

LGBA SPECIAL PROJECT WORK STREAM

MUNICIPAL FINANCIAL PLANNING & BUDGET REFORM

Budgeting for Free Basic Services

Presenter: EC Le Roux Technical Advisor : LGBA, National Treasury | 23 September 2016
Contact Detail: Cell 083 287 4905
Email: [Eduard.leRoux @treasury.gov.za](mailto:Eduard.leRoux@treasury.gov.za)



national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

Documents

The following documents have been consulted regarding budgeting & accounting for Free Basic Services (FBS)

- Circular 51 – par 6.4 Revenue & Revenue Foregone
- Circular 58 – par 6.8 & 6.9 Cost of FBS vs Revenue Cost of Free Services
- GRAP 9 Revenue From Exchange Transactions
- GRAP 23 Revenue From Non-exchange Transactions (Taxes And Transfers)
- IGRAP 1 Applying The Probability Test On Initial Recognition Of Revenue
- FAQ on FBS - ASB website
- 2016 DoRA

Budgeting for Free Basic Services – FBS vs Subsidised Services

Free Basic Services

The basic services component of Equitable Share Formula

This component helps municipalities provide free basic **water, sanitation, electricity and refuse removal services to households that fall below an affordability threshold.**

The monthly amount provided for each service is detailed in Table W1.24 and includes an allocation of 10 per cent for service maintenance costs.

Table W1.24 Amounts per basic service allocated through the local government equitable share

	Allocation per household below affordability threshold (R per month)			Total allocation per service (R million)
	Operations	Maintenance	Total	
Energy	63.87	7.10	70.97	7 830
Water	96.58	10.73	107.31	11 839
Sanitation	76.72	8.52	85.24	9 403
Refuse	64.30	7.15	71.45	7 882
Total basic services	301.47	33.50	334.97	36 953

Source: National Treasury

Budgeting for Free Basic Services – FBS vs Subsidised Services

Subsidised Services (Revenue Foregone)

- Assessment rates to Indigent households (Not FBS as per the definition of the Equitable Share Formula)
- Exemptions, reductions and rebates and impermissible values in excess of section 17 of MPRA
- FBS in excess of the norms as per DoRA
- Funding – Rates and service charges (Council policy decision)

A1 Schedule Areas - Budgeting for Free Basic Services – Current Position

FBS subsidised from the basic services component of the Equitable Share

Basic services component of ES provides a subsidy of R334.97 per month in 2016/17 (R313.76 in 2015/16) for households below the monthly household income of R2 300 for the cost of providing basic services: **6kl Water, 50 Kwh electricity, refuse removal, sanitation**

- Subsidy as per national standard**
 - FBS => SA9
- Subsidy above national standard (additional subsidy)**
 - Revenue forgone – subtract on SA1
- Free Basic Alternative Energy supplied to indigent households – Where electricity is not available**
 - Non-Cash grant SA21 => A4
- Free Basic Electricity to indigent households – where Eskom holds the license**
 - Payment to Eskom – Cash grant SA21 => A4

A1 Schedule Areas - Budgeting for Free Basic Services – Current Position

Property rates (Not FBS as per the definition of the Equitable Share Formula)

Impermissible values as per MPRA

- Section 17 (1) of MPRA (R15 000, 30%PSI, public worship, etc.).
- Section 2 of Regulation on Ratio Between Residential/Non-Residential Category of Property (Government Gazette 33016, 12 March 2010)
 - Do not levy – Tariff Adjustment - Not revenue forgone Higher values than impermissible values
- Impermissible values higher than MPRA - Revenue forgone – subtract on SA1

Rebate/reduction/exemption in terms of sect 15(1) of MPRA to all ratepayers of a particular category (property or owners) as defined in subsection 15(2)

- Revenue forgone – subtract on SA1

Rebate/reduction/exemption in terms of sect 15(1) of MPRA to some ratepayers or an individual of a particular category (property or owners) as defined in subsection 15(2)

- Revenue forgone – subtract on SA1

A1 Schedule Areas - Budgeting for Free Basic Services – Current Position

Table SA9 - Detail of Free Basic Services (FBS) provided

- FBS – formal settlements –**
 - Subtracted on SA1 - Elect, Water, Sanitation & Refuse (formula linked)
 - Linked to A10 – Cost of FBS
- FBS – Informal settlement**
 - Linked to A10 – Cost of FBS

Table A10 – Cost of FBS

- Totals for formal & informal FBS on SA9 - linked to Table A10 – Cost of FBS**
- Excludes Rate (not FBS in terms of Free Basic Services component of Equitable Share)**

Table A10 – Revenue Cost of Subsidised Services provided

- Revenue foregone**
 - Rates, Electricity, Water, Sanitation & Refuse - (linked from Table SA1)
- Rebates**
 - Municipal Housing - rental rebates – (manual capture)
 - Housing - top structure subsidies – (manual capture)
 - Other – (manual capture)

A1 Schedule Areas - Budgeting for Free Basic Services – Current Position

Table SA1 – Deductions from Revenue

- Revenue foregone
 - Rates – amounts in excess of impermissible values – section 17 of MPRA
 - Elect, Water, Sanitation & Refuse – amounts in excess of national norms or amounts to non-indigent households
- FBS to Indigent Households
 - Elect, Water, Sanitation & Refuse as per the national norms – linked to SA1 from SA9

Table SA21 – Cash & Non-Cash Grants to Groups of Individuals & Institutions

- Free Basic Alternative Energy supplied to indigent households – Where electricity is not available
 - Non-Cash grant SA21 => A4
- Free Basic Electricity to indigent households – where Eskom holds the license
 - Payment to Eskom – Cash grant SA21 => A4

A1 Schedule Areas - Budgeting for Free Basic Services – Current Position

Choose name from list - Supporting Table SA1											
Description	Ref	2012/13	2013/14	2014/15	Current Year 2015/16				2016/17 Medium Term		
		Audited	Audited	Audited	Original	Adjusted	Full Year	Pre-audit	Budget	Budget	Budget
R thousand											
REVENUE ITEMS:											
Property rates	6										
Total Property Rates											
<i>less Revenue Foregone (exemptions, reductions and rebates and impermissible values in excess of section 17 of MPRA)</i>											
Net Property Rates		-	-	-	-	-	-	-	-	-	-
Service charges - electricity revenue	6										
Total Service charges - electricity revenue											
<i>less Revenue Foregone (in excess of 50 kwh per indigent household per month)</i>											
<i>less Cost of Free Basis Services (50 kwh per indigent household per month)</i>		FROM Table SA 9									
Net Service charges - electricity revenue		-	-	-	-	-	-	-	-	-	-
Service charges - water revenue	6										
Total Service charges - water revenue											
<i>less Revenue Foregone (in excess of 6 kilolitres per indigent household per month)</i>											
<i>less Cost of Free Basis Services (6 kilolitres per indigent household per month)</i>		FROM Table SA 9									
Net Service charges - water revenue		-	-	-	-	-	-	-	-	-	-
Service charges - sanitation revenue											
Total Service charges - sanitation revenue											
<i>less Revenue Foregone (in excess of free sanitation service to indigent households)</i>											
<i>less Cost of Free Basis Services (free sanitation service to indigent households)</i>		FROM Table SA 9									
Net Service charges - sanitation revenue		-	-	-	-	-	-	-	-	-	-

A1 Schedule Areas - Budgeting for Free Basic Services – Current Position

Choose name from list - Table A10 Basic service delivery measurement										
Description	Ref	2012/13	2013/14	2014/15	Current Year 2015/16			2016/17 Medium Term Revenue & Expenditure Framework		
		Outcome	Outcome	Outcome	Original Budget	Adjusted Budget	Full Year Forecast	Budget Year 2016/17	Budget Year +1 2017/18	Budget Year +2 2018/19
Cost of Free Basic Services provided - Formal Settlements (R'000)	8									
Water (6 kilolitres per indigent household per month)		-	-	-	-	-	-	-	-	-
Sanitation (free sanitation service to indigent households)		-	-	-	-	-	-	-	-	-
Electricity/other energy (50kwh per indigent household per month)		-	-	-	-	-	-	-	-	-
Refuse (removed once a week for indigent households)		-	-	-	-	-	-	-	-	-
Cost of Free Basic Services provided - Informal Formal Settlements (R'000)		-	-	-	-	-	-	-	-	-
Total cost of FBS provided		-	-	-	-	-	-	-	-	-
Revenue cost of subsidised services provided (R'000)	9									
Property rates (tariff adjustment) (impermissable values per section 17 of										
Property rates exemptions, reductions and rebates and impermissable		-	-	-	-	-	-	-	-	-
Water (in excess of 6 kilolitres per indigent household per month)		-	-	-	-	-	-	-	-	-
Sanitation (in excess of free sanitation service to indigent households)		-	-	-	-	-	-	-	-	-
Electricity/other energy (in excess of 50 kwh per indigent household per month)		-	-	-	-	-	-	-	-	-
Refuse (in excess of one removal a week for indigent households)		-	-	-	-	-	-	-	-	-
Municipal Housing - rental rebates										
Housing - top structure subsidies	6									
Other										
Total revenue cost of subsidised services provided		-	-	-	-	-	-	-	-	-

GRAP Reporting Framework

GRAP 9 - Revenue From Exchange Transactions

No definition or guidance with regard to treatment of FBS

Measurement of revenue

.15 Revenue shall be measured at the ***fair value of the consideration received or receivable***.

.16 The amount of revenue arising on a transaction is usually determined by agreement between the entity and the purchaser or user of the asset or service. It is ***measured at the fair value of the consideration received or receivable taking into account the amount of any trade discounts and volume rebates allowed by the entity***.

.17 ***In most cases, the consideration is in the form of cash or cash equivalents*** and the amount of revenue is the amount of cash or cash equivalents received or receivable.

GRAP Reporting Framework

GRAP 23 Revenue From Non-exchange Transactions (Taxes And Transfers)

Definitions

.05 The following terms are used in this Standard with the meanings specified:

Tax expenditures are preferential provisions of the tax law that provide certain taxpayers with concessions that are not available to others.

.71 Taxation revenue shall not be grossed up for the amount of tax expenditures.

.72 Tax expenditures are foregone revenue, not expenses, and do not give rise to inflows or outflows of resources – that is, they do not give rise to assets, liabilities, revenue or expenses of the taxing government.

GRAP Reporting Framework

I-GRAP 1

Scope

.04 This Interpretation of the Standards of GRAP addresses the manner in which an entity applies the probability test on initial recognition of:

(a) exchange revenue in accordance with the Standard of GRAP on Revenue from Exchange Transactions, and

(b) non-exchange revenue in accordance with the Standard of GRAP on Revenue from Non-exchange Transactions (Taxes and Transfers).

.06 **This Interpretation of the Standards of GRAP does not deal with:**

(a).....

(b).....

(c) exchange or non-exchange transactions where there is no intention to charge for all or some services. Examples include goods and services provided to indigent consumers or households or rebates deducted on the provision or acquisition of certain goods or services.

GRAP Reporting Framework

FAQ's on the Standards of GRAP

Is revenue foregone recognised in the statement of financial performance?

1. In the **public sector**, entities frequently provide goods and services to consumers for free or at subsidised amounts, while rebates or similar reductions may be granted on taxes or other fees due.
2. **Questions** have been raised about whether these subsidies, rebates or similar reductions should be recognised as revenue. IGRAP 1 Applying the Probability Test on the Initial Recognition of Revenue, states the following:
 3. This Interpretation of the **Standards of GRAP does not deal with:**
 - c. exchange or non-exchange transactions where there is no intention to charge for all or some services. **Examples** include goods and services provided to indigent consumers or households or rebates deducted on the provision or acquisition of certain goods or services.
 4. IGRAP 1 clearly only applies to those amounts that the entity intends to collect. As entities do not intend to collect the revenue related to the subsidised goods and services or other rebates, these amounts should not be recognised as revenue.

GRAP Reporting Framework vs Equitable Share Policy Implementation

GRAP Reporting Framework

- ❑ Indigent subsidies for basic services (FBS), rebates or similar reductions should not be recognised as revenue
 - transfers in kind to households
 - should be treated as revenue forgone
- ❑ Subsidised services (rebates, concessions or reductions) – should be treated as revenue forgone
- ❑ GRAP reporting framework - Municipalities need to comply

Equitable Share Policy Implementation

- ❑ Equitable share not a conditional grant
- ❑ Structure of the local government equitable share formula - DoRA
 - First part of the formula consists of the **basic services component**, which provides for the cost of free basic services for poor households.
- ❑ **Reporting** on policy implementation increasingly important – **schedule A10**

GRAP Reporting Framework vs Equitable Share Policy Implementation

From policy implementing perspective

Cost of Free Basis Services – schedule A10

- ❑ Subsidies and rebates to indigent households to be disclosed separately –
 - Supporting budget schedules
 - enable data extraction for reporting

Revenue Cost of Subsidised Services – schedule A10

- ❑ Revenue forgone other than indigent subsidies and rebates to be disclosed separately –
 - supporting budget schedules
 - enable data extraction for reporting

Principles

- ❑ All indigent accounts are billed for all services monthly
- ❑ Indigent tariffs should be calculated at the level of the cost of providing the service to bring the cost of the subsidy in line with the DoRA allocation
- ❑ Indigent accounts are then subsidised monthly
 - passing a subsidy (credit) on the account
- ❑ “*Revenue Forgone – FBS*” subsidy is disclosed separately on the supporting budget tables and will not be disclosed as a non-cash transfer in the Statement of Financial Performance but will be treated as revenue foregone
 - Subsidy passed on the indigent account is funded by an equal contribution from the Equitable Share – Accounting Treatment mSCOA ??
- ❑ “*Revenue Forgone – Subsidised Services*” is disclosed separately on the supporting budget tables will be treated as revenue foregone
 - Funding will not be from the equitable share but from rates and service charges – Accounting Treatment mSCOA ??

A1 Schedule Areas – Possible Accounting Treatment

- ❑ **Contra accounts** – Item Revenue & Item Expenditure – Zero effect when preparing AFS mSCOA v6
- ❑ Split of cost of FBS as a % based on the composition of its cost and allocation of each component to “**Less expenditure allocated to FBS**” in the Financial Performance – Difficult to achieve as it would require detail breakdown of the cost of FBS which municipalities may not have
- ❑ Allocate total cost of FBS to “**Less expenditure allocated to FBS**” in the Financial Performance – NB show as one amount
- ❑ Process cost of FBS & rebates as a **movement through debtors** in the Financial Position
- ❑ **Operational Project**
- ❑ Treat it as **non-financial information** - not in mSCOA chart

Thank You