**1. REPORT OF THE SELECT COMMITTEE ON APPROPRIATIONS ON THE ROLL-OVER OF MUNICIPAL INFRASTRUCTURE GRANT FUNDS FOR THE 2010-2015 FINANCIAL YEARS, DATED 24 MAY 2016**

1. **Introduction and background**

The purpose of the Municipal Infrastructure Grant (MIG) is to support municipalities with regard to the provision of basic services such as water, sanitation, roads, and recreational facilities. The Grant is administered through the Department of Cooperative Governance and Traditional Affairs, who coordinates its activities in collaboration with other stakeholders through various structures. The Grant primarily contributes to Outcome 9 of the Medium Term Strategic Framework, namely ensuring a responsive, accountable, effective and efficient developmental local government system.

The Division of Revenue Act requires that any conditional grant funds which are not spent at the end of the municipal financial year must revert to the National Revenue Fund, unless the receiving officer proves to the satisfaction of the National Treasury that the unspent allocation is committed to identifiable projects, in which case the funds may be rolled over. The Act further provides that unspent funds from the preceding financial year may be rolled over when activities planned to be completed, by the end of that year have not been completed but are close to completion and such funds have been committed to identifiable projects.

The management and use of rolled-over funds is a topical issue within the public funding system as it is generally representative of planning and spending inefficiencies, which ultimately results in delayed service delivery.

The Committee invited National Treasury to do a presentation on the roll-over of MIG funds for the past five years, including the following issues:

* MIG rollovers as a percentage of total MIG allocation for all municipalities for the five year period;
* Monitoring of expenditure of rolled over funds and outputs delivered;
* How successful the recently introduced stricter clauses with respect to the roll-over application process have been in reducing roll-over applications; and
* Challenges experienced and remedial measures put in place.

The above briefing was made to the Committee during a meeting on 17 May 2016.

1. **Presentation by National Treasury**
   1. **Legislative requirement and background to roll-over process**

In terms of Section 216 of the Constitution of the Republic of South Africa, National Treasury (NT) is required to prescribe measures to establish both transparency and control in each sphere by introducing generally recognised accounting practice; uniform expenditure classifications; and uniform Treasury norms and standards. Section 30 of the Public Finance Management Act (PFMA) provides for an adjustment to be passed following an approval of a roll-over of a national allocation. Section 30 of the Municipal Finance Management Act (MFMA) provides that an appropriation of an annual or adjustment budget lapses to the extent that those funds are unspent, except where an appropriation for that expenditure is made for a period of more than one year. Section 28 of the MFMA authorises the spending of unspent funds from a previous financial year, and Section 22 of the Division of Revenue Act (DoRA) provides for all unspent conditional grants to revert to the National Revenue Fund, unless permission is granted by National Treasury to roll over the unspent funds into the next financial year.

The National Treasury regulation provides further guidelines on how roll-overs should be conducted, including the following:

* Payment for capital assets may only be approved to finalise assets in progress;
* Savings on transfers and subsidies may not be rolled over for purposes other than originally voted for; and
* Savings on compensation of employees may not be rolled over.

The National Treasury issues annual circulars to guide municipalities on how roll-over applications should be submitted to the National Treasury and how unapproved roll-overs should revert to the National Revenue Fund. The DoRA provides that, should municipalities fail to repay unapproved or unspent conditional grants, the funds be offset against their respective conditional or unconditional grants. Further, to avoid funds being offset, a periodical repayment of unspent funds can be arranged on behalf of municipalities.

The first roll-over clause was included in the 2004/05 DoRA. This was after the promulgation of the MFMA in 2003, which in the main gave effect to Section 216 of the Constitution. Between 2005 and 2008, National Treasury focussed on establishing the uniform Treasury norms and standards and uniform expenditure classifications. In 2009, the Municipal Budget Reporting and Regulation were approved by the Minister of Finance and the regulation paved the way to allow for recalling unspent conditional grants sitting with municipalities. In cleaning historical data, National Treasury undertook a process of verifying all unspent funds from 2005 until 2009. This process was concluded in 2011 and it is now an annual occurrence.

* 1. **Procedure for applying for roll-overs**

Municipalities must submit roll-over applications or required information by 31 August of each year. If this deadline is missed, the application will not be considered. Municipalities are required to supply Treasury with the following information:

* A formal letter signed by the accounting officer addressed to Treasury requesting the roll-over of unspent conditional grants in terms of Section 22(2) of the DoRA.
* A list of projects that are linked to the unspent funds and evidence that work has commenced on each of the projects, including the following:

1. Proof that the project tender was published and the period for tender submissions closed before 30 June; or
2. Proof that a contract for delivery of the project was signed before 30 June.

* A progress report on the implementation of each of the projects.
* The amount of funds committed to each project, and the conditional allocation from which the funds come.
* Reasons why the grant(s) were not fully spent in the year that it was originally allocated as per the DoRA.
* An indication of the time period within which the funds are to be spent.
* Proof that the Chief Financial Officer of the municipality is permanently appointed.

When considering roll-over requests from municipalities, all unspent cash-backed grants should be classified only as “Cash and cash equivalents”. This number must also reconcile with the cash flow statements. All conditional grants must be spent in line with the conditions for which they are set and must not be invested.

* 1. **Monitoring expenditure on roll-overs**

National Treasury, in consultation with transferring officers and provincial departments, considers rollover requests. Transferring officers are responsible for monitoring expenditure on roll-overs against projects on a monthly and quarterly basis, and to monitor registered projects and verify their delivery. Treasury requires municipalities to report separately on the spending of conditional grant funds that are rolled over, and monitors the expenditure on roll-overs in terms of Section 71 of the MFMA and the DoRA – through monthly reports by both municipalities and transferring officers. Annual Financial Statements are used to verify expenditure on roll-overs, to prevent approval of a roll-over of a roll-over.

* 1. **Municipal Infrastructure Grant roll-overs**

The MIG allocations are biased towards provinces without access to basic services, and is linked to backlogs in mainly water and sanitation.

Table 1 below reflects the total amount of MIG funds allocated to each province over the five year period from 2010 to 2015; the total amount rolled over per province as well as the total amount unspent during the same period. In addition, each province’s percentage of the total MIG allocation is reflected, as well as the percentage of unspent funds each province is responsible for.

Table 1:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Total MIG for 2010 - 2015** | | | **Total percentages** | |
| **Province** | **MIG allocation** | **MIG roll-over** | **MIG unspent** | **Percentage of allocation per province** | **Unspent percentage per province** |
| Eastern Cape | 13 549 655 655 | 783 245 | 226 248 | 18.87% | 7.45% |
| Free State | 4 528 970 | 217 803 | 94 813 | 6.31% | 3.12% |
| Gauteng | 2 118 266 | 87 444 | 30 407 | 2.95% | 1.00% |
| KwaZulu-Natal | 14 376 144 | 812 038 | 210 448 | 20.03% | 6.93% |
| Limpopo | 14 625 192 | 2 072 045 | 1 192 276 | 20.37% | 39.27% |
| Mpumalanga | 9 327 608 | 1 180 512 | 195 996 | 12.99% | 6.46% |
| Northern Cape | 2 255 686 | 310 565 | 193 555 | 3.14% | 6.38% |
| North West | 6 832 082 | 1 073 927 | 882 874 | 9.52% | 29.08% |
| Western Cape | 4 174 562 | 82 826 | 9 263 | 5.82% | 0.31% |
| **TOTAL** | **71 788 165** | **6 620 405** | **3 035 880** | **100%** | **100%** |

From the above table it can be seen that the Eastern Cape, KwaZulu-Natal and Limpopo receive the highest MIG allocation, while Gauteng, the Northern Cape and the Western Cape receive the lowest. Limpopo and the North West account for almost 70 per cent of the total of R3 billion unspent MIG funding over the five year period from 2010 to 2015.

The National Treasury reported that the unspent MIG as a percentage of the total allocation has increased over the period, from 2.5 per cent in the 2010/11 financial year to 7.05 per cent in the 2014/15 financial year. In this regard North West leads with an average of 13 per cent unspent MIG annually, followed by Limpopo, with an average of 9 per cent unspent MIG over the five year period.

The National Treasury reported that it had instituted stricter conditions for roll-overs, including linking the submission of Annual Financial Statements (AFS) to the Auditor-General (AG) with the roll-over approval process. This has led to an increased number of AFS being submitted to the AG on time and also improved the quality of AFS submitted for audit. This has resulted in improved audit outcomes for municipalities. In addition, it has led to improved compliance by municipalities with the DoRA; improved accountability in municipalities; and also improved overall performance of the MIG – 95 per cent compared to 77 per cent four to five years back.

* 1. **Challenges and remedial measures**

The National Treasury reported the following challenges in terms of the roll-over of the MIG:

* Non-submission of Annual Financial Statements (AFS), without which Treasury can only rely on monthly reports and a wrong decision could potentially be taken.
* Insufficient motivation, as required by the circular, means that Treasury might not be able to tell what projects are being referred to.
* The restating of AFS by municipalities causes delays in the process of approval, leading to approval being received too late for municipalities to spend the funds.
* Grants are often not properly disclosed in the AFS.
* Municipalities sometime have a negative bank balance, but still show unspent funds. The unspent funds are thus not cash-backed.
* Contrary to National Treasury’s instructions that interest, VAT and retention amounts should never form part of a roll-over, in some cases municipalities still include these in the unspent amounts.
* Municipalities report inadequately on approved roll-overs or not at all; and sometimes incorporate roll-over expenditure in the current allocation.
* Late submission of roll-over applications and multiple applications for the same grant.
* The biggest challenge is that Treasury is unable to verify the expenditure against approved projects on the ground. There have been instances where the situation on the ground was found not to match what was on paper.
* Municipalities sometimes request a roll-over of a roll-over, which Treasury cannot approve.

The National Treasury further reported that the following remedial actions were being taken:

* MIG funds of non-performing municipalities are stopped and reallocated to fast-spending municipalities, where possible within the same district or province.
* Where possible, funds are re-channelled via the relevant district municipalities, to ensure that contractors are paid.
* In some instances, the allocation is converted from a direct to an indirect allocation in order to address capacity and supply chain management constraints within municipalities. Municipalities are supported in this regard by the Municipal Infrastructure Support Agency (MISA) and other agencies.
* MFMA budget circulars provide municipalities with guidance for roll-over applications.
* Provincial DoRA workshops are conducted.
* Provincial Treasuries provide support to delegated municipalities.
* Support is provided in the form of deployments through the Municipal Finance Management Internship Programme (MFMIP).
* Treasury allows for repayment arrangements if a municipality is unable to repay the money immediately.
* One-on-one sessions are conducted with affected municipalities.

1. **Observations**

3.1 The MIG allocations to provinces exclude the eight metropolitan areas (City of Cape Town, eThekwini, City of Johannesburg, City of Tshwane, Nelson Mandela Bay, Buffalo City, Mangaung and Ekurhuleni). Instead, the metros receive the Urban Settlements Development Grant as well as the Integrated City Development Grant. For this reason the Committee will also look into the grant/s spending of metropolitan municipalities in the third term.

3.2 The MIG is administered through the Department of Cooperative Governance and Traditional Affairs, who coordinates its activities in collaboration with other stakeholders through various structures. This calls for a collaborative approach in monitoring and support to municipalities to ensure effective spending of the Grant. The Committee will for this reason engage the Department of Monitoring and Evaluation in order to strengthen the cooperative government and intergovernmental relations in support of municipalities.

3.3 The Committee noted with appreciation that measures applied by the National Treasury for approval of roll-overs have not only improved the grant spending from 77 per cent to 95 per cent but have also translated into improved reporting by municipalities. The Committee will, however, as part of its oversight look into how the MIG spending translated into improved access to basic services as well as the reduction of backlogs.

3.4 Situations where municipalities request roll-overs of roll-overs are cause for concern on the credibility of information provided when requests for roll-overs are made.

3.5 The incidences of roll-overs that are not cash-backed are indications of, among others, cash-flow problems, budgeting and spending challenges, and that MIG allocations might be used for other purposes.

3.6 Late submission for requests for roll-overs are indications of poor planning that must not be condoned.

3.7 There is an urgent need to address the inability of the National Treasury to verify the roll-over expenditures against the approved projects on the ground. The Committee will ensure that MIG-funded projects are targeted during oversight visits.

3.8 The incidences of supplying inaccurate information should be seen as financial misconduct and be treated as such, where applicable. This includes re-statement of Annual Financial Statements (AFS), failure to properly disclose grants in AFS, use of grants for other purposes and failure to follow the National Treasury’s instructions with regard to unspent grant funds.

3.9 There are challenges with regard to supply chain management processes in municipalities that might require the intervention of the Chief Procurement Officer.

1. **Recommendations**
   1. The Limpopo Provincial Treasury as well as the Provincial Department of Cooperative Governance should, within three months after the adoption of this Report by the House, report to the Committee on measures put in place to ensure that municipalities within the province are able to spend their Municipal Infrastructure Grant allocations as expected.
   2. North West Provincial Treasury as well as the Provincial Department of Cooperative Governance should, within three months after the adoption of this Report by the House, report to the Committee on measures put in place to ensure that municipalities within the province are able to spend their Municipal Infrastructure Grant allocations as expected.
   3. The National Treasury should, within three months after the adoption of this Report by the House, provide the Committee with the list of municipalities with persisting under-spending of roll-overs and also indicate measures in place to support such municipalities.
   4. The National Treasury should, within three months after the adoption of this Report by the House, provide the Committee with the list of municipalities with persisting inaccurate reporting on their roll-overs and also indicate any remedial action taken by appropriate authorities.
   5. The National Treasury should, within three months after the adoption this Report by the House, provide the Committee with a list of municipalities whose roll-overs were not backed by cash and the Treasury should also indicate any remedial steps taken.

Report to be considered.