



Municipal Financial Systems and Processes

This circular provides an update to municipalities and municipal entities regarding the ongoing investigation into local government financial systems and processes. This Circular augments the information and guidance provided in MFMA Circular No. 80 and must be read in the context of all the Municipal SCOAs Circulars issued to date, and MFMA Circular No. 57 and aims to provide further clarity on the transversal tender RT25-2016.

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1 Background

National Treasury issued MFMA Circular No. 80 on 8 March 2016, which in effect removed the “moratorium on ICT procurement”, put in place through MFMA Circular No. 57. The intention of MFMA Circular No. 80 is to ensure that municipalities going forward, when reviewing and/or considering compliance of systems of financial management and internal control, going forward, are empowered to do so in the most appropriate manner. In this regard it is advised that, given the imminent requirement to comply with the Standard Chart of Accounts for Local Government Regulations, 2014 (*m*SCOA Regulations), and the recently articulated business processes, municipalities are advised to:

- Avoid wasting public funds on unnecessary and fruitless ICT and internal control system changes;
- Conduct the appropriate level of assessments and/or ICT due diligence, if necessary, as envisaged and guided through Municipal SCOAs Circulars No. 5 and 6; and
- Assess the most economically effective approach to ensure that the municipality is compliant, from a systems perspective, with the requirements of the *m*SCOA Regulations as a first priority. Compliance with the business processes, as envisaged and specified in Annexure B of MFMA Circular No. 80.

In order to avoid unnecessary wastage of state resources, it is strongly recommended that municipalities first consider carefully whether any change of ICT-related systems of financial management and internal control are warranted. In the event that a material upgrade or change to the existing package of systems are indeed warranted, and cannot practically be

addressed economically through engagement with present service providers, then municipalities are reminded that due process should be followed. In the event that procurement is at all necessary, then municipalities are advised to compare system costs against offerings available in terms of the RT25-2016 transversal contract.

Since March 2016, engagement with practitioners revealed large-scale misinterpretation of the following paragraph of MFMA Circular No. 80 (Paragraph 8):

“The National Treasury acknowledges that metropolitan municipalities and secondary cities, in most instances, have the necessary skills and ability to deal with not only procurement but also highly technical aspects of financial management and internal control systems. In this regard, and with the exception of metropolitan municipalities and secondary cities, all other municipalities are highly recommended to make use of the transversal contract and associated panel of service providers for the supply of financial management and internal control systems once finalised. Should a municipality decide not to do so, it is required of them to formally write to the National Treasury (Chief Directorate: Local Government Budget Analysis) prior to going out on a supply chain management process, supplying clear reasons and motivation in support of the decision after which National Treasury will provide a written response and clear recommendations.”

It appears that local government practitioners across the affected sphere interpreted this paragraph to mean that the RT25-2016 transversal contract was an accreditation process of each and every system offering available to local government. Extending this notion further, it appears that local government practitioners also interpreted service providers listed in terms of the RT25-2016 tender process to imply that other established service providers already providing these services to municipalities for several years, to be incapable to continue providing these services. This was neither the intention of the RT25-2016 tender process, nor can the outcome of the process serve as any conclusion of this nature. The National Treasury hereby categorically state that the **RT25-2016 tender process was not an accreditation process but a procurement process with various obstacles and disqualifications in terms of normal supply chain management policy**, over-and-above ensuring that these systems are enabled for the implementation of mSCOA.

In addition it should be re-iterated that the purpose of the RT25-2016 tender process was to provide a clear set of systems specifications, reference pricing and contracting means for municipalities, where a systems upgrade was determined to be necessary; where other means

of complying with the requirements of the *mSCOA* Regulations and business process specifications for municipalities are not viable.

At no stage did this Paragraph 8 (of MFMA Circular No. 80 quoted above) imply or can it be construed to imply that the National Treasury requires any municipality to move away from its existing systems simply because such system(s) and/or vendors are not listed on the panel of RT25-2016 transversal contract service providers. On the contrary, Paragraph 3 of MFMA Circular No. 80 specifically guides that:

“The outcome of this research, which was aligned and informed by the ‘piloting’ of the mSCOA classification, has resulted in a comprehensive list of business processes that should be supported by system functionality (systems of financial management and internal control). Annexure B (System Specifications) to this Circular includes a detailed list of these business processes and will be further explained in this MFMA Circular. Importantly, municipalities need to evaluate the functionality of their current financial management and internal control systems against these business processes and technical specifications. If the outcome of the assessment is favourable, then municipalities would not necessarily need to replace their current financial management and internal control system. The service provider would however have to provide the municipality with guarantees to this effect.”

2 What Constitutes *mSCOA* Compliance

The RT25-2016 technical specification was designed to address not only the *mSCOA* requirements but also to list all the components needed to fully automate and accommodate the accountability cycle of municipalities (considering the current local government legal environment). Best Practices and optional requirements were discerned in this tender in order to clearly identify only the essential systems functionality. Optional systems features and functions have been identified as *non-regulated options* / add-ons. RT25-2016 also allowed for 3rd party integration as well as future developments. Through this approach the National Treasury allowed for a municipality to follow an evolutionary systems approach if such is preferred.

For avoidance of doubt, a municipality is not legally compelled or required to employ RT25-2016 when upgrading or replacing financial systems in municipalities. The intent of establishing the panel of vendors is to support interested and/or ill-equipped municipalities in their endeavour to procure these systems. Whether employing the RT25-2016 panel or not, municipalities are required to:

- (i) Have a systems-integrated IDP (integrated development plan) Module. All municipalities must submit by end of November 2016 their data strings to the National Treasury reflecting their IDP aligned to the Project, Function and Regional segments of the *mSCOA* chart version 6. Municipalities must provide proof of their preparations in this regard during October 2016 by means of draft data strings loaded onto the National Treasury LG database. Municipalities will need to utilise system functionality as a first indicator that a system is enabled for the implementation of *mSCOA*;
- (ii) Have a systems-integrated Budget Module. The next critical delivery is the tabling of the budget by 31 March 2017 and will require a municipality's system(s) to have budgeting functionality including but not limited to:
 - a. Organogram Budgeting;
 - b. Billing historical trends and new developments;
 - c. Asset maintenance plans;
 - d. Building rentals;
 - e. Fleet costs;
 - f. Loans, bonds and repayments;
 - g. Grants and subsidies;
 - h. Costing allocations; and
 - i. Long term forecasting and tariff modelling tools.

This is the **2nd measurement** of whether any system is enabled for the implementation of *mSCOA*; and

- (iii) Enable a municipality, with effect 1 July 2017, to transact across the seven segments of *mSCOA* with subsystems seamlessly integrating to the core financial system. This 3rd measurement criterion of *mSCOA* compliance will be tested by the National Treasury through its data extraction (across the 6 regulated *mSCOA* segments) from the information submitted by the municipality on/ before the 10th working day of August 2017. The municipality is therefore urged to already submit such data strings to the National Treasury to resolve any errors.

Due to these imminent deadlines, all municipalities are urged to consider the guidance on *mSCOA* compliance (set-out above) and engage with their respective systems vendors to duly conclude on the required processes.

Taking the evolutionary nature of the process into account, municipalities are advised to (where practically possible) consider all alternatives and are reminded that all systems which participated in the *mSCOA* piloting process, did have a successful piloting municipality. This

is a reminder again that the success of *m*SCOA compliance is therefore less dependent on the systems capability (many of which have shown the ability to comply with *m*SCOA requirements) and more dependent on municipalities embracing and ushering in the change with resolve and systematic planning.

3 Application of RT25-2016 – Transversal Awards

Municipalities requesting the National Treasury and Provincial Treasuries' comments in terms of Municipal SCOA Circular No. 6 (Annexure B) on the proposed way forward with regard to its existing package of system(s) will be required to illustrate, by supplying supporting evidence, that the municipality followed due process in terms of the guiding Municipal SCOA Circulars No. 5 and 6.

Considering that municipalities are required to prepare the 2017/18 MTREF aligned to the *m*SCOA Regulations in October/ November 2016, timeframes for making these decisions are limited. These matters do however, have to be considered and entails:

- (i) Tabling considerations and recommendations to the **municipal council**, in relation to *m*SCOA and systems compliance. Costs, benefits and risks should be thoroughly deliberated if necessary;
- (ii) Consider guarantees of compliance from either the existing or future vendor;
- (iii) Consider associated costs and follow due process, where a systems upgrade or replacement is considered the only viable option, when cancelling the existing service level agreement (SLA) including, whether support from the National Treasury and/ or Provincial Treasury is needed in this regard;
- (iv) We confirm that the municipality may procure directly from the panel of service providers on the RT25-2015 transversal tender. In this regard we advise that the municipality engage the Office of the Chief Procurement Officer in the National Treasury (to guide you, also to ensure due process in terms of the Municipal Supply Chain Management Regulations, the municipality's policies and minimum requirements for any proposed Service Level Agreement (SLA). This does not preclude a municipality procuring a service using SCM Regulation 32, as long as the service is aligned to the requirements of the Regulation;
- (v) Should the municipal council approve the procurement of a system from a service provider not on the RT25-2016 – transversal tender, the National Treasury and Provincial Treasury must be consulted as envisaged in Municipal SCOA Circular No. 6 prior to any such procurement process kicking off, including support in terms of the technical specification, the minimum requirements for any proposed service level

agreement (SLA), and pricing comparisons with the pricing available from tender RT25-2016. Thereafter the municipality must follow its supply chain process to procure the system; and

- (vi) Should council approve that the municipality remains with its current system (whether such system is on the RT25-2016 transversal tender of service providers or not), the municipality is advised to ensure comparable or more favourable pricing when compared with reference pricing specified in RT25-2016. The National Treasury and/ or Provincial Treasuries can be requested to assist in negotiating such pricing arrangements.

It should be noted that ensuring compliance of the municipality's ICT systems represents only one of several important steps step in the wider *m*SCOA reform objective of rendering data and business processes of municipalities uniform, transparent, consistent and relevant. These are envisaged to, ultimately, facilitate improved service delivery and community awareness of government's performance.

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