



Supply Chain Management: Enhancing compliance and accountability

The Municipal Finance Management Act (No. 56 of 2003), (MFMA) requires that the resources of municipalities and municipal entities are used effectively, efficiently and economically.

This circular aims to enhance compliance, improve accountability and transparency, update measures required to combat fraud, promotes transparency in supply chain management practices in municipalities and municipal entities as required by regulation 2.1(b) of the Municipal Supply Chain Management Regulations.

A number of circulars have been issued since the MFMA came into effect to explain supply chain management reforms and assist in its implementation in municipalities and municipal entities. This circular must be read in conjunction with previous circulars on supply chain management.

Supply Chain Management compliance and implementation weaknesses have been highlighted in recent audit findings. These practices at municipalities and municipal entities are impacting negatively on sound financial management, weakening the spirit and ethos of the MFMA and affecting service delivery. These include the circumvention of official competitive bidding processes, among others.

It is therefore imperative that accounting officers of municipalities and municipal entities establish mechanisms to urgently identify the risks and weaknesses facing their respective supply chain management environments with the aim of introducing improved mitigation strategies and internal processes to address these weaknesses.

It must be emphasized that the relevant treasuries are committed to assisting municipalities and municipal entities to improve the status of their financial management.

Government has also elevated the combating and prevention of corruption as an output in Outcome 12. The Minister of Finance has therefore established a Multi-Agency Working Group to coordinate and investigate corruption related to supply chain management practices across government.

The measures below are therefore intended to provide municipalities and municipal entities with guidelines to improve accountability and transparency and to ensure value for money in the procurement of goods, services and/or infrastructure projects.

Guideline on the implementation of Demand Management and the submission of Procurement Plans in respect of advertised competitive bids

The “Guidelines on the Implementation of Demand Management” (Annexure A) aims to provide accounting officers of municipalities and municipal entities with a general understanding of the procedures to be followed when implementing demand management and the compilation of procurement plans.

The objective of this guide is to assist municipalities and municipal entities with the planning for the procurement of goods, service or infrastructure projects in a proactive manner and to move away from merely reacting to purchasing requests.

Accounting officers of municipalities may, upon request, make available to the relevant treasury a procurement plan containing all planned procurement for the financial year, in respect of the procurement of goods, services and infrastructure projects which exceed R200 000 (all applicable taxes included) per case as described in the Supply Chain Management: Guide for Accounting Officers. This procurement plan must be approved by the accounting officer or his or her delegate.

Accounting officers of municipal entities must submit the procurement plans to the accounting officer of their parent municipality.

All user departments are required to submit their procurement plans to the Head Supply Chain Management in the municipality or municipal entity to improve planning and management of resources.

The relevant information should preferably be furnished in the format contained in the Procurement Plan Template enclosed as Annexure B. Municipalities/municipal entities may customize and utilize the template with minimum changes necessary to address the municipality’s/municipal entity’s specific issues. The template should however cover the minimum information reflected in Annexure B to this Circular.

Publication of names of bidders in respect of advertised competitive bids, above the threshold value of R200 000 (all applicable taxes included)

After the closure of any advertised competitive bid, municipalities and municipal entities must, further to information to be published in terms of section 75 of the MFMA, publish on their websites, the reference number of the bid, the description of the goods, services or infrastructure project, names of all bidders, the B-BBEE status level of contribution of all bidders, where applicable, the local content percentages of the goods offered and where practical, total price of the bids, by all bidders that submitted bids in relation to that particular advertisement. Copies should be made available at municipal offices and libraries. The municipality / municipal entity should endeavor to publish the aforementioned information within ten (10) working days after closure of the bid and it must remain on the website of the municipality or municipal entity for at least thirty (30) days. See below regarding information to be posted on the municipal website, after awarding of bids.

Verifying the names and identity numbers of directors / trustees / shareholders of companies, enterprises, closed corporations and trusts against the relevant municipal staff structure

The Municipal Bidding Document (MBD 4) "*Declaration of Interest*" attached as Annexure C has been augmented to require bidders to submit the names of their directors / trustees / shareholders, their individual identity numbers, personal tax reference numbers and employee numbers of those who are in the service of the state as defined in the Municipal Supply Chain Management Regulations as part of their bid submissions. A shareholder is defined as a person who owns shares in the company and is actively involved in the management of the company or business, and exercises control over the company. This is applicable for all written price quotations, advertised competitive bids, limited bids, unsolicited bids and proposals.

Accounting officers of municipalities and municipal entities are required to utilize the attached revised MBD 4 form when inviting bids and to verify the identity numbers of the directors / trustees / shareholders of the preferred bidder(s) against the municipality's or municipal entity's staff establishment in order to determine whether or not any of the directors / trustees / shareholders are employees of the municipality or municipal entity. Furthermore, other specific information to be disclosed relating to any other official in the service of the state, as defined in the SCM regulations will also be utilized during the evaluation process.

The review of all disclosures referred to in the previous paragraph must take place during the bid evaluation process. If a bidder / director / trustee / shareholder declares that he / she is in the employ of the state, the municipality or municipal entity must not make any award to such bidder as this is prohibited in terms of the SCM regulations.

Municipalities and municipal entities may not have access to all HR databases across government and entities to verify upfront whether a prospective bidder is in the service of the state as defined in the SCM Regulations. It is therefore understood that municipalities and municipal entities will not be able to verify this information but will rely on the content and disclosures made by bidders.

Should it come to light that a false declaration was made by the bidder after the municipality had awarded the bid, the contract must be immediately suspended and payments made, recovered. False declarations by bidders can be viewed as a criminal offence and charges must be laid by the municipality with the South African Police Services for further investigation. Details will be reported to Council at its next meeting and information contained in the Annual Report of the municipality.

In the event that the Auditor-General detects irregular expenditure during the audit process as a result of possible false declarations and subsequent awards based on those declarations, the municipality or municipal entity will be informed of such irregular expenditure. The municipality or municipal entity will be required to rectify this matter by instituting the necessary remedial measures, by investigating the matter, recovering the funds spent, instituting disciplinary proceedings against those liable for such actions and possible criminal prosecution as may be appropriate. The accounting officer must also apply the remedial measures contained under

“Termination for Default” in the General Conditions of Contract. The expenditure at this stage will not be classified as irregular expenditure.

In the event that the same expenditure is detected in the following year’s audit and the remedial measures referred to above were not instituted, the expenditure will then be classified as irregular expenditure.

The measures contained in MFMA Circular 43 relating to the restriction of suppliers in terms of the Preferential Procurement Regulations are still relevant. Municipalities and municipal entities are therefore encouraged to; once again, familiarize themselves with the content of this circular.

The revised MBD 4 attached to this Circular replaces the MBD 4 issued in terms of MFMA Circular 25 dated 30 October 2005.

In addition to the above, accounting officers of municipalities and municipal entities must ensure that:

- (a) the preferred bidders’ tax matters are in order;
- (b) the municipal rates and taxes or municipal charges owed by the preferred bidder or any of its directors to the municipality or municipal entity, or to any other municipality or municipal entity, are not in arrears for more than three months;
- (c) the names of the preferred bidders and their directors / trustees / shareholders are not listed on the Register for Tender Defaulters and the Database of Restricted Suppliers. These databases are now available on the National Treasury website; and
- (d) a process is conducted to determine whether the preferred bidders have the capability and ability to execute the contract.

Definition of “Principal Shareholder”

Regulation 44(b) of the Municipal Supply Chain Management Regulations prohibits a municipality or municipal entity from making any awards, if that person is not a natural person, of which any director, manager, principal shareholder or stakeholder is a person in the service of the state. Although the regulation is clear, an elaboration of the terms ‘principal shareholder or stakeholder’ is provided to assist interpretation and application.

Whilst many have initially pointed to 50% + 1% as explaining who is a principal shareholder, there are other permutations that must be considered when determining the definition. Any interpretation of regulation 44 without due consideration of the problem the regulation seeks to remedy will always be defective, as it risks being incomplete. One has to consider a scenario where the shareholders have equal shareholding in the entity, say two shareholders holding 50% each or 4 shareholders holding 25% each. Does this imply non-existence of a principal shareholder? Certainly not, because careful reading of regulation 44(b) refers to any principal shareholder, which implies that there could be more than one principal shareholder. This would be the case where the shareholding is equal irrespective of the number of

shareholders. It could also happen that one shareholder has the largest holding, though not more than 50%, in comparison to other shareholders either directly or indirectly (e.g. through another company).

Consideration should also be given to the issue of influence, 'control' and voting rights at meetings, especially decision making at annual, general or board meetings. This is particularly important in cases where there is equal shareholding but one of the members or shareholders have been nominated or appointed as chairperson and the articles of association give such person the power to make final decisions where there is no agreement amongst members or even to provide the decisive vote where there is a tie. In this instance, this person can be regarded as the principal shareholder for purposes of regulation 44(b) of the Municipal Supply Chain Management Regulations.

It is evident from the above that due consideration for the problem which the regulation seek to remedy is given. To this end one needs to be mindful of the implied assumption in the regulation and that is that any person in the employ of the state could, by that reason, be conflicted in the procurement process. This is exactly what section 112(1)(j) of the MFMA is trying to manage by stating that the supply chain management policy of a municipality must address the compulsory disclosure of any conflicts of interests prospective contractors may have in specific tenders and the exclusion of such prospective contractors from those tenders or bids.

The remedy is therefore to manage that interest which is likely to unduly influence the decision-making process during the procurement of goods or services. It should therefore follow that any procurement policy that does not give effect to the potential conflict of interest, as denoted by shareholding, is thus defective. It is therefore important that a case by case analysis be undertaken as it would provide the most appropriate response to the meaning of principal shareholder.

Verification by the Chief Financial Officer prior to advertisement of bids above R10 million

The following information must be submitted by the senior manager responsible for the Vote to the CFO **prior** to the public advertisement of any bids in excess of R10 million (all applicable taxes included):

- (a) Proof that budgetary provision exists for procurement of the goods, services and/or infrastructure projects;
- (b) Any ancillary budgetary implications related to the bid, for example, if the project is for the acquisition of a municipal asset, does budgetary provision exist for the operation of the asset, maintenance costs relating to the asset, administration costs and rehabilitation/renewal costs;
- (c) Any multi-year budgetary implications, for example, if a project will take more than one financial year, the estimated expenditure per financial year.

Goods, services and/or infrastructure projects above the value of R10 million (all applicable taxes included) may only be advertised after the CFO has verified in writing that budgetary provision exists for the commencement of the particular project.

Requirements may not be deliberately split into parts or items of lesser value merely to avoid the information being submitted.

Verification from the Chief Financial Officer prior to the award of contracts above the value of R10 million

Contracts above the value of R10 million (all applicable taxes included) may only be awarded to the preferred bidder after the Chief Financial Officer has verified in writing that budgetary provision exists for the acquisition of the goods, infrastructure projects and/or services and that it is consistent with the Integrated Development Plan.

Confirmation of bidding process for bids in excess of R10 million (all applicable taxes included)

Internal audit units must compile risk based audit plans, review internal control measures, and ensure that supply chain management, including the requirements of this Circular, is sufficiently and adequately covered in the annual coverage plan.

Internal auditors must be alert to fraud risks and design audit procedures and indicators that would reasonably assist in preventing and detecting potential or actual fraud and corruption.

During competitive bidding and adjudication processes or before the award of a contract, the accounting officer may, at his or her discretion, specifically request the internal audit function to carry out audit procedures and provide an opinion on compliance of the bidding process with the Municipal Supply Chain Management Regulations.

Where bids involve internal audit service, the audit of the bidding process may be outsourced to an independent external service provider or internal audit function of another organ of state, subject to the oversight of the audit committee.

The accounting officer may, at his or her discretion, decide to have a specific contract audited by external service providers prior to the award of the contract.

Legal sound written contracts or service level agreements

Accounting officers must ensure that all written contracts or service level agreements that are entered into by their respective institutions are legally sound. This measure is aimed at avoiding potential litigation and minimizing possible fraud and corruption.

Such contracts or agreements must be actively managed in order to ensure that both parties (the municipality or municipal entity and the contractors) meet their respective obligations.

Publication of awards in respect of advertised competitive bids (above the threshold value of R200 000)

Section 75 (1) (g) of the MFMA prescribes that the accounting officer of a municipality must place on the website all supply chain management contracts above a prescribed value. Municipal Supply Chain Management Regulation 23 (c) requires of accounting officers of municipalities and municipal entities to publish their bid results on the website. This relates to bids above R200 000 (including all applicable taxes).

The following information on the successful bids must be made available on the municipal or municipal entity's website:

- (a) Contract numbers and description of goods, services or infrastructure projects;
- (b) Names of the successful bidder(s) and the B-BBEE level of contribution claimed;
- (c) The contract price(s), and;
- (d) Brand names and dates for completion of contracts.

Records of such publication must be retained for audit purposes.

Placing of orders for payment in another financial year

Accounting officers of municipalities and municipal entities are prohibited from deliberately placing orders for goods, services and/or infrastructure projects from suppliers, receiving such goods, services and/or infrastructure projects and arranging with suppliers for such goods, services and/or infrastructure projects to be invoiced and paid for in another financial year.

The prohibition above does not apply to multi-year contracts and projects adopted over multi-years in terms of MFMA sections 19 and 33.

Management of expansion or variation of orders against the original contract

It is recognized that, in exceptional cases, an accounting officer of a municipality or municipal entity may deem it necessary to expand or vary orders against the original contract.

The expansion or variation of orders against the original contract has, however, led to wide scale abuse of the current SCM system.

In order to mitigate such practices, accounting officers of municipalities and municipal entities are advised that, from the date of this Circular, contracts may be expanded or varied by not more than 20% for construction related goods, services and/or infrastructure projects and 15% for all other goods and/or services of the original value of the contract. Municipal Councils and Board of Directors of municipal entities are required to amend their supply chain management policies accordingly. Furthermore, anything beyond the abovementioned thresholds must be reported to council or the board of directors.

Any expansion or variation in excess of these thresholds must be dealt with in terms of the provisions of section 116(3) of the MFMA which will be regarded as an amendment to the contract.

The contents of the above paragraph are not applicable to transversal term contracts, facilitated by the relevant treasuries on behalf of municipalities and municipal entities and, specific term contracts. The latter refers to orders placed as and when commodities are required and at the time of awarding contracts, the required quantities were unknown.

Payment within 30 days

The contents of MFMA Circular 49 issued in 2009 with regards to the payment of suppliers within 30 days are confirmed. Municipalities and municipal entities are encouraged to familiarize themselves with the content of that Circular.

Transitional arrangements and auditing of this Circular

The Circular is also applicable to those bids that are in the process of being finalized. For example, if a bid was advertised prior to the issuance of this Circular and has not yet been awarded, the contents of this Circular will apply.



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Annexure A: Guide on the Implementation of Demand Management

Annexure B: Procurement Plan Template

Annexure C: Municipal Bidding Document (MBD 4) “Declaration of Interest”