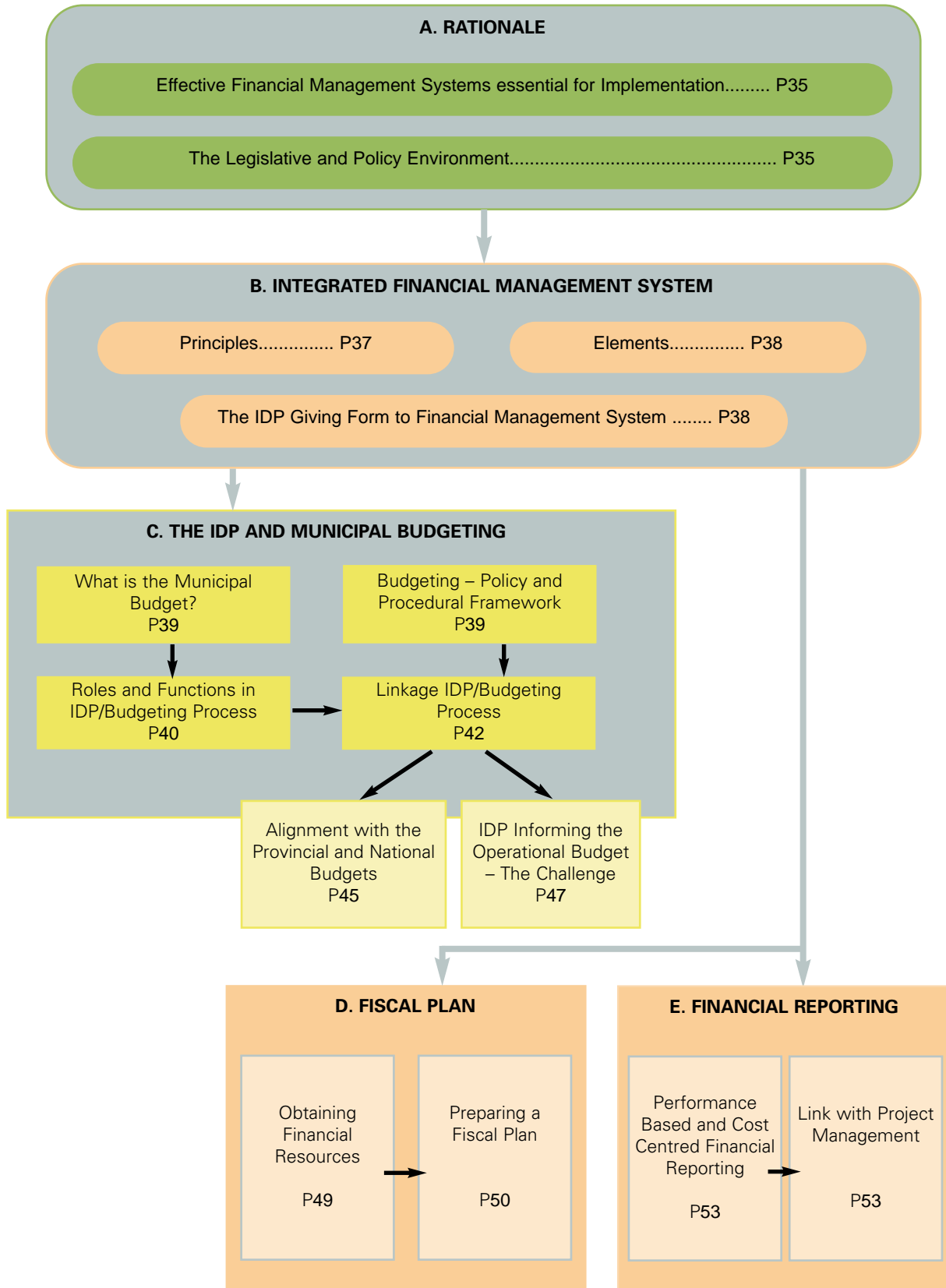


SECTION 2: INTEGRATED FINANCIAL MANAGEMENT – A PRIMARY LINKAGE OF PLANNING TO DELIVERY

ROUTE MAP FOR THIS SECTION



A. RATIONALE

1. EFFECTIVE FINANCIAL MANAGEMENT SYSTEM – ESSENTIAL FOR IMPLEMENTATION

Implementation and service delivery within the Local Municipality require resources. In almost all instances the resources cost money. Your Municipality has a responsibility to ensure that it accesses financial resources for its development objectives and then uses them effectively and responsibly.

Structuring the most effective ways of doing this constitutes the financial management system of your Municipality. Success in implementing the IDP is heavily dependent upon the quality of this system.

It is not an isolated internal system. Since Municipalities are dependent upon other spheres of government and the broader external environment for some of their resources, their financial management systems must fit within a range of external and internal processes and time spans.

2. PURPOSE OF THIS SECTION

This section deals with the key parts of the financial management system directly linking the IDP and implementation.

It also examines the existing state of the important linkages between the financial management, IDP's and the government's budgeting processes.

It is not a total guide to the development of a financial management system. Such detailed guidance is available elsewhere. It is particularly intended to help non-financial management staff involved in the IDP and its implementation to understand relevant aspects of financial management.

3. LEGISLATIVE AND POLICY ENVIRONMENT

Since 1994 the South African Government has taken a number of legislative and policy initiatives to change the focus and quality of financial management in local government.

All these have strengthened the linkage between planning and implementation. The following legislation provides the important guidelines for local government financial management.

Municipals Systems Act 2000 – This Act provides the principles, mechanisms and processes necessary to enable Municipalities to provide the developmental delivery for which they are responsible. It specifically highlights the use of Integrated Development Planning in defining and detailing the Municipality's priority delivery programme and its crucial function in giving form to Municipal budgets. The legislation gives the framework for the IDP methodology. The methodology binds the process for Integrated Development Planning with municipal budgeting and links it to structured programme and project financial management.

The Act specifically states that the **Integrated Development Planning** "forms the policy framework and general basis upon which the annual budgets must be based" (Chap 5, Section 25 1c).

Inter Governmental Fiscal Relations Act 1997 – This Act provides the framework that permits the implementation of the sharing of state financing between the 3 spheres of government in support of Section 214 of the Constitution. It does not stipulate the precise split but provides for the institutions to do this on an annual basis.

Division of Revenue Act – This is the annual Act that defines the horizontal and vertical distribution of national finances. It provides the detail of the split of the national finances for the following financial year. It is crucial for the Municipality as it provides information on a significant income stream that it requires to provide effective service.

The annual Act is supported by accompanying Government gazettes that elaborate the conditions and responsibilities in receiving and using the allocated finances.

Provincial Division of Revenue Acts – Each Province must also pass the relevant legislation to spell out its vertical and horizontal disbursement of finances available to the province. This informs the directing of finances across different provincial government programmes and departments. It also defines financial allocations to Municipalities. In its interlinkage with other legislation it should take some of its form from the priorities emerging from the IDP processes within Municipalities.

The Financial and Performance Management Act – This is a national Act that provides the conditions for the effective management of the use of state financial resources. It is specifically directed at the national and provincial spheres but contains many of the principles and systems that are considered good practice and a precursor to similar relevant legislation for the Local Government sector.

The Municipal Finance Management Bill, 2001 – This is the Bill presently under consideration in parliament that will provide the financial management framework for Local Government. It importantly defines:

- the powers of National Treasury in relation to Local Municipalities
- the opening and management of bank accounts
- management of cash and investments
- disposal of assets
- acquisition and disposal of interest in outside entities
- approach to municipal budgeting
- dealing with short and long term debt
- roles and responsibilities of Councillors and Municipal Officers
- municipal entities and their scope and constraints
- financial statements and auditing
- dealing with financial misconduct
- dealing with financial disasters in Municipalities.

The draft Bill contains sections specifically defining the close relationship of Municipal budgeting to the IDP e.g. “The annual budget of a Municipality must indicate how it gives effect to the IDP of the Municipality over the three coming budget years, and how the IDP may need to be revised given the budgetary resources and spending commitments.” (Municipal Financial Management Draft Bill – Chapter 4 16 – 5).

Until this Bill become law Municipal Financial Management is governed by the Act below.

“The Local Government Transition Act, Act 209” of 1993 (Section 10G) and **“The Local Government Transition Act Second Amendment (Act 97 of 1996)”**.

This Act deals with the specific provision that govern the following issues for Local Municipalities:

- Effective and sound municipal administration
- Accounting records; audit and accountability
- Budgets
- Procurement and tender policies
- Borrowing
- Income of Municipalities
- Investments
- Funds
- Assets
- Creditors

INFORMATION BOX

The principle provisions of these acts and their relevance to improved Local Government and financial management are dealt with in concise and understandable manner in the booklet:

“Financial Management and Planning for Local Government” – issued by
The Department of Provincial and Local Government.

Medium Term Expenditure Framework (MTEF) – This is a significant guide to future approaches by national government to financing its programmes including those designated in Local Government. It requires all three spheres of government to do budget projections for 3-year periods. It importantly assists the different spheres of government to establish 3-year budgets with actual commitments for year 1 and indicative figures for the following 2 years.

Its purpose is to increase the scope for longer term planning and more coherent delivery over a number of years. The 3-year MTEF process is now policy for Local Government. It takes its detail from the 5 year Financial Plan of the IDP and the annual IDP reviews.

Other Policy Guidelines

In addition to the legislation there are a number of linked circulars, guides and gazettes that help to detail and specify the broad framework. We turn to some of these in the different sections.

EMPHASIS BOX

In considering the Financial Management Systems the government's emphasis is upon the **allocation of scarce resources to government priorities** in ways in which they are **used effectively to deliver the prioritised services** within a framework of **proper accountability**.

B. INTEGRATED FINANCIAL MANAGEMENT SYSTEM

1. INTEGRATED FINANCIAL MANAGEMENT SYSTEM – PRINCIPLES

The Fiscal Service Commission outlines the following important themes underpinning financial management reforms of particular relevance to Local Municipalities:

- The introduction of medium term expenditure frameworks to promote improved planning and greater stability and continuity in the budgeting process, and to overcome some well known problems associated with annual incremental budgeting.
- The development of systems and mechanisms aimed at forging closer links between strategic planning, budgeting, financial and performance management systems.
- The move towards an outputs, outcomes, programme-based and results-orientated approach to budgeting, rather than the traditional input-based approach.
- The decentralisation of greater managerial autonomy at operational level, to promote flexibility and responsiveness to local needs.
- The introduction of incentives and controls to ensure that greater managerial responsibility and autonomy is matched by accountability for the achievement of centrally established goals and priorities.
- The increasing use of computerised information systems as a key component of budgeting and financial management.
- The introduction of skills development programmes to upgrade the capacity of Financial Managers and staff, as well as to make non-finance staff more knowledgeable and aware of their financial responsibilities.
- The promotion of greater transparency and accountability to the public in budgetary matters.
- The introduction of improved systems for financial monitoring and review.

While at national level there is much progress in introducing legislation, policy and procedures to turn this into action to date, the progress in the field of Local Government has been limited.

Its major form starts to come together in the responsibilities within the legislation described above and significantly in the application of the Systems Act with its stress on Integrated Development Planning and Performance Management.

So what should a Municipality seeking good practice be doing?

- Well-developed financial management policy and procedures that integrate the fiscal planning, with budgeting, disbursement, financial control and organisational performance management.
- Ensuring that in the budgeting both capital and operational inputs are linked with defined outputs and outcomes.
- That the managers responsible have the responsibility and incentives to ensure that the financing is efficiently directed at the developmental priorities.
- That the financial management is linked to cost centres that reflect the cost of inputs against the defined outputs.

While the present legislative and policy environment doesn't oblige Local Municipalities to adopt best practice, it does not prevent Municipalities wanting to do so from proceeding.

So now lets
consider
the key elements
of a good Financial
Management
System

2. ELEMENTS OF FINANCIAL MANAGEMENT SYSTEM

FINANCIAL MANAGEMENT SYSTEM	FUNCTIONS	ELEMENTS
	1. Obtaining financial resources and managing assets	– The revenue management plan
	2. Planning the allocation of resources	– The 3 year Medium Term Expenditure Framework – The 5 year business plan within the IDP – The annual municipal budget – Capital – Operational – 5 year investment plan
	3. Managing the flow of income and expenditure	– Cash flow income and expenditure plan – Income and expenditure reports – Procurement system
	4. Reporting on use of financial resources	– Cash flow/budget report – Annual financial report – Audited financial report – Reports to provincial and national government – Reports to other grant or loan providers
	5. Monitoring and evaluating the use of resources	– Financial spend and outputs – Financial spend and outcomes

3. THE IDP GIVING FORM TO GOOD FINANCIAL MANAGEMENT

While the IDP gives important structure to the financial management mechanisms of the Municipality, it does not, in itself, structure the total Financial Management System to ensure implementation. Additional planning and structuring is required outside of the IDP process to achieve this.

In addition both the internal IDP process and other activities require close linkage with external policies, procedures and actions that impact directly on the Municipality's financing.

The support of good financial planning and management is at the heart of the contribution of IDP process and particularly the integration it forges with:

- project costing;
- fiscal planning;
- 5 year financial plan;
- capital and operational budget development.

While the thread of financial planning weaves through the whole IDP process, it is particularly strong in the development of the 5-year financial plan, the fiscal plan and the annual budgeting process. The detailed contribution of key activities of IDP to budgeting and financial management are dealt with below.

This Section of the Manual does not deal with all the elements of the Financial Management System. This is better covered in its entirety in other documents specifically prepared for South African Municipalities. It concentrates on the following elements that are central to ensuring that the IDP is implemented:

- Budgeting
- Fiscal Plans
- Cost Centre Financial Management as important for effective financial resource control of inputs.

C. THE IDP AND MUNICIPAL BUDGETS

1. WHAT IS THE ANNUAL MUNICIPAL BUDGET?

The Municipal budget is a legal requirement of all Municipalities. It provides the plan for the appropriation of finances for the implementing of the Municipality's activities.

It also provides the financial framework in which all the resources are allocated to achieve the Municipality's objectives within a given year. There are two components that are finally integrated into a total budget:

- Capital
- Operational

DEFINITION BOX

What are Capital and Operational Budgets?

Capital Budget – The capital budget refers to the amounts that are allocated to spend on acquiring or developing Municipal assets that generally have an expected lifespan or use period of at least 3 years e.g. purchase of Municipal vehicle, development of new clinic buildings.

Operational Budget – These are the amounts allocated to pay for the running costs of the Municipality covering both its direct and support services e.g. salaries, rental, electricity, telephone, repairs projects for assets.

In most Municipalities in South Africa the operational budgets are usually 4 or more times larger than the capital budgets.

2. POLICY AND PROCEDURAL BUDGETING FRAMEWORK

Under the existing legislation preparing the Municipal budget and the IDP are separate processes that are closely linked; interacting together and informing each other.

The two link closely as tools that help Municipalities achieve their developmental responsibilities. In doing so they meld the planning relationship between the Municipality's proposed delivery programme and the annual budget.

The IDP linked to the budget process meets the important principles articulated in national budgeting policy:

- Closely integrates the strategic, organisational and financial aspects of the policy process in regard to the dimensions of planning implementation and monitoring.
- Is concerned with budgeting for outcomes and outputs as well as inputs.
- Encourages public participation that helps make the allocation of finances transparent and provides the base for the publication of accessible information on the use of finances.

This requires the interactive planning and managing of both the IDP and the budgeting processes within the Municipality.

There is always the danger that particular interests attempt to separate them or assert one over the other. It is important that key managers in the Municipality ensure the two processes are properly aligned.

INFORMATION BOX

Different Forms of Budgeting

There is a range of different forms of budgeting used within government in South Africa. The three described below are used most often.

In some instances the type of budgeting is prescribed in regulations. Increasingly national government is encouraging the use of the third type.

Incremental Budgeting is the system historically most commonly used. It entails allocating additional revenues as they become available without examining existing spending or allocation and technical efficiency in the use of resources. It works in opposition to budgeting that attempts to make optimal use of scarce financial resources on developmental priorities. It is the approach that budget and planning reform by government in the country is directed at changing.

Zero Based Budgeting (ZBB) is the system in which every item of spending is rejustified on an annual basis against the identified priorities of the Municipality. While making very strong linkages between inputs and prioritised outputs it underemphasizes continuity and is very costly in staff time.

Performance Based Programme Budgeting is a system for allocating costs based on programme and project outputs linked to defined performance measures. It provides a framework that integrates policy objectives, implementation strategy, required inputs, obtaining and allocating of funds and defined outputs and performance measures. It emphasises the value of inputs in terms of their efficiency in achieving the prioritised outputs and outcomes. It also recognises the importance of continuity but flexibility to new priorities or service delivery approaches.

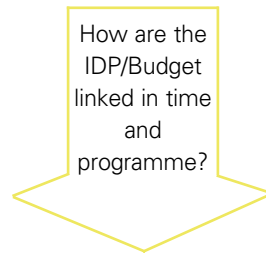
“As goals and priorities change over time, programmes can be expanded or phased out and new programmes introduced.” (FSC Report)

3. THE POTENTIAL ROLES AND FUNCTIONS IN ENSURING IDP LINKAGE WITH THE MUNICIPAL BUDGETING PROCESS

The table on the next page outlines the potential functions of different parts of the Municipality that should give direction to an integrated structure for effective management of these processes.

POSITION/ STRUCTURE	FUNCTION IN IDP PROCESS	FUNCTION IN BUDGET PROCESS	ROLE IN INTEGRATION OF PROCESSES
Executive Mayor or Exco	Responsibility to ensure the Council fulfils its legal responsibilities by preparing an IDP within legislative and procedural guidelines.	Responsibility to ensure the Council fulfils its legal responsibilities by preparing an annual budget and a 3-year financial plan within legislative and procedural guidelines.	<ul style="list-style-type: none"> • Gives key political support to the proper integration of processes.
Council	Responsible for approving the IDP.	Responsible for passing the Budget.	<ul style="list-style-type: none"> • Assess that the linkage is achieved at the points of passing joint IDP and Budget and at interim points in process.
Municipal Manager	Strategic management of the Process. Responsible to see that IDP is carried out as required by legislation and procedures.	Strategic management of the Budgeting Process and preparation of 3 year plan. Accounting Officer of the Municipality.	<ul style="list-style-type: none"> • Is in best position to ensure strategically that the process is integrated structurally within the Council.
IDP Manager (Where no IDP Manager responsibility of Municipal Manager)	Day to day responsibility for the IDP Process.	Day to day work to link with financial manager in helping to ensure IDP outputs are integrated into Budget.	<ul style="list-style-type: none"> • Through all IDP activities ensures that linkage is made between 2 processes. • Ensure the flow of information from the Budget process into the IDP and IDP outputs into the Budgeting process. • Close day to day management interaction with Financial Manager.
Financial Manager	Key participant in the IDP Steering Committee.	Day to day management of the Budgeting Process.	<ul style="list-style-type: none"> • Ensure that IDP outputs are integrated into Budget. • With IDP manager align the timing and outputs of the 2 processes. • Ensure the flow of information from the Budget process into the IDP and IDP outputs into the Budgeting process.
IDP Steering Committee	Oversee the effective management of the IDP process. Contribute to the assessing of needs and the prioritising.	Proper organisational linkage with the Budget Steering Committee or equivalent in the Municipality.	<ul style="list-style-type: none"> • IDP and Budget Steering Committees could be structured together under the co-ordination of Municipal manager. • Ensure that Terms of Reference of steering committee(s) stress the interlinking of IDP with budgeting process.
IDP Representative Forum	To provide community stakeholder inputs into all phases of the IDP.	Can provide community stakeholder inputs into consultation parts of the IDP linked to Budgeting process.	<ul style="list-style-type: none"> • Ensure that Terms of Reference and membership of Forum reflects this contribution to both processes.

All individuals and structures should ensure the integration of the planned outputs through a good understanding of the respective processes.



4. LINKAGE OF THE IDP TO THE BUDGETING PROCESS

Effective interlinking relies on pro-active management. The linking of activities within joint time frames is crucial. The timing is predominantly determined by the budgeting process that is a key determinant of the structuring of the timing of Phases of the IDP. The close co-operation of the Municipal Manager, the Financial and the IDP Manager (or whoever drives the IDP and budget processes in your Municipality) is crucial in making sure the alignment is made between the processes.

The table on the next page highlights the points in the IDP process where the potential linkage with budgeting is most important. The linkages with the annual IDP review would be a simpler interaction that will be dealt with in Section 5 of this Guide.

IDP PHASES AND ACTIVITIES	OUTPUTS RELEVANT TO FINANCIAL MANAGEMENT	RELEVANCE TO LINKAGE OF IDP/BUDGET PROCESSES
PREPARATION PHASE		
Advertise IDP with Budget Process	<ul style="list-style-type: none"> Stakeholders in Municipality properly informed of the planning process that will give form to the budget. 	<ul style="list-style-type: none"> To encourage submissions/participation from stakeholder – community.
Finalise Process Plan and Framework integrating budgeting process within Integrated Development Process	<ul style="list-style-type: none"> Completed IDP/Budget process plan that demonstrates a seamless process IDP/Budget. 	<ul style="list-style-type: none"> To identify to Council and management the role, responsibilities, deliverables and milestones in preparation of the IDP and its link to the Budget process.
Finalise integrated IDP/ Budget Structures	<ul style="list-style-type: none"> Formed IDP Steering Committee and the IDP Forums integrating respective budgeting Committee and as Budgeting Consultative Forum respectively. 	<ul style="list-style-type: none"> To establish the Municipality's key team to steer IDP/Budgeting processes. To establish forum for receiving submissions and consulting on issues related to IDP/Budgeting. To consolidate and make recommendations to Council on the form and broad content of IDP/Budget.
PHASE 1 – ANALYSIS		
1/1 – Existing information Available Resource Potential	Financial resources differentiated by sources of income and type of expenditure.	<ul style="list-style-type: none"> Information available on previous years' expenditure against budget to help with analytical financial framework to guide planning for next year. Contributes information to fiscal strategy and Budget structuring.
1/4c – Institutional Analysis	Overview of strengths and weaknesses of financial management system.	Identifies what is required to improve and properly resource the right Financial Management System
1/7 – Aggregation Priority Issues	Identification of priorities.	<ul style="list-style-type: none"> Budget process provides analysis of the available resources and financial potential based on previous years. This financial information helps inform the detailed defining of priority objectives in the Council and community analysis.
1/9 – Analysis of priority issues – Resources/Potentials	Identification of available sector specific financial resources.	<ul style="list-style-type: none"> Providing information on potential priorities to link with indicative financial sources.
PHASE 2 – STRATEGIES		
2/4 – Defining resource frames/ Financial Strategies	<ul style="list-style-type: none"> Problem and guidelines for necessary reforms of Financial Management System. 	<ul style="list-style-type: none"> Provision of more precise financial resource frames linking with emerging priority objectives. Defining of more detailed fiscal strategy to maximise usable income.
2/5 – Creating Strategic Alternatives	<ul style="list-style-type: none"> Realistic alternative strategies for each priority issue. 	<ul style="list-style-type: none"> Identifying financial possibilities and constraints for different strategies.
2/9 – Development Strategies	<ul style="list-style-type: none"> Prioritised Municipal strategies for agreed developmental objectives. 	<ul style="list-style-type: none"> Detailing the key strategies with broad financial possibilities and limitation to assist with more detailed prioritising. Identifying the projects that require detailed linkage with 5-year Financial Plan, 3 year MTEF and 1 year Budget.

IDP PHASES AND ACTIVITIES	OUTPUTS RELEVANT TO FINANCIAL MANAGEMENT	RELEVANCE TO PREPARING IDP/BUDGET
PHASE 3 – PROJECTS		
3/2 – Preliminary Budget Allocation per Project	<ul style="list-style-type: none"> Preliminary budget allocation per project. Preliminary budget allocation for operational and non-prioritised routine budget. 	<ul style="list-style-type: none"> More detailed budgeting figures for IDP. IDP project planning provides initial operational implications to budget.
3/3 – Designing project proposals	<ul style="list-style-type: none"> Cost, budget and financial source estimates for each prioritised project and re-prioritising in terms of cost and available resources. 	<ul style="list-style-type: none"> More specific financial information about the prioritised projects that gives form to the capital and operational budget.
3/9 – Cost/Budget estimates – source of finance		
PHASE 4 – INTEGRATION		
Activity 4/1 – Feasibility and viability checks – Negotiations for funds/priorities	<ul style="list-style-type: none"> Revised project proposals including adjustments in terms of budgets and finance available. Draft sector programmes aligned with available financing. 	<ul style="list-style-type: none"> Further detailing of the budget and the prioritising of projects on the basis of financial resources available.
4/4 – 5 year Financial Plan operational strategy	<ul style="list-style-type: none"> Financial Strategy Revenue and expenditure forecast for 5 years 3 years Medium Term Expenditure Framework Draft Budget 	<ul style="list-style-type: none"> Provides guidelines and procedures Revenue raising strategies Asset management strategy Operational expenditure estimates on basis of the IDP programme Financial position of Council for 5 years Base for the preparation of 3 years MTEF
FINANCIAL OPERATIONAL STRATEGY		
4/5 – 5 year capital investment programme	<ul style="list-style-type: none"> Tabular overview of the capital investment projects, sources and timing of financing. 	<ul style="list-style-type: none"> Provides the basis for the preparation of the details of the financial management of the delivery of the capital programme.
4/7 – Integrated Monitoring and Performance Management System	<ul style="list-style-type: none"> Specifying relevant financial indicators for developmental objectives, projects and non-project specific activities. Time scheduling and major milestones of projects. Action plan with financial resource implications for managing integrated M&E system. 	<ul style="list-style-type: none"> Relevant financial indicators are built into M&E system. Financial monitoring is linked to the broader monitoring and evaluation system of Municipality – impacts on the design of the overall financial management system. Resource implications of financial management system detailed.
4/12 – Integrated institutional programme	<ul style="list-style-type: none"> Specific proposals as to institutional organising to ensure smooth implementation of the IDP. 	<ul style="list-style-type: none"> Specific proposals with time spans and resource allocation to ensure that the Financial Management System supports the implementation of IDP.
PHASE 5 – APPROVAL		
5/1 – Opportunities for comments from provincial/national government	<ul style="list-style-type: none"> Comments on the financial prioritising of the Municipality's developmental programmes. Further provision of information that can inform future provincial/national government budgets. 	<ul style="list-style-type: none"> Presentation of the Municipality's proposed programme of implementation is linked to detailed budgeting. This enables government to assess and consider viability and possible linkages.
5/2 – Opportunities for public comment	<ul style="list-style-type: none"> Comments from public on IDP/Budget. 	<ul style="list-style-type: none"> Presentation to public of seamless linkage of development programme with financing for final consideration before legally approved.
5/3 – Incorporating and responding to comments	<ul style="list-style-type: none"> Adjustments to IDP/Budget where appropriate. Responses on all inputs. 	
5/4 – Final adoption by the Municipal council	<ul style="list-style-type: none"> Adopted IDP. Adopted Municipal budget in tandem with IDP. 	<ul style="list-style-type: none"> Official endorsement of the IDP linked to separate approval of budget.

INFORMATION BOX

Adjustment of Annual Budgets and the IDP

In its present form the **Municipal Finance Management Bill 2000** if passed will make it possible for the Municipal Council to agree a budget adjustment after 7 months of the financial year. The adjustment budget may only apply for matters where there is:

- adjustment to revenue and expenditure estimates where there is material undercollection of revenue
- appropriation of new revenue over and above what was projected
- unforeseeable and unavoidable expenditure
- utilisation of savings against votes
- any other matter prescribed or approved in writing by the Minister.

The Bill does not prescribe further consultation for such changes.

With IDP and Municipal budget process linked how does this now link with National and Provincial budgeting?

5. BUDGETING – ALIGNING THE MUNICIPAL BUDGETING AND IDP WITH NATIONAL AND PROVINCIAL BUDGETING FRAMEWORK

In their budgeting, Municipalities are reliant on National and Provincial government for:

- Some of their operational and capital finance.
- Annual regulations on limits of expenditure and conditions for lending.

In turn legislation and policy requires that the Municipality's IDP provide the developmental priorities to inform the relevant parts of National and Provincial Budgets.

INFORMATION BOX

Reorganising of The National Budgeting Process

The national budgeting process has undergone substantial re-organising since 1994. This has concentrated on the following principles relevant to local government:

- Transparent processes for the allocation of resources between different spheres of government (vertical) and across the different Municipalities (horizontal).
- Processes that recognise the legislative development responsibilities of the Municipalities and the extent of poverty, the lack of services and the Municipalities' ability to raise its own resources.
- Decentralisation of control of finances to where services are delivered.
- IDP feedback of priorities to aid national priority setting and allocation.
- Multi-year allocations to facilitate longer term planning and programme of implementation.

While policy shifts have occurred, the procedural systems have not always followed. For example there are still no standardised national approaches to the integration of IDP priorities into Provincial and National Budgets. The 3-year MTEF, now a requirement of all three spheres of government, could help achieve this over time.

In the meanwhile it depends upon the pro-active interaction of Municipal Officers handling the IDP and Municipal Budgets – particularly their interaction with relevant national and provincial departments.

This re-enforces the importance of actively encouraging provincial and national government inputs at all stages in the IDP process. It is through this that closer linkages can be made with their budgeting processes.

You should remember that when designing strategies around financing, do not only consider paper submissions but also some level of national and provincial government involvement in the IDP and linked Municipal processes themselves. At this present point in procedure development you are more likely to have success.

But be aware where financing needs are built into budgets under preparation, your Municipality will need to wait at least 5 months before it can access the money even if approved. You therefore need to plan accordingly.

The diagram on the next page illustrates the key interactive points between the budgeting processes.

Be aware that the differences in the financial year of the spheres of government and the IDP process can cause complications:

- National and Provincial Government Financial Year: 1 April – 31 March.
- Municipal Financial Year: 1 July – 30 June (IDP Planning process linked to these dates).

This makes it more difficult to synchronise budgeting processes. It also requires Municipalities to have their priority inputs ready 12 months before the actual financial year in which they will spend on implementation. This is particularly relevant to the full IDP. Once the 5-year Financial Plan is completed it can inform other spheres' annual budgets of other spheres in a proactive and timeous manner.

Notwithstanding the constraints, the IDP and the Municipal budgeting must interact with the national and provincial budget processes if Municipalities are to maximise the resources available to them.

This must also take into account the complex process that interlinks provincial and national government budgeting that feed backwards and forwards through the whole process. The details of this interaction are not dealt with in this manual, only the points at which it impacts on the IDP/Budget process.

Such interaction requires active planning and proper management.

Now consider linkages between the Municipal Budgeting and National and Provincial budgeting Processes

MUNICIPAL IDP & BUDGETING PROCESS

NAT. & PROV. GOVT. BUDGETING PROCESS

STARTS 1 JULY 2001

By April 2002
Draft Priority Projects
Draft Budget for Council

End June 2002
Approved IDP and Budget

STARTS 1 JULY 2002

Nov/Dec
Initial capital and operational budgets prepared. (Incorporate indicative allocations.)

March/April
Draft Budget to Council by end March.
Preparing and consulting on final draft of Budget
Incorporate National and Provincial Allocations into Municipal Budgets

Ends 30 June 2003
With Council Approved IDP/Budget for 2003 – 2004

STARTS 1 APRIL 2002

PROV.	NAT.
May to July Initial preparation of budgets	
↔	
↔	
November Issue of Medium Term Expenditure Framework	
↔	
↔	

Ends 31 March 2003
Approved National and Provincial Approved Budgets for 2003

Prior involvement of officials in various sectoral activities in IDP should have fed into this budget preparation

Submit IDP's relevant to these budgets as early as possible. Includes 3 year Financial Plan from IDP's 5 year Financial Plan. In draft form if properly done

Indicative allocation from National Govt to Municipalities for their next 3 financial years. (No later than 15 December).

12 Months

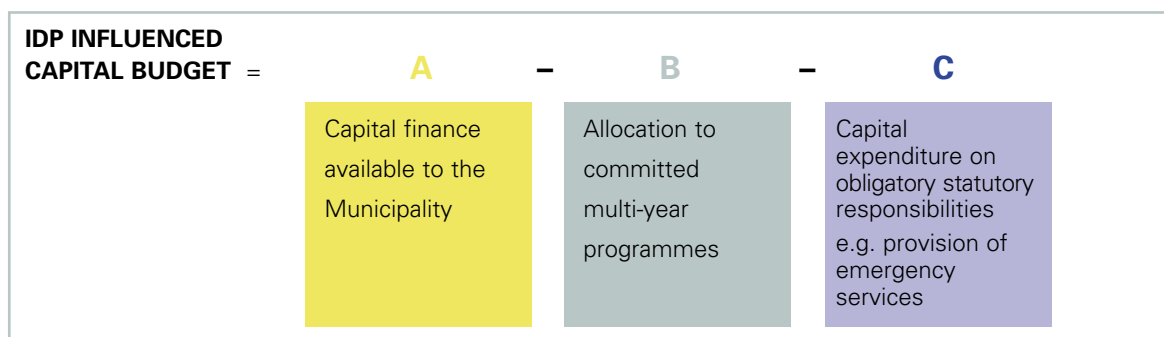
- Allocations for Municipalities formally approved in National and Provincial Budgets
- Firm Commitments to Municipalities. (No later than 28 February.)

6. BUDGET – IDP INFORMING THE OPERATIONAL BUDGET: A CHALLENGE

The IDP Primarily Focuses On The Capital Budget

The IDP is an important process to prioritise Municipal implementation.

However its focus at the point of prioritising financial allocations, concentrates primarily on the capital budget. Within this, it can only effect the allocation of the non-committed part of the capital budget i.e.



The budgeting process gives specific attention to the overall operational budget and the capital budget and the interaction between the two.

The Challenge – Strengthening the Impact of the IDP on the Operational Budget

The challenge is to strengthen the impact that the IDP process has on broader budgetary allocation including the operational budget, and through this to expand its contribution to a better prioritised Municipal delivery programme.

In the study on Planning Implementation Linkage the Municipalities’ operational budgets were at least 4 – 6 times larger than their capital budgets. Yet only one Municipality made a pro-active attempt to assess and align this budget with the Municipality’s IDP determined priorities.

There are four key ways in which the IDP should influence the operational parts of the budget process:

	FORM OF INFLUENCE ON OPS BUDGET	EXAMPLES	WHERE IN IDP PROCESSES
1.	OPERATIONAL IMPACT OF CAPITAL PROJECTS WHEN COMPLETED Operational impact of capital commitments on the operational services required operating and maintaining capital investments.	Development of primary health care clinic. This will require financing in future years’ operational budgets for: – Staffing costs for clinic – Maintenance of clinic – Medicines and other health care	IDP Activity Budget
2.	OPERATIONAL COSTS OF DELIVERING CAPITAL PROGRAMME Direct and support operational costs of delivering the Capital Programme.	The shift in emphasis from road development to health issues as priorities require a shift of operational resources from engineering to health departments.	IDP Activities: 1/1, 1/4c, 1/9, 2/4, 3/8, 4/4, 4/5, 4/7 Budget
3.	OPERATIONAL FINANCED PROJECTS OF IDP IDP Priority projects that require primarily operational expenditure and minimal capital financing.	HIV/Aids Awareness Programme identified as priority project. Requires operational funding for the staff, materials, transport etc. Community based road maintenance programme requires: – Payment of community members. – Purchase and maintenance of basic equipment e.g. spades. – Infrastructure maintenance	IDP Activities: 3/3, 3/9, 4/4 Budget
4.	RE-ALIGNMENT LOCATION OF EXISTING OPERATIONAL RESOURCES IN LINE WITH IDP PRIORITIES Re-allocation of operational resources in line with the general Municipality’s developmental objectives as identified in the IDP.	Consideration of whether the existing infrastructure maintenance budget is going to already well-resourced areas. Consideration of whether to reduce 2 day a week refuse collection service in well-resourced areas to allow for establishment in underresourced areas.	IDP Activities: 1/1, 1/4c Budget

To achieve greater IDP impact on the operational budget the Municipality must strengthen the interaction between the budgeting process and the IDP process in its assessment and allocation of available operational resources. In doing this it must give emphasis to the following important points:

- Separate the service and delivery components of the budget from support components.
- Define direct service delivery components either as part of agreed capital programmes or as separate operational delivery programmes.
- Define which of the operational programmes are statutory obligatory and those over which the Council has discretionary responsibility.
- Assess these discretionary operational programmes against the priorities emerging from the IDP.
- Assess the output effectiveness of resource allocation to the statutory and prioritised operational delivery programmes.
- Develop a programme for:
 - the phased redirecting of the non statutory and non prioritised operational resources to statutory or prioritised programmes;
 - the redirecting of poorly directed operational resources in prioritised programme; and
 - the appropriate allocation of the support inputs to the operational and capital programmes.
- Link the developed programme to the Performance Management System of the Municipality.

EMPHASIS BOX

ITS NOT EASY – RESOURCES TO HELP DO THIS

Achieving shifts in the operational allocation is often difficult.

Usually 60 – 70% of a Council’s operational budget is staffing costs.

Changes in the use of operational budgets must of necessity involve the difficult task of re-organising staffing resources.

It is recognised that this is not a simple task and that it is likely to take a few years to develop and implement a cohesive plan for correct alignment. Implementing it will also require resources in dealing with institutional structuring, staff relations, training and negotiations to overcome potential complex obstacles.

Individual Municipalities are not left alone on this. Under the 3-year MTEF allocation by National Government there are 4 grants under the Capacity Building and Restructuring/Local Government Support Grants that can help support such reorientating of budget/resources:

- Local Government Support Grant
- Local Government Financial Management Grant
- Municipal Systems Improvement Programme
- Municipal Restructuring Grant

EXAMPLES BOX

Ideas from Other Municipalities

Some Municipalities are strengthening the influence of the IDP on the operational budgets by organising service provision financed by operational budget as projects. These are then subjected to the same planning and prioritising as the capital projects.

Examples:

- Integrated Service Maintenance Project – Defines the input costs, prioritises the type of repairs and targeted areas, sets and publishes service standards and sets up Performance Management System.
- Primary Health Care Delivery Project – Defines available input costs, prioritises the target and area for the use of these resources on the basis of the IDP, sets and publishes service standards for clinic, managing assessment of this as project against indicators established within IDP.

D. FISCAL PLAN

1. OBTAINING THE FINANCIAL RESOURCES – THE FISCAL MANAGEMENT PLAN HELPING IMPLEMENTATION

Implementation cannot take place unless the financial resources required to pay for it are obtained.

The budgeting process stresses the broad activities required to identify revenue.

This is linked to the work within the IDP process to develop a Fiscal Plan.

It highlights the need for the Municipality to have a pro-active plan and linked strategy to maximise its revenue and to ensure the most effective medium and long-term management of its assets.

While it is integral to the budgeting process it is an important function in its own right. Approaches to this are dealt with in this section.

DEFINITION BOX

What Is A Strategic Fiscal Plan?

This plan which the Municipality should prepare, defines the financial opportunities and constraints available to obtain the revenue to implement its statutory responsibilities. It focuses on the long-term financial sustainability of the Council in delivering its services.

It is a specifically designed plan with a strategy that attempts to maximise the financial resources available to the Council to carry out its responsibilities in accordance with its identified development priorities.

The Municipality must ensure that it does so in a way that maximises its long-term financial viability as well as that of its targeted population.

In obtaining financial resources the Municipality should maximise both its operational and capital financing.

In doing so the Municipality must take into account three important constraining conditions:

- National regulations and guidelines that set borrowing and expenditure ceilings for Municipalities.
- A Municipality's capacity to use the resources obtained well and within the period that it is available.
- Its ability to apply the use of the financing so as to improve its longer term financial sustainability and that of its targeted population.

2. PREPARING A FISCAL PLAN

ACTIVITY	Development of Strategic Fiscal Plan															
Purpose WHY?	<ul style="list-style-type: none"> • To define the financial opportunities and constraints for the Council to implement its statutory responsibilities. • To analyse the most effective way of applying available finances for the long-term financial sustainability of the Council in delivering its services. • To define a strategy that maximises financial resources while meeting the Municipality's key developmental objectives. 															
Output WHAT?	<p>Fiscal Plan over 5 year period including:</p> <ul style="list-style-type: none"> • Potential internal and external finance – operational and capital. • Asset management strategy. • Impact of using different fiscal strategies on longer term viability of Municipality. 															
Process HOW?	<table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="background-color: #d9e1f2;">STEP</th> <th style="background-color: #d9e1f2;">PURPOSE</th> </tr> </thead> <tbody> <tr> <td style="text-align: center;"> 1 Identifying the available resources </td> <td> <ul style="list-style-type: none"> • Know what internal and external financing opportunities are available to the Municipality and constraints of national government regulations. • How possible it is to access these and how and who should do this. </td> </tr> <tr> <td style="text-align: center;"> 2 Assessing the implication of their use or different forms of use </td> <td> <ul style="list-style-type: none"> • To assess the different ways of using the financing. • To analyse the implications of applying the financing in different ways to the longer term sustainability of the Municipality. </td> </tr> <tr> <td style="text-align: center;"> 3 Preparing the fiscal strategy and the action plan to implement the strategy </td> <td> <ul style="list-style-type: none"> • Making the choices between different financing sources and their application. • Defining these into a total fiscal strategy. • Stating the actions, timing and responsibility on how to link this to the work of the Council </td> </tr> <tr> <td style="text-align: center;"> 4 Developing the policy and procedural framework and systems for implementing the Fiscal Plan </td> <td> <ul style="list-style-type: none"> • To put in place the required policy and procedures e.g. debt collection. • To put in place the resources to ensure the implementation of the plan. </td> </tr> <tr> <td style="text-align: center;"> 5 Linking with the IDP and the budgeting process </td> <td> <ul style="list-style-type: none"> • To link the sources of financing to the programme and project costing from the IDP process. • To use the Fiscal Plan to inform the final prioritisation of the programme and projects for the forthcoming financial year. </td> </tr> <tr> <td style="text-align: center;"> 6 Annual Review of the Fiscal Strategy </td> <td> <ul style="list-style-type: none"> • To evaluate the success of the Fiscal Plan in helping the Municipality achieve its priorities. • To make necessary changes to the plan arising from better approaches or changes in the financing environment. </td> </tr> </tbody> </table>	STEP	PURPOSE	1 Identifying the available resources 	<ul style="list-style-type: none"> • Know what internal and external financing opportunities are available to the Municipality and constraints of national government regulations. • How possible it is to access these and how and who should do this. 	2 Assessing the implication of their use or different forms of use 	<ul style="list-style-type: none"> • To assess the different ways of using the financing. • To analyse the implications of applying the financing in different ways to the longer term sustainability of the Municipality. 	3 Preparing the fiscal strategy and the action plan to implement the strategy 	<ul style="list-style-type: none"> • Making the choices between different financing sources and their application. • Defining these into a total fiscal strategy. • Stating the actions, timing and responsibility on how to link this to the work of the Council 	4 Developing the policy and procedural framework and systems for implementing the Fiscal Plan 	<ul style="list-style-type: none"> • To put in place the required policy and procedures e.g. debt collection. • To put in place the resources to ensure the implementation of the plan. 	5 Linking with the IDP and the budgeting process 	<ul style="list-style-type: none"> • To link the sources of financing to the programme and project costing from the IDP process. • To use the Fiscal Plan to inform the final prioritisation of the programme and projects for the forthcoming financial year. 	6 Annual Review of the Fiscal Strategy	<ul style="list-style-type: none"> • To evaluate the success of the Fiscal Plan in helping the Municipality achieve its priorities. • To make necessary changes to the plan arising from better approaches or changes in the financing environment. 	
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Hints for designing the Output

- Competitiveness of local Municipality in extending its rates base.
- Maximising the use of existing assets.
- Maximising access to available financial resources in line with developmental objectives.
- Intensity and nature of development given the requirement of longer term affordability.
- Effect of local government expenditure on the economy – Municipal expenditure stimulating local economic growth rather than creating greater financial dependency.

Institutional Arrangements/ Responsibilities

WHO?

Management responsibility for the preparation rests with the Financial Manager as part of both the Budgeting and IDP processes.

Work in close conjunction with the Steering Committee and the IDP Forum.

Links to IDP and Budgeting Processes

IDP

Activities: 1/1, 1/9, 2/4, 2/5, 2/9, 3/9, 4/1, 4/4, 4/5

IDP Tool Box – E1 – Defining financial resource frames – P147

E2 – Revenue Planning – P149

E3 – Audit and Strategy for Asset Management – P156

Note: Annual Actions Plans

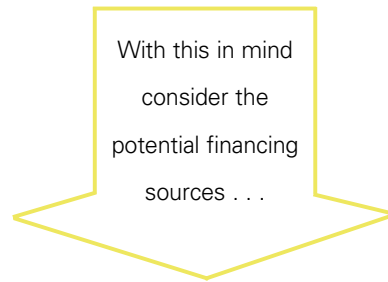
The objectives are usually not achievable in a single year. A fiscal management strategy is likely to have at least a five-year perspective. It requires an action plan showing how, on an annual basis and the Municipality will have to ensure that it progressively meets its fiscal objectives. This could include operational strategies e.g. improvement in revenue collection, extending the rates base.

INFORMATION BOX

What Finances to Use – Seeking a Sustainable Strategy

It is important that a Municipality identifies all potential sources of revenue to help it deliver. However, decisions to use the different resources require careful strategic consideration that must address key questions including the following:

- Is the Municipality maximising its internal revenues through the level of rates, taxes and service charges and its system for revenue collection?
- Can the residents of the Municipality afford the individual household cost of services to the standards developed by the Municipality?
- Does the Municipality have the capacity to meet its principal and interest on loans in a sustainable way in the longer term?
- Can the Municipality support the future operational expenses of its primary investments e.g. maintenance of infrastructure?
- Is the Municipalities targeted at both income generation as well as “social” projects to ensure long-term financial sustainability?



IDENTIFYING SOURCES OF FINANCE

The table below outlines the sources for financing for local government financing of its implementation programmes both capital and service delivery.

INTERNAL

Applies to finance raised through the internal resources of the Council. Responsibility for Municipalities to proactively determine and maximise this source of revenue is contained in national legislation e.g. Municipal Systems Act.

This is a crucial source of finance for the longer-term sustainability of the Municipality. It is very dependent upon the affordability levels of the residents of the Municipality. Important also is the cost to the Council of exemptions e.g. free basic water both for income and expenditure.

Examples:

- Taxes – Rates
- Service Charges
- Dedicated Funds, Reserves and special provisions

EXTERNAL

Resources that are obtained through other spheres of government and agencies and institutions that are not part of the Municipality.

National Government Grants:

Grants provided by the national government for accessing by Municipalities. The type and targeting of such grants can change over time depending upon the national priorities for Local Government.

Grants have very specific conditions and require Municipalities to prepare detailed business plans before accessing funds. These grants are integrated into the gazetted MTEF giving Municipalities strong indicative projections of this source of revenue.

Examples of present grants:

- **Equitable Share and Related Grants**
 - Equitable Share
 - R293 Personal
 - Transition Grant
 - Water and Sanitation Operating Grant
- **Capacity Building & Restructuring**
 - Restructuring Grant
 - Local Government Support Grant
 - Financial management Support Grant
 - Urban Transport Fund
 - Municipal Systems Improvement Programme
- **Capital Grants**
 - CMIP
 - Water Services Projects
 - Community Based Public Works
 - Local Economic Development

Provincial Government Loans and Direct Payments:

This applies to finances from provincial government revenue resources to Municipalities.

Examples:

- Agency Agreements – where there is a direct transfer of finances for a provincial government service function carried out by a Municipality on behalf of the provincial government.
- Specialist Subsidy e.g. Housing Subsidy.

External Loans:

The Municipality enters into agreement to obtain loan finance. The borrowing powers of Local Municipalities are tightly controlled by legislation and annual national government regulations. In principles these attempt to ensure that:

- loans take place within the defined national fiscal strategy.
- Municipalities have demonstrated ability to repay long-term capital loans within the lifetime of the asset developed.
- short term bridging loans are repayable within the fiscal year to which they apply.
- loans from outside the country meet stringent controls on foreign borrowing.

Examples:

- National – Private Sector
- Parastatals
- International – Private Sector and Government

Government Grants (Non South African)**Examples:**

- Internal – through international agencies operating within South Africa.
- External – through international agencies without presence in South Africa.

E. COST CENTRE FINANCIAL REPORTING

1. PERFORMANCE BASED & COST CENTRE BUDGETING AND FINANCIAL REPORTING – ASSISTING SOUND CAPITAL BUDGET AND PROJECT MANAGEMENT

With good Performance Based Management Budgeting there is a close alignment of planned expenditure to programme and project inputs and outputs.

This applies to both capital and operational programmes and projects. It can also apply to the support service for the projects and programmes as well as for the Municipality as a whole.

What is required is a **Financial Expenditure Management System** that supports priority delivery by controlling the efficient channelling of finances.

Such systems are encouraged and supported by legislation and policy. However, to structure and manage, they require skilled resources not available to all Municipalities.

2. LINKING FINANCIAL MANAGEMENT WITH PROJECT MANAGEMENT

With good Performance Based Management Budgeting there is a close alignment of planned expenditure to programme and project inputs and outputs.

This applies to both capital and operational programmes and projects. It can also apply to the support service for the projects and programmes as well as for the Municipality as a whole.

The Budget provides the baseline for the allocation of resources. To make implementation happen effectively the managed disbursements of these financial resources is required.

What is required is a **Financial Expenditure Management System** that supports priority delivery by controlling the efficient channelling of finances. It is the point at which the project management system and the financial management system must interact to ensure that resources are used:

- in the right amount;
- at the right time; and
- in the right way,

in order to produce the outputs envisaged within the priority objectives and prioritised projects of the IDP.

INFORMATION BOX

Cost Centre Budgeting and Financial Reporting

Increasingly, across the public sector the approach is to develop Cost Centre Financial Management. Each function and activity constitutes a **Cost Centre**. For example each project will be a cost centre, or administration can be a cost centre allocated back to each project.

The system of cost centres has numerous advantages:

- It links costs to activities, which traditionally public sector systems do not
- It helps non- financial staff assess the cost of their activity and has led to much tighter management of budgets
- It helps management of decentralisation

Such systems are encouraged and supported by legislation and policy. However, they require skilled resources to structure and manage. This is not available to all Municipalities.

How can a Municipality structure such a system?

ACTIVITY	Financial Management of Capital Programme	
Purpose WHY?	<ul style="list-style-type: none"> • To provide for the availability of the financial resources at the time required within the implementation and service delivery programme. • To ensure that this money is disbursed within the agreed priority framework of the Council. • To ensure that the finances are used in accordance with national, provincial and local regulations and procedures. 	
Output WHAT?	A system to permit the release of financing to ensure that prioritised projects are implemented smoothly and that the overall finances are controlled and spent in terms of the Municipality's identified priorities.	
Key elements	Performance Management Based Budget	Provides the baseline for determining the allocation of the financial resources by project, programme and support function.
	Annual Cash Flow Plan	Provides a cash flow projection by project over the 1-year budgeted period. Based on project, programme and support expenditure projections. This is aggregated to programme and Municipal levels.
	Service Procurement System	Policy, procedures and necessary systems to permit Project Managers to contract work outside of the Council where it is necessary.
	Programme and project based financial income and expenditure information system	A system that records separately the allocation, commitment and expenditure of resources against budget on a programme, project and Municipality basis, that feeds the relevant information to different levels in the structure.
	Programme and project based financial Monitoring and Evaluation system	Integration of the financial expenditure at project and programme level linked to the Key Performance Indicators of the Municipality's M&E Programme.

<p>Process</p> <p>HOW?</p>	<ul style="list-style-type: none"> • Project projected financial flows. • Agreed system for the requisition and release of finances during project cycle. • Regular monthly or weekly project financial reports. • Monthly capital programme financial reports.
<p>Hints for designing the Output</p>	<ul style="list-style-type: none"> • Use of Cost Centre Budgeting and Financial Management Reporting. • Regular financial reports by project and by capital programme as a whole.
<p>Suggested Institutional Arrangements/ Responsibilities</p> <p>WHO?</p>	<ul style="list-style-type: none"> • Each project has a Project Manager responsible for implementing the project. • Each project has one Finance Officer responsible for ensuring the disbursement of money and reporting. • Integrated monitoring of expenditure across the whole capital programme by IDP Steering Committee/Executive Committee.

REFLECTION BOX

Correct allocation and use of finances are at the heart of turning the IDP into implementation.

All staff involved should understand the basics of the way the financial management system should support delivery.

If you've understood this section you are in a good position to engage with others and make adjustments in the way your financial management system is organised.

Your best chance of success in this is when the technical skills of the financial management team are directly in harmony with the IDP initiative.