	Tariff in 2014	Increase of cents in the Rand		
	0.004787	**0.005782**	**23.25%**		
Value of property in 2013/2014	**Yearly rates paid in 2013/2014**	**Yearly rates paid in 2014/2015**	**Value of property in 2014/2015**	**Difference in Rand Value**	**Increase**
2 400 000.00	11 488.80	12 720.00	2 200 000.00	1 231.60	10.72%
2 000 000.00	9 574.00	13 298.00	2 300 000.00	3 724.60	38.90%
1 500 000.00	7 180.50	8 383.00	1 450 000.00	1 203.40	16.76%
130 000.00	622.31	780.57	135 000.00	158.26	25.43%
130 000.00	622.31	751.66	130 000.00	129.35	20.79%

The summary of the total income and expenditure for the 2014/2015 financial year per directorate and per department is attached as Annexure D.

1.4 Operating Revenue Framework

The continued provision and expansion of services is largely dependent on the Municipality generating the required revenues. Efficient and effective revenue management is thus critical in ensuring the ongoing financial sustainability of the Municipality. It is worth noting that, in accordance with the MFMA, expenditure has to be limited to the realistically anticipated revenues.

The Municipality's revenue management strategy includes the following key components:

- National Treasury's guidelines;
- Growth in the Municipality's revenue base;
- Efficient revenue management, which aims to ensure a 95 per cent annual collection rate for property rates and other key service charges, after discounting rebates given to indigents;
- Electricity tariff increases as approved by the National Electricity Regulator of South Africa (NERSA);
- Water bulk tariff increases as approved by NMBM;
- Ensuring of fully cost reflective tariffs for trading services;
- Determining the tariff escalation rate by establishing/calculating the revenue requirement of each service;
- The municipality's Property Rates Policy approved in terms of the Municipal Property Rates Act, 2004 (Act 6 of 2004) (MPRA);
- Increase ability to extend new services and recover costs;
- The municipality's Indigent Policy and rendering of free basic services; and
- Tariff policies of the Municipality;
- The level of property rates and tariff increases must ensure financially sustainable services delivery;

- The level of property rates and tariff increases to provide for the maintenance and replacement of infrastructure, including the expansion of services.

The following is a high level summary of the 2014/15 MTREF (classified by main revenue source):

The operational revenue of R619,063,918.00 will be sourced as follow:

- Assessment rates (less rebates) R138,420,009.16
- Electricity R215,764,928.81
- Water R56,970,194.59
- Sewerage R30,516,258.50
- Refuse R32,090,412.76
- Equitable share R66,129,000.00
- Grants and subsidies R21,717,799.00
- Other Income R57,455,315.60

In line with the formats prescribed by the Municipal Budget and Reporting Regulations, capital transfers and contributions are excluded from the operating statement, as inclusion of these revenue sources would distort the calculation of the operating surplus/deficit.

Revenue generated from rates and services charges forms a significant percentage of the revenue basket for the Municipality (79%).

Operating grants and transfers total R87.8 million in the 2014/15 financial year. There has been an increase in the Equitable Share Allocation. The increase in Equitable Share Allocation based on the new census data is now seen in the 2014/15, but especially the 2015/16 financial year.

Tariff-setting is a pivotal and strategic part of the compilation of any budget. When rates, tariffs and other charges were revised, local economic conditions, input costs and the affordability of services were taken into account to ensure the financial sustainability of the Municipality. It should however be noted that all tariffs are still not cost reflective and this will be phased in over a period of time to be cost reflective by 2014 as advised by National Treasury.

The cost drivers of a municipality are informed by items such as the cost of remuneration, bulk purchases of electricity and water, petrol, diesel, chemicals, cement etc. The current challenge facing the Municipality is managing the gap between cost drivers and tariffs levied, as any shortfall must be made up by either operational efficiency gains or service level reductions. Within this framework the Municipality has undertaken the tariff setting process relating to service charges as follows.

1.4.1 Property Rates

Property rates cover the cost of the provision of general services, such as recreational, library and roads and storm water services. Determining the effective property rate tariff is therefore an integral part of the municipality's budgeting process.

The categories of rateable properties for purposes of levying rates and the rates for the 2014/15 financial year based on a 23.25 per cent increase for businesses and 20.79 percent for residential properties from 1 July 2014 is contained in Annexure B.

It should be noted that the Municipality will implement the new valuation roll on 1 July 2014. This matter and the increase have been detailed previously in this document.

1.4.2 Sale of Water and Impact of Tariff Increases

National Treasury is encouraging all municipalities to carefully review the level and structure of their water tariffs to ensure:

- Water tariffs are fully cost-reflective – including the cost of maintenance and renewal of purification plants, water networks and the cost associated with reticulation expansion;
- Water tariffs are structured to protect basic levels of service and ensure the provision of free water to the poorest of the poor (indigent); and
- Water tariffs are designed to encourage efficient and sustainable consumption.

In addition National Treasury has urged all municipalities to ensure that water tariff structures are cost reflective by 2014.

A tariff increase of 8% will be implemented as from 1 July 2014. The tariff increase is mainly influenced by the following:

- The increased cost of bulk water purchases;
- Increase in repairs and maintenance of water infrastructure;
- Moving towards cost reflective tariffs
- Providing for debt impairment.

A summary of the tariffs for households (residential) and non-residential can be obtained in Annexure B.

The tariff structure has not been changed. The tariff structure is designed to charge higher levels of consumption at a higher rate per 30 day period.

1.4.3 Sale of Electricity and Impact of Tariff Increases

Considering the Eskom increases, the consumer tariff had to be increased by an average of 8.3 per cent to offset the additional bulk purchase cost from 1 July 2014.

The tariff increases are mainly influenced by the following:

- The increase in cost of bulk electricity purchases;
- Increase in repairs and maintenance of electricity infrastructure;
- Providing for debt impairment.

The electricity tariff increases have been approval by NERSA.

The tariff structure of the 2014/15 financial year has not been changed. The tariff structure is designed to charge higher levels of consumption at a higher rate per 30 day period. The aim is to subsidise the lower consumption users (mostly the poor).

A summary of the tariffs can be obtained in Annexure B.

R5 million’s worth of Capital Projects funded by grants have been identified for the financial year.

1.4.4 Sanitation and Impact of Tariff Increases

A tariff increase of 6 per cent for sanitation from 1 July 2014 will be implemented. This is based on the input cost assumptions related to water. It should be noted that electricity costs contributes approximately 20 per cent of waste water treatment input costs.

A summary of the tariffs can be obtained in Annexure B.

1.4.5 Waste Removal and Impact of Tariff Increases

A 10 per cent increase in the waste removal tariff will be implemented from 1 July 2014 to ensure that the tariff is now fully cost reflective. In the 2013/2014 financial year, this tariff was still trading at a deficit; however we anticipate that this increase will enable the service to break even.

A summary of the tariffs can be obtained in Annexure B.

1.5 Operating Expenditure Framework

The Municipality’s expenditure framework for the 2014/15 budget and MTREF is informed by the following:

- Funding of the budget over the medium-term as informed by Section 18 and 19 of the MFMA;
- A balanced budget approach by limiting operating expenditure to the operating revenue;
- Strict adherence to the principle of *no project plans no budget*. If there is no business plan no funding allocation can be made.

The following is a high level summary of the 2014/15 budget and MTREF (classified per main type of operating expenditure):

The operational expenditure of R696,535,225 is split as follow:

- Remuneration R213,686,840.00 (including Councillors)
- Bulk purchases R190,710,580.00
- Other general expenses R118,456,724.00
- Depreciation (non-cash flow) R80,357,833.00
- Repairs and Maintenance R43,640,066.00
- Provision for non-payment R49,683,182.00

The budgeted allocation for employee related costs for the 2014/15 equals 35 per cent of the total operating income (including operating grants). As per guidance from National Treasury, Municipalities must take into account the multi-year Salary and Wage Collective Agreement for the period 1 July 2012 to 30 June 2015. The agreement provides for a wage increase based on the average CPI for the period 1 February 2012 until 31 January 2013, plus 1.25 per cent for the 2013/14 financial year.

Municipalities were advised by National Treasury to provide for 6,8% increase in salaries for 2014/2015 in line with the Collective Salaries and Wage agreement.

The cost associated with the remuneration of councillors is determined by the Minister of Co-operative Governance and Traditional Affairs in accordance with the Remuneration of Public Office Bearers Act, 1998 (Act 20 of 1998). The most recent proclamation in this regard has been taken into account in compiling the Municipality's budget. In addition, a provision has been made for possible increases.

Bulk purchases are directly informed by the purchase of electricity from Eskom and water from the Metro (NMBM). The annual price increases have been factored into the budget appropriations and directly inform the revenue provisions.

Other expenditure comprises of various line items relating to the daily operations of the municipality. This group of expenditure has also been identified as an area in which cost savings and efficiencies can be achieved and is implemented as contracted services fall beyond the contracted term.

The provision of debt impairment was raised at 9%. All non-cash flow items and grants were eliminated from the income balance before the provision calculation was applied. While this expenditure is considered to be a non-cash flow item, it informed the total cost associated with rendering the services of the municipality, as well as the municipality's realistically anticipated revenues.

Finance charges consist primarily of the repayment of interest on long-term borrowing (cost of capital).

Depreciation charges have been explained previously within this document.

1.5.1 Free Basic Services: Basic Social Services Package

The social package assists households that are poor or face other circumstances that limit their ability to pay for services. To receive these free services the households are required to register in terms of the Municipality's Indigent Policy. Details relating to free services, cost of free basis services, revenue lost owing to free basic services as well as basic service delivery measurement is contained within the expenditure budget.

The cost of the social package of the registered indigent households is largely financed by national government through the local government equitable share received in terms of the annual Division of Revenue Act.

The current assistance being provided is:

- FREE 50 Kwh plus basic charge
- FREE 6 kl water plus basic charge
- FREE Monthly refuse, sewerage (based on 6 kl water), EMF levy
- FREE Extra R85,000 on the value of property for rates

In the amended and updated policy for Indigent Support Policy we have increased the FREE 6 kl water plus basic charge to 12 kl water plus basic charge.

1.6 Annual Budget Tables – Annexure A

Explanatory notes to MBRR Table A1 - Budget Summary

1. Table A1 is a budget summary and provides a concise overview of the Municipality's budget from all of the major financial perspectives (operating, capital expenditure, financial position, cash flow, and MFMA funding compliance).
2. The table provides an overview of the amounts approved by Council for operating performance, resources deployed to capital expenditure, financial position, cash and funding compliance, as well as the municipality's commitment to eliminating basic service delivery backlogs.
3. Financial management reforms emphasises the importance of the municipal budget being funded. This requires the simultaneous assessment of the Financial Performance, Financial Position and Cash Flow Budgets, along with the Capital Budget. The Budget Summary provides the key information in this regard:
    a. The operating surplus/deficit (after Total Expenditure) is positive over the MTREF
    b. Capital expenditure is balanced by capital funding sources, of which
        i. Transfers recognised is reflected on the Financial Performance Budget;
        ii. Borrowing is incorporated in the net cash from financing on the Cash Flow Budget
        iii. Internally generated funds are financed from a combination of the current operating surplus and accumulated cash-backed surpluses from previous years. The amount is incorporated in the Net cash from investing on the Cash Flow Budget..The fact that the municipality's cash flow remains positive, and is improving indicates that the necessary cash resources are available to fund the Capital Budget.
4. The Cash backing/surplus reconciliation shows that in previous financial years the municipality was not paying much attention to managing this aspect of its finances, and consequently many of its obligations are not cash-backed. This places the municipality in a very vulnerable financial position, as the recent slow-down in revenue collections highlighted. It is necessary to ensure adequate cash-backing for all material obligations. This cannot be achieved in one financial year.
5. Even though the Council is placing great emphasis on securing the financial sustainability of the municipality, this is not being done at the expense of services to the poor. The section of Free Services shows that the amount spent on Free Basic Services and the revenue cost of free services provided by the municipality continues to increase. In addition, the municipality continues to make progress in addressing service delivery backlogs.

Explanatory notes to MBRR Table A2 - Budgeted Financial Performance (revenue and expenditure by standard classification)

1. Table A2 is a view of the budgeted financial performance in relation to revenue and expenditure per standard classification.
2. Note the Total Revenue on this table includes capital revenues (Transfers recognised – capital) and so does not balance to the operating revenue shown on Table A4.
3. Note that as a general principle the revenues for the Trading Services should exceed their expenditures.

Explanatory notes to MBRR Table A3 - Budgeted Financial Performance (revenue and expenditure by municipal vote)

1. Table A3 is a view of the budgeted financial performance in relation to the revenue and expenditure per municipal vote. This table facilitates the view of the budgeted operating performance in relation to the organisational structure of the Municipality. This means that it is possible to present the operating surplus or deficit of a vote.

Explanatory notes to Table A5 - Budgeted Capital Expenditure by vote, standard classification and funding source

1. Table A5 is a breakdown of the capital programme in relation to capital expenditure by municipal vote (multi-year and single-year appropriations); capital expenditure by standard classification; and the funding sources necessary to fund the capital budget, including information on capital transfers from national and provincial departments.

Explanatory notes to Table A6 - Budgeted Financial Position

1. Table A6 is consistent with international standards of good financial management practice, and improves understandability for councilors and management of the impact of the budget on the statement of financial position (balance sheet).
2. This format of presenting the statement of financial position is aligned to GRAP1, which is generally aligned to the international version which presents Assets less Liabilities as "accounting" Community Wealth. The order of items within each group illustrates items in order of liquidity; i.e. assets readily converted to cash, or liabilities immediately required to be met from cash, appear first.

Explanatory notes to Table A7 - Budgeted Cash Flow Statement

1. The budgeted cash flow statement is the first measurement in determining if the budget is funded.
2. It shows the expected level of cash in-flow versus cash out-flow that is likely to result from the implementation of the budget.

Explanatory notes to Table A8 - Cash Backed Reserves/Accumulated Surplus Reconciliation

1. The cash backed reserves/accumulated surplus reconciliation is aligned to the requirements of MFMA Circular 42 – Funding a Municipal Budget.
2. In essence the table evaluates the funding levels of the budget by firstly forecasting the cash and investments at year end and secondly reconciling the available funding to the liabilities/commitments that exist.
3. The outcome of this exercise would either be a surplus or deficit. A deficit would indicate that the applications exceed the cash and investments available and would be indicative of non-compliance with the MFMA requirements that the municipality's budget must be "funded".
4. Non-compliance with section 18 of the MFMA is assumed because a shortfall would indirectly indicate that the annual budget is not appropriately funded.

Explanatory notes to Table A9 - Asset Management

1. Table A9 provides an overview of municipal capital allocations to building new assets and the renewal of existing assets, as well as spending on repairs and maintenance by asset class.

Explanatory notes to Table A10 - Basic Service Delivery Measurement

1. Table A10 provides an overview of service delivery levels, including backlogs (below minimum service level), for each of the main services.

Part 2 – Supporting Documentation

2.1 Overview of the annual budget process

Section 53 of the MFMA requires the Mayor of the municipality to provide general political guidance in the budget process and the setting of priorities that must guide the preparation of the budget.

2.1.1 Budget Process Overview

In terms of section 21 of the MFMA the Mayor is required to table in Council ten months before the start of the new financial year a time schedule that sets out the process to revise the IDP and prepare the budget.

Key dates applicable to the process were:

- **August 2013 –** Joint strategic planning session of the Mayoral Committee and Executive Management. Aim: to review past performance trends of the capital and operating budgets, the economic realities and to set the prioritisation criteria for the compilation of the 2013/14 MTREF;
- **November 2013** – Detail departmental budget proposals (capital and operating) submitted to the Budget and Treasury Office for consolidation and assessment against the financial planning guidelines;
- **3 to 7 January 2014** - Review of the financial strategy and key economic and financial planning assumptions. This included financial forecasting and scenario considerations;
- **January 2014 –** Multi-year budget proposals are submitted to the Mayoral Committee for endorsement;
- **30 January 2014** - Council considers the 2013/14 Mid-year Review and Adjustments Budget;
- **February 2014** - Recommendations of the Mayoral Committee are communicated to the respective departments. The draft 2014/15 MTREF is revised accordingly;
- **31 March 2014** - Tabling in Council of the draft 2014/15 IDP and 2014/15 MTREF for public consultation;
- **April 2014 –** Public consultation;
- **6 May 2014** - Closing date for written comments;
- **May 2014 –** finalisation of the 2014/15 IDP and 2014/15 MTREF, taking into consideration comments received from the public, comments from National Treasury, and updated information from the most recent Division of Revenue Bill and financial framework; and
- **30 May 2014** - Tabling of the 2014/15 MTREF before Council for consideration and approval.

2.1.2 Financial Modelling and Key Planning Drivers

As part of the compilation of the 2014/15 MTREF, extensive financial modelling was undertaken to ensure affordability and long-term financial sustainability. The following key factors and planning strategies have informed the compilation of the 2014/15 MTREF:

- Asset maintenance
- Economic climate and trends (i.e inflation, Eskom increases, household debt, migration patterns)
- Performance trends
- Cash Flow Management Strategy
- Debtor payment levels
- The need for tariff increases to be cost reflective versus the ability of the community to pay for services;
- Improved and sustainable service delivery

In addition to the above, the strategic guidance given in National Treasury's MFMA has been taken into consideration in the planning and prioritisation process.

2.1.3 Community Consultation

The draft 2014/15 MTREF as tabled before Council and adopted on 8 April 2014 was subject to community consultation. The draft budget was published on the municipality's website, and hard copies made available at various libraries. Consultation started in April and public written comments could also be submitted to be considered by 6 May 2014.

All documents in the appropriate format (electronic and printed) were provided to National Treasury, and other national and provincial departments in accordance with section 23 of the MFMA, to provide an opportunity for them to make inputs. Provincial Treasury did provide feedback and their recommendations as agreed upon were updated in the budget document.

Submissions received during the community consultation process and additional information regarding revenue and expenditure and individual capital projects were addressed, and where relevant considered as part of the finalisation of the 2014/15 MTREF. It should be noted that some inputs given were addressing issues not relating to the budget. Often times inputs also only addressed concerns without proposals. These inputs were considered at the budget steering committee that took place on 15 May 2014.

2.2 Legislation compliance status

Compliance with the MFMA implementation requirements have been substantially adhered to through the following activities:

1. In year reporting
   Reporting to National Treasury in electronic format was complied with on a monthly basis.

2. Internship programme
   The Municipality is participating in the Municipal Financial Management Internship programme and has employed interns undergoing training in various divisions of the Financial Services Department. It is a concern of the Finance directorate that we have invested time and resources into our Finance Interns, but are not able to absorb them into our staff establishment. They have become to fulfil critical functions within the different finance departments and it would be to our detriment to loose these individuals. Council should take serious consideration of this matter and see how best these Finance Interns can be absorbed in the future into the Institution.

3. Budget and Treasury Office
   The Budget and Treasury Office has been established in accordance with the MFMA.

4. Audit Committee
   An Audit Committee has been established.

5. Service Delivery and Implementation Plan
   The detailed SDBIP document is still to be developed after the approval of the annual budget and draft IDP.

6. Annual Report
   Annual report is compiled in terms of the MFMA and National Treasury requirements.

7. Policies (Annexure F)
   The following policies has been amended and updated as per our annual review and serves before Council for adoption with this Annual Budget:
   - Property Rates Policy and By-law
   - Credit Control and Debt Collection Policy and By-law
   - Indigent Support Policy
   - Supply Chain Management Policy

   The following policy has been developed to assist in implementing the budget for 2014/2015 and serves before Council for adoption with this Annual Budget:
   - Virement policy

2.3 Municipal Manager's Quality Certificate

I …………………………………, Municipal Manager of Kouga Local Municipality, hereby certify that the annual budget and supporting documentation have been prepared in accordance with the Municipal Finance Management Act and the regulations made under the Act, and that the annual budget and supporting documents are consistent with the Integrated Development Plan of the municipality.

Print Name ____

Municipal manager of Kouga Local Municipality

Signature ____

Date ______________________________