

NATIONAL COUNCIL OF PROVINCES

QUESTION FOR WRITTEN REPLY

QUESTION NUMBER 424

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Mr Tboho Edwin Chaane (MP) to ask the Minister of Finance:

- (1) Whether the Minister is aware of the huge investments done by some Municipalities, if yes, whether such is allowed and why should municipalities be allowed to make investments when they are supposed to deliver essential services, if not would the Minister consider investigating the matter.
- (2) Whether the Minister is aware that part of the reason for under spending of Conditional Grants for Municipalities is their drive to cash-in on the interest rates generated through grants to cushion their own revenues, if yes, what is the Ministry doing at the moment to deal with the root causes of this problem?

[CW478E]

REPLY:

- (1) I presume the Honourable Member is referring to cash investments by municipalities and not investments in service delivery infrastructure – although the two are closely related.

Municipalities are required to manage investments in terms of the MFMA Municipal Investment Regulations (Government Gazette No. 27431 of 1 April 2005). These Regulations require each municipal council to adopt an investments policy that is consistent with the requirements of the MFMA and the Regulations. The Regulations also set out the standard of care that the municipal manager, or his or her delegated investment managers, needs to exercise when making investments on behalf of the municipality. These are as follows:

Standard of care to be exercised when making investments

Investments by a municipality or municipal entity, or by an investment manager on behalf of a municipality or entity –

- (a) must be made with such judgement and care, under the prevailing circumstances, as a person of prudence, discretion and intelligence would exercise in the management of that person's own affairs;
- (b) may not be made for speculation but must be a genuine investment; and
- (c) must in the first instance be made with primary regard being to the probable safety of the investment, in the second instance to the liquidity needs of the municipality or municipal entity and lastly to the probable income derived from the investment.

There are many perfectly legitimate reasons why municipalities make investments. In many instances, they are required to do so by law – for instance municipalities are required to maintain cash-back reserve funds for the future rehabilitation of municipal waste landfill sites. In other instances, municipalities are required in terms of their contractual agreements with lending institutions to maintain so-called 'sinking funds' in order to pay off loans when they fall due. It is also good financial management practice for municipalities to maintain certain cash-backed reserve funds, for example for the renewal/replacement of large infrastructure items, customer deposits, self-insurance etc. It is also prudent for municipalities to maintain sufficient cash to cover at least three months worth of normal operating expenditure – in order to cushion them against unexpected events such as the slow-down in the economy, natural disasters or even in certain instances rates-boycotts which are threatening certain municipalities.

Indeed the National Treasury is concerned that most municipalities have in recent years run down or depleted their cash reserves (and the related investments) to the extent that they are now dangerously exposed. The recent cash crisis in some municipalities partly highlights the risks associated with inadequate cash reserves, and the dire consequence of service delivery failure that ensues.

- (2) The spending of conditional grants by municipalities in the 2009/10 financial year shows a significant improvement over previous years. As a matter of fact, spending of municipal conditional grants has improved from 77.5 per cent in 2006/07 to 97.9 per cent in 2009/10. Municipalities are to be congratulated on this outcome. The problem that the honourable member is referring to is therefore on the decline. This is in part because of the steps that the National Treasury has instituted in order to ensure that municipalities spend conditional grant funds allocated to them within the relevant financial year:

- (a) The Division of Revenue Act provides that any unspent conditional grant funds have to be returned to the National Revenue Fund at the end of the financial year. In the previous financial year National Treasury enforced this provision and it is now standard practice. If municipalities do not spend their conditional grant funds, they stand to lose them;
- (b) The Division of Revenue Act provides for an upfront payment schedule agreement between the municipality, transferring national officer and National Treasury. This payment schedule provides that each municipality will only receive its allocations in tranches as and when it can demonstrate spending of that which has already been given to them; and
- (c) The Division of Revenue Act also empowers me as the Minister of Finance to delay or stop the transfer of conditional grant funds to any municipality should the municipality, amongst other factors, under spend. Therefore, if a municipality is not spending its conditional grant funding in accordance with the provisions of the DORA, future transfers can then be stopped.

The interventions described above are to incentivise municipalities to spend conditional grant allocations within the financial year in which they are allocated. There is now very little space left for municipalities to hoard unspent conditional grants in order to reap the interest on them – they are now spending them as intended: this is clearly reflected in the latest spending numbers for conditional grants.