



## Budget Process 2005/06

This circular has been prepared to provide guidance to municipalities on the 2005/06 budget process in line with the Municipal Finance Management Act (MFMA). All provisions of the MFMA relating to the budget process will apply to all municipalities for the 2005/06 budget. Mayors should already have tabled a “*schedule of key deadlines*” in council by 31 August. Municipalities who have yet to comply are requested to treat this step as a high priority and to make the schedule of key deadlines public.

The IDP and budget process must be one process. It is considered that a well-run budget process that incorporates the IDP review will facilitate community input, encourage discussion, promote a better understanding of community needs, provide an opportunity for feedback and improve accountability and responsiveness to the needs of the local communities. It also positions the municipality to represent the needs of the community and to provide useful inputs to the relevant provincial and national department strategies and budgets for the provision of services such as schools, clinics, hospitals and police stations.

This circular deals only with the budget process and further information on: budget formats and content; the Service Delivery and Budget Implementation Plan (SDBIP); implementation and monitoring of the budget will be issued in the near future.

### Six steps to preparing a budget

There are six distinct steps to the preparation of a budget. It is important to mention up front that consultation on the budget occurs throughout the preparation cycle. Further information on consultation is provided towards the end of this circular.

|   | Step                | Process   |
|---|---------------------|---|
| 1 | <b>Planning</b>     | Schedule key dates, establish consultation forums, review previous processes  |
| 2 | <b>Strategising</b> | Review IDP, set service delivery and objectives for next 3 years, consult on tariffs, indigent, credit control, free basic services, etc and consider local, provincial and national issues, previous years performance and current economic and demographic trends etc |
| 3 | <b>Preparing</b>    | Prepare budget, revenue and expenditure projections, draft budget policies, consult and consider local, provincial and national priorities  |
| 4 | <b>Tabling</b>      | Table draft budget, IDP and budget related policies before council, consult and consider formal local, provincial and national inputs or responses  |
| 5 | <b>Approving</b>    | Council approves budget and related policies  |
| 6 | <b>Finalising</b>   | Publish and approve SDBIP and annual performance agreements and indicators  |

## **Step 1: Planning**

### **Coordination of the budget preparation process**

Section 21 of the MFMA is the primary provision relating to the municipal budget process. It requires the mayor to coordinate the processes for preparing the annual budget and for reviewing the Integrated Development Plan (IDP) and budget related policies. The mayor must table in council by 31 August (10 months before the start of the budget year) a schedule of key deadlines for various budget related activities as spelled out in section 21. The accounting officer is tasked by section 68 of the MFMA with assisting the mayor in developing and implementing the budgetary process. The process should provide for both internal (within municipality) and external (local community and other stakeholder) consultations.

An example schedule of key deadlines that may be tabled before council by the mayor is posted on the MFMA web site (see last page for contact details). Municipalities may adopt this example or adapt it by inserting the actual dates of planned meetings and include more detail. Please note that where a specific time frame is shown in the example schedule, it is a deadline requirement of the MFMA and must be complied with.

Municipalities are advised to make public a simplified version of the schedule to ensure the community is aware of the timelines, process and opportunities and to have input to the budget and IDP. A simplified version of the schedule should be placed in local newspapers, newsletters and the municipal website alerting the public that more information on the budget process is available on the municipal website and offices, including how the public can make an input into the budget process.

### **Review of previous budget process – budget evaluation checklist**

While the MFMA does not explicitly require a review of the previous budget process, it is strongly recommended that this undertaken in early August by the mayor and municipal manager before determining the new schedule of key deadlines. Such a review can provide information about what worked well, what didn't, where to improve and issues to address for legislative compliance.

A Budget Evaluation Checklist (BEC) template has been developed and will assist municipalities evaluate the budget process to facilitate eventual compliance with the MFMA, including previous budget preparation, tabling, approval and implementation. The BEC is available on the MFMA web site. When completing the checklist if a municipality answers "No" next to one of the items, this will serve as an indication of where more effort is needed to ensure compliance in the future. Immediate compliance with all provisions is not expected for the 2005/06 Budget, given that this is the first year of implementation of the new budget process. National Treasury will also use BEC information submitted by municipalities to monitor the progress of implementation across the country and target assistance where required.

Instructions for completing the BEC are as follows: answers must only be selected from the drop down list; all questions must be answered; for questions with multiple requirements, all requirements must be satisfied before scoring a "Yes"; each answer should be referenced to a page number in the supporting documentation; some questions require an answer for the tabled budget and the approved budget. Once completed please email to [lqdatabase@treasury.gov.za](mailto:lqdatabase@treasury.gov.za) with a subject heading of "Demarcation Code – Municipality Name – Budget Evaluation Checklist 2005".

Many of the municipalities piloting the municipal finance management and budget reforms have already submitted this checklist after the approval of the 2004/05 Budget. Other municipalities may find that their 2004/05 Budget does not comply with many of the questions. This is not cause for concern as these municipalities will generally have longer to comply with the MFMA and should utilise the checklist as a tool to identify areas for improvement.

We request all municipalities that have not already submitted the BEC to submit it by **30 November 2004**. Municipalities that have not as yet tabled their schedule of key deadlines, or wish to revise or improve their existing schedule, should ensure that they do so by 30 November.

### **Entities and the budget process**

Municipalities with entities will have a slightly more complex budget process and must ensure that the municipal budget process includes the budget process for each of its entities. The entity budget processes must be shaped by, and be within the framework of, the municipality's budget process. In particular, it will be necessary to ensure that the entities strategic plan and budget is consistent with the direction of the parent municipality's IDP and budget. The mayor of the parent municipality must therefore coordinate the overall budget process including that of its entities.

## **Step 2: Strategising**

### **Review of IDP and budget related policies**

The amendment to the Municipal Systems Act (MSA) and chapter 4 of the MFMA require that a revised IDP be adopted at the time of adopting the budget. Therefore, the process leading to the adoption of the 2005/06 budget and IDP must be incorporated into one process, together with the process for approving taxes, levies, user charges and budget related policies. This will ensure credible plans and budgets that are realistic and implementable. Furthermore, the IDP should be informing the entire budget, not just the capital budget, which has traditionally been the case.

Budget related policies include but are not limited to policies on: tariff setting; credit control / debt collection; indigents; cost recovery; investment; borrowing; cash management; spending delegations or authorisations; other supply chain considerations such as purchasing limits for sole supplier versus quote or tender; and so on. Some of these are required to be passed as a by-law and may require significant planning before changes can be made.

### **Internal consultations within the municipality**

The Budget process is consultative and the collective product of all within a municipality. If treated as an accounting exercise only, the mayor and accounting officer will have failed in their obligations to the municipality and the community. The budget process must involve all the senior managers and, importantly, it must be guided by the strategic priorities of the municipality.

The budget process should be preceded by a number of strategic and consultation processes within the municipality, involving the mayoral/executive committee and councillors. These processes are not legislated and are left to the discretion of each municipality. The consultation proposals outlined in this circular may not all be possible for the 2005/06 budget, but municipalities should strive to consider such consultations to the extent that these are still possible.

The internal strategic consultation should commence around September/October, with the mayor convening a meeting of the mayoral or executive committee and senior managers. The purpose is to determine the priorities of the municipality for the coming budget, taking into account the financial and political pressures facing the municipality. It should also consider what revisions should be considered to its current IDP. This process need not involve any non-executive councillors at this stage.

The above process ideally would culminate in a major council strategic workshop around the beginning of October involving the entire council (or if the council is too large, at least the chairpersons of all council committees). The purpose of the workshop is to gain understanding of budgetary pressures and to win the support of councillors to the budget priorities proposed by the mayor. It should be noted that at this stage the mayor and mayoral/executive committee determine the budget priorities – the council should not be asked to vote on such priorities and the mayor should strive to only win the broad support of the council. The actual priorities will be approved by the council when it approves the budget and revisions to the IDP at the end of the process.

The budget priorities are tentative at this stage and offer a basis for consulting with the community and stakeholders. It may be necessary for the mayor to revise the priorities following the consultation process.

### **External consultations with the community and other stakeholders**

There are two external consultation processes envisaged in the MFMA and Municipal Systems Act. The **first** external consultation process is informal, and open-ended, which begins around October and includes the following:

1. Public meetings with residents and small businesses in local communities - to identify and prioritise the greatest local needs (e.g. housing, water, electricity, recreation facilities, schools, clinics, streets and street lighting, refuse removal, social services and related issues, crime and functioning of local police stations, etc). To obtain the views of the community the council should consider the use of ward committees to gain an understanding of the issues in each ward;
2. Meetings with key stakeholders (e.g. residents associations, NGOs, business organisations) - to identify community and business needs and concerns, including the level of municipal tariffs and charges.
3. Consultations between the municipality and other municipalities, provincial and national departments and entities.

This first phase of informal or open-ended consultations ends when the mayor tables the budget and revisions to the IDP around the end of March.

The **second** external consultation process is more formal and takes place after the tabling of the draft budget, when the council convenes hearings on the draft budget and revisions to the IDP. The municipality must invite the public and stakeholder organisations to submit comments and submissions in response to the draft budget and revised IDP. Since specific proposals are contained in the draft budget and revised IDP the public comments and responses tend to be more directed to these proposals.

It should be noted that since municipalities are the closest interface between the community and government (all three spheres), they are best placed to consult communities on matters of

a national and provincial function, such as policing, schools, clinics and housing - in a sense they are the eyes and ears of national and provincial governments. In this respect, it is important the municipalities and/or councillors act as a channel between local communities and the relevant national and provincial government departments and entities feeding information into the relevant department's budget process.

The IDP is a co-ordinating tool that includes the needs of the community with respect to local services provided by all three spheres of government. It follows that the IDP of a municipality should differentiate between two sections – one part related to municipal functions and responsibilities and a second part relating to national and provincial responsibilities. The budget of the municipality can only fund the first part of the IDP related to municipal functions and services. The second part of the IDP requires the municipal manager to co-ordinate with national and provincial departments advocating on behalf of the local community.

### Step 3: Preparing

The preparation of the budget is a lengthy process spanning many months. It can be said to start in August at the time the mayor tables the schedule of key deadlines and conclude in June or early July when the mayor approves the Service Delivery and Budget Implementation Plan (SDBIP) and annual performance agreements with senior managers. In practice however, the budget preparation process is an ongoing function where processes and budget years will overlap. There are generally three different budget processes operating in parallel all the time - reporting on the past year (e.g. annual reports and audited financial statements), current year implementation, and preparations for the coming budget year.

Budget preparation includes the following processes:

- Winning support for the priorities that will shape the way budget allocations will be determined
- Integration of strategic objectives with budget allocations
- Appropriate planning and improved project management
- Assessing affordability of rates and service charges, and identifying poor households unable to afford such rates and charges;
- Accurate in the estimation of revenue and expenditure projections
- Consultation and review of national, provincial and local priorities
- Assessment of previous year performance and corrective action to be incorporated in the next budget

Whilst the technical preparation of the Budget is undertaken by the municipal manager, senior managers and chief financial officer, it is important that the mayor meet with the municipal manager and CFO on a monthly basis after the priorities are set, particularly during November, January, February and March. Such political oversight is necessary to guide officials and to assist in making the hard trade-offs necessary to determine the budget.

A key step in the budget process occurs at the end of January, when the mayor is required to table the annual report for the past year and the mid-year report on the current financial year. For example, on 31 January 2005, the mayor will be tabling the 2003/04 annual report, and will be submitting the mid-year report on the 2004/05 budget. This mid-year report will also inform the mayor and municipal manager on adjustments that need to be made to the 2004/05 current year budget. It is recommended that a *municipal adjustment budget* be tabled at the end of February 2005 which takes into account adjustments to be addressed in the current budget, such as under-collection of revenue, to address emergencies and adjustments in

national and provincial allocations (i.e. for the period 1 April 2005 to 30 June 2005). All the above considerations must be used to determine the coming budget for the 2005/06 budget year.

### **Previous performance**

Throughout the budget process, and specifically at key times, consideration should be given to the effect that previous performance will have on the medium term plan and the current and forthcoming budgets. This should include past year and current year information.

### **Municipal Infrastructure Grant (MIG)**

Municipalities are encouraged to produce a 3 year capital plan when tabling the draft budget. This is required to be disaggregated by municipal ward and reflect the MIG sector priorities to enable national and provincial transfers to flow directly to municipalities. The sector priorities in MIG refers to functions of water, sanitation, refuse, electricity, roads, public amenities, etc. This will allow for sector departments like, DWAF, DME and others to monitor progress in addressing backlogs, as reflected in the Division of Revenue framework for MIG. Moreover, it is a requirement that consultations on these capital plans be undertaken for water and sanitation, electricity with national sector departments about early November, and similarly for roads with provincial departments of transport.

Further information on the MIG framework may be found in the Division of Revenue Gazette.

## **Step 4: Tabling**

The draft budget and revised IDP must be tabled together in council no later than 1 April (90 days before the start of the budget year), together with the draft resolutions and budget-related policies. The accounting officer must immediately (on the same day) post the budget, revised IDP and all related documents onto the municipal website so that the budget is accessible to the public. The accounting officer must also immediately make available to the public hard copies of the budget and all other related documents and send (hard and electronic) copies to the National and provincial treasuries and other relevant organs of state (e.g. water affairs, mineral and energy, water boards and all other municipalities within the same district).

Once the budget is tabled the local community must be invited to make written submissions to the council on the budget and to make representation at the council hearings. Key stakeholders like national and provincial departments (e.g. treasuries, local government, water, environment, health) should also be invited to submit written comments to the hearings. The Council may also wish to host special sessions with community organisations, business organisations and public sector institutions prior to convening the hearings on the budget. Pilot municipalities that have followed this route have gained from such experiences.

The council is required to have hearings on the budget before it considers the budget for adoption. Such hearings can take the form of various committee hearings and should be convened soon after tabling the budget. The hearings may need to extend over a number of weeks, after which a full council meeting should be convened to consider and make recommendations arising out of the hearings process. The council must consider all the submissions and representations received during its hearings process. The mayor must be given an opportunity to respond to the recommendations (at that or a subsequent council meeting), and where necessary, to make revisions and amend the tabled budget.

The diagramme below illustrates the sequence of events to table the proposed budget and amendments to the IDP.

### Tabling the budget – suggested timing

| MARCH   |     |     |     | APRIL   |     |     |     | MAY  |     |     |     |  |  |  |  |
|---|-----|-----|-----|---|-----|-----|-----|--|-----|-----|-----|--|--|--|--|
| Wk1   | Wk2 | Wk3 | Wk4 | Wk1   | Wk2 | Wk3 | Wk4 | Wk1  | Wk2 | Wk3 | Wk4 |  |  |  |  |
| <p><b>Table</b> municipal and entity budgets, resolutions, SDBIP, IDP revisions and budget related policies</p> |     |     |     | <p>Call for <b>public submissions</b>, council to have meetings with key stakeholders</p> |     |     |     | <p>Council <b>hearings</b> and Council meeting to consider submissions</p> |     |     |     | <p>Council <b>meeting</b> - mayor to submit amended budget</p> |  |  |  |

## Step 5: Approving

After the mayor has responded to the recommendations and made amendments to the draft budget, the full council must meet to consider the budget for approval no later than 31 May (30 days before the start of the budget year). Ideally the council should consider approving the budget, and related policies, at the same meeting that the mayor tables any revisions/amendments. If the council is not able to approve the budget, the speaker/mayor must ensure that further council meetings are convened every week thereafter to ensure that the budget is approved before the start of the budget year. Failure to approve the budget before the start of the budget year will have serious operational consequences for the municipality (as no payments can be made without an approved budget) and could result in a section 139 constitutional intervention in terms of sections 25 and 26 of the MFMA. Should the municipality fail to approve the budget before the start of the budget year, the mayor must inform the MEC for Finance that the budget has not been approved.

## Step 6: Finalising Plans to Implement the Budget

This step of the budget process involves the finalisation of plans to implement the budget, through the approval of the Service Delivery and Budget Implementation Plan (SDBIP) and the performance agreements for the municipal manager and other senior managers for the coming financial year. While the MFMA requires this to happen within 28 days after the approval of the budget it is recommended that draft SDBIP and performance agreements be tabled with the budget and considered in conjunction with the budget approval, if possible.

The recommended approach to prepare the SDBIP is to develop implementation plans for each vote in the budget (note the definition of “vote” – MFMA section 1). The vote implementation plans would show:

- monthly projections of revenue by source and expenditure by vote;
- quarterly projections of measurable performance indicators; and service delivery targets.

The SDBIP approved with the budget or shortly after would be a summary of these plans. Further guidance on the preparation of an SDBIP is provided in a separate MFMA circular.

A delegations policy of spending authority on budget votes is critical for successful budget implementation and subsequent monitoring and evaluation. It is important that delegations required to give effect to sections 79, 82 and 106 of the MFMA are addressed.

Once the budget is finalised, the process for implementation (or preparing to implement) commences. Further information on implementation will be provided in subsequent circulars.

## **Consultation**

Both the MSA and MFMA require extensive consultation with the local community for important decisions like budgets, tariff setting, borrowing, IDPs, performance systems, annual reports, etc. The process of consultation is set out in chapter 4 of the MSA as amended (sections 21A and 21B have been added). Sections 21, 22 and 23 of the MFMA deal specifically with consultation on the budget.

Section 16 of the MFMA requires the budget resolutions; proposed revisions to the IDP; budget related policies; and other required supporting documentation to be tabled before a full council meeting by 1 April (i.e. at least 90 days before the start of the budget year). This allows adequate time for consultation prior to approval of the budget and ensures that councillors are aware of the budget implications so they can consult with their constituents.

The MFMA also requires consultation with relevant government departments and municipalities affected by the budget. Consultation with provincial and national sector departments such as, Agriculture, Health, Housing, Education, Welfare, Water Affairs and Mineral and Energy Affairs will ensure improved co-operative governance between the spheres. It is recommended that municipalities contact their Provincial Treasuries to coordinate consultation meetings with relevant provincial departments. This engagement will ensure better coordination, alignment and resource allocation from provincial and national governments.

District and local municipalities must consult each other when finalising plans and budgets to ensure that allocations between them are aligned, priorities are addressed and implementation is executed during the year. Historically, delays in project approval, spending and implementation have occurred undermining service delivery due to a lack of this early consultation. District municipalities must consult all municipalities within its area and must notify relevant municipalities of projected allocations, for the next three budget years, no later than 2 March (120 days prior to the start of the budget year). These allocations must be published with the draft municipal budget and will be audited by the Office of the Auditor-General to ensure consistency of amounts reflected in the transferring municipality and the recipient municipality.

The MFMA requires that municipalities submit their tabled and approved budgets to National Treasury and the relevant provincial treasury. Provincial treasuries will become progressively more involved with the monitoring and support of municipal finance management as capacity is being developed in this area over the next year. Planning is underway to ensure that submission of information is streamlined and requests for information from government departments are not duplicated.

Municipalities will need to keep abreast of developments in the various sectors to ensure their budgets for water, sanitation, electricity etc are well informed. Municipal IDPs and budgets should inform and be informed by the development plans of sector departments to ensure a coordinated approach to infrastructure planning and service delivery. Furthermore, municipalities should have a good knowledge of all grants from government departments including their objectives, conditions and medium term allocations as gazetted. To assist municipalities in proper planning and budgeting a commitment has been obtained from all role-players to provide information on allocations in provincial budgets and the annual Division

of Revenue Act around February and March that reflect transfers to municipalities over a multi year period.

Hence, it is critical that early on in the budget process, the mayor coordinates a schedule of key deadlines for all of the required meetings, workshops, community forums etc and makes this schedule public so that those being consulted are aware of their opportunities for input into the IDP and budget process.

## Conclusion

This circular is the first of several to be issued to guide municipalities and municipal entities on the 2005/06 budget and focuses on the early preparatory work for the budget process. The budget process will take time to evolve and each year after budget approval the mayor should lead a process of review to assess what worked well, what did not and whether or not the process complied with all of the relevant legislation. These lessons should then be factored into the next planning and budgeting cycle.

Both the Budget Evaluation Checklist and the example *schedule of key deadlines* can be downloaded from the National Treasury website (see contact details below).

A copy of the Budget Evaluation Checklist is to be returned via email to [lqdatabase@treasury.gov.za](mailto:lqdatabase@treasury.gov.za) by **30 November 2004**.

This circular should be tabled before full council and the mayor should immediately begin work on the coordination of the 2005/06 budget process if not already commenced. The municipal manager should ensure this circular is distributed to all senior managers and municipal entities.

## Contact



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