Zululand

DISTRICT MUNICIPALITY

UMKHANDLU WESIFUNDA

FINANCIAL RECOVERY PLAN

Prepared in terms of section 135 (3)(a) of the Local Government: Municipal Finance Management Act no.56 of 2003

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EXECUTIVE SUMMARY

On realisation of the fact that the municipality may not be able to meet its financial obligations it has come to dawn to this municipality that it is in serious financial problem. As a result, following the mandate in terms of section 135(3)(a) of the MFMA, the resolution is sought.

After a prolong absence of the municipal manager the Council appointed the Acting Municipal Manager, Mr K E Mpungose. Due to his experience on similar municipal problems Council so it fit to use his skills to this municipality. Given the mandate to put the municipality in the right path, the strategic session was held. Amongst the problems facing the municipality, financial problems were identified as the key source of all these problems. A turn around strategy in a form of a financial recovery plan was then proposed. The plan is the self-correction tool that is aimed at intervening to provide assistance without the provincial MEC interning in terms of section 139 of the Constitution.

Zululand district municipality is facing the significant fiscal and service delivery difficulties, which undermine the effective and efficient performance of its function and mandate.

Past cash flow reports were presented to Council that were showing the situation where the municipality may fail to finish the financial year in positive position. The adjustment budget was passed with the disclaimer that it is not supported by cash. Provincial Treasury did point out that this is the fact in its budget analysis report. Management has engaged the cash flow position and agreed on this financial recovery plan.

The principal strategic objective of this financial recovery plan is to identify key priority areas before the financial year end, as an immediate intervention and to set out specific intervention projects which will address the financial problems identified for a new financial year. The plan will then set parameters which will bind the municipality in the preparation of future budgets until the long-term financial plan is sustainable.

Key components of these priority areas:

Before year-end (next two months)

Review and implement expenditure management systems

Review and implement revenue management systems

Review and implement SCM systems

Review liabilities, long and short term, and conclude payment plans with creditors where appropriate.

Audit action plans

2019/ 2020 Budget year

Review and implement expenditure management systems

Review and implement revenue management systems

Review and implement SCM systems

Audit action plans

2019/2020 Budget outer years

Review and implement expenditure management systems

Review and implement revenue management systems

Review and implement SCM systems

The financial recovery plan must be approached with a holistic view in order to get the successful outcome of the intervention. This will ensure that the Zululand District Municipality is placed on a successful footing that will ensure efficient and effective financial astute that can provide service delivery that is sustainable to the communities it serves. This approach includes strategic leadership, institutional stability and transformation, financial management and focused service delivery.

INTRODUCTION

The financial recovery plan is prepared after realising that the municipality may not be able to fulfil its financial obligations as well as introspect in executing its mandate. Zululand District Municipality is a Category C municipality in terms of section 84 of the Municipal Structures Act, serving 892310 people in a district according to Census 2016. Being a rural municipality, the rate of unemployment is very high, sitting at 32%.

Paramount to its mandate is to provide purified water and bulk sewer to communities. This is done through bulk infrastructure development and maintenance. As a result of poor maintenance of infrastructure, a backlog has overwhelmed the Municipality. Adding to this is the lack of skill within the Municipal staff. Reliance has now been put on the private service providers with poor monitoring of contracts and without transfer of skills.

Over the years the wage bill has grown with the staff not normally operating on the core function of the municipality. All these problems combined they resulted in a poor budgeting and prioritisation of activities, hence causing cash flow problems. This is the core of the all Zululand District Municipality crisis to be addressed by this financial recovery plan.

BACKGROUND TO THE DECISION

Historically, the municipality has been changing hand in terms of the political leadership. With little care taken to ensure that the administration remain true to the course of service delivery, institutional integrity was at risk. The recent past exodus where the municipality replaced all its senior management at once, open the gate of free for all, weak organisational culture and inconsistencies. The absence of the municipal manager has put pressure on the administrative stability. The turn of events has seen the appointment of the Acting municipal manager who possess vast competency in the administration of municipalities. That open a new chapter for the municipality to be able to introspect itself and agree that it is in a crisis. With a need to change the old culture, a turn around strategy in a form of financial recovery plan was decided.

Assessment done to date indicate that financial institutional recovery would take a minimum of three years to ensure the full sustainability of the service delivery.

LEGAL FRAMEWORK

In terms of the Local Government, Municipal Finance Management Act 56 of 2003, section 142 sets out the criteria that must be addressed in the financial recovery plan which are:

(1) A plan must be aimed at securing the municipality's ability to meet its obligations to provide basic services or its financial commitments and such a plan, whether mandatory or discretionary intervention;

  (a) Must-

    (i) Identify the financial problems of the mucipality;

    (ii) Be designed to place the municipality in a sound and sustainable financial condition as soon as possible;

    (iii) State the principal strategic objectives of the plan, and ways and means for achieving those objectives;

(iv) Set out the principal strategy for addressing the municipality’s financial problems, including a strategy for reducing unnecessary expenditure and increasing the collection of revenue, as may be necessary;

(v) Identify the human and financial resources needed to assist in resolving financial problems, and where those resources are proposed to come from;

(vi) Describe the anticipated time frame for financial recovery, and milestones to be achieved; and

(vii) Identify what actions are necessary for the implementation of the plan, distinguishing between actions to be taken by the municipality and actions to be taken by other parties; and

(b) may—

(i) provide for the liquidation of specific assets, excluding those needed for the provision of the minimum level of basic municipal services;

(ii) provide for debt restructuring or debt relief in accordance with Part 3 of the MFMA Chapter 13;

(iii) provide for special measures to prevent unauthorised, irregular and fruitless and wasteful expenditures and other losses; and

(iv) Identify any actual and potential revenue sources.

(2) In addition, a financial recovery plan—

(a) For a mandatory intervention must—

(i) Set spending limits and revenue targets;

(ii) Provide budget parameters which bind the municipality for a specified period or until stated conditions have been met; and

(iii) Identify specific revenue-raising measures that are necessary for financial recovery, including the rate at which any municipal tax and tariffs must be set to achieve financial recovery; and

(b) for a discretionary intervention may suggest for adoption by the municipality—

(i) spending limits and revenue targets;

(ii) budget parameters for a specified period or until stated conditions have been met; and

(iii) specific revenue-raising measures that are necessary for financial recovery.

FINANCIAL PROBLEMS IDENTIFIED

1. Cash flow is an urgent matter that requires immediate attention. A decisive decision has to be taken almost now if the municipality has to be in a position to finish this financial year afloat, at least being able to pay salaries for the remaining 2 months **(adhere to financial recovery plan).**
2. Critical management positions have been vacant for a prolong period as a result of political and administrative decisions and that has left the municipality in an institutional as well as administrative crisis.

   The positions include:

   (i) Chief financial officer;
   (ii) HOD: Corporate services;
   (iii) HOD: Technical services;
   (iv) HOD: Community services;
   (v) SCM manager;

3. A lack of oversight, risk management and control coupled with leadership inefficiencies have created opportunity for misappropriation of funds, non-value for money spending and excessive occurrences of unauthorised, irregular, fruitless and wasteful expenditure. The following table illustrate the extent of the occurrences:

FINANCIAL RATIOS AND NORMS	NORM	2014 AUDIT	2015 AUDIT	2016 AUDIT	2017 AUDIT	2018 AUDIT
unauthorised, irregular, fruitless and wasteful expenditure	0			11 252 819	190 836 232	122 883 183

(non- existence of SCM- staff and unit, contract management, number of appeals resulting in deviations.)

4. A lack of restraint in budgeting, management and control has resulted in misappropriation of budget and other resources and little linkage between the budget and actual spending could be found **(lack of procurement plan, poor planning resulting to irregular expenditure**).
5. Service delivery has failed and, in many instances, basic services delivery infrastructure has been allowed to deteriorate to the extent that service delivery mechanism such as waste water treatment works have failed causing health hazard to the community it was intended to serve **(Idle staff and lack of tools of trade to attend to O+M).**
6. The municipal adjustment budget for 2018/19 financial year was found to be fundamentally unsustainable to the extent that the municipality find it self in severe financial distress as the adjustment budget is was not cash backed. This finding was also an observation by the Provincial Treasury when the budget was assessed in terms of section 23 of the MFMA **(re-arrange the business model to deliver).**
7. The Municipality regressed to qualified opinion by the Auditor General for the 2017/18 financial year with emphasis on revenue completeness and material water losses **(integrated metering infrastructure).**
8. Policies and procedures for a number of corporate, institutional and administrative functions have not been revised nor have been put in place to ensure adequate corporate governance required to ensure a healthy organisation **(policy workshop).**
9. Staff members were appointed or promoted on an ad-hoc basis with the total disregard of the Human Resources processes being followed and adding to the unaffordability of the municipal budget employee related costs **(double parking).**

10. A revision of the organisational structure has not been done such that structure follow functions. This is adding to the dysfunctionality of the municipality **(job evaluation).**
11. Financial mismanagement has resulted in the municipality finding itself in a dismal financial position with creditors inundated the municipality with demand for payments for long outstanding debt, absence of reserves and poor unspent grant reserves management **(WSSA, DWS, Aqua transport).**
12. Debt collection and credit control management has failed to such an extent that non-payment culture has been entrenched adding to the depletion of funds and reserves **(lack of coherent RES).**
13. A lack of restrained in all categories of expenditure has resulted in many instances of non-value for money spending and conclusion of contracts with services providers that left the municipality vulnerable and exposed to litigation **(Brand partners, branding registrations, functions, poverty and LED votes, water tankers).**
14. Excessive spending on litigation and security (body-guards) due to fear on perceived political attacks has added to the depletion of funds at a huge cost to the service delivery **(Attorneys panel, lack of policy on VIP protection).**
15. The socio- economic conditions of the municipal profile, high level of unemployment as a result, high indigent customers, have placed a further strain on municipal resources and the ability to function as a going concern **(Indigent register- write off possibility).**
16. A high rate of rotation of senior management left the administration unstable, leaderless and without direction **(Acting MM position**).
17. Unpalatable relationship between administrative staff and councillors has resulted in a sour working environment, as a result prolong leave of senior staff and mistrust, contributing to the dysfunctionality of the municipality **(Dir technical services).**
18. As a result of previous long-term financial decisions with long term implication, the municipality is at a brink of collapse as these decisions are not informed by plausible reasons. **(Outsourcing WSSA, Dam source- Usuthu bulk scheme)**
19. The tariff structure of the municipality has not been cost-reflective thereby under recovering on the cost of providing services. This include extending billing to all population receiving the services **(charge for rural communities).**
20. Inability to implement audit action plans has resulted in disregard for identification of fraud and corruption occurrences that may be revealed through consequence management and forensic investigations **(Audit action plan).**

METHODOLOGY IN DEVELOPING THE FINANCIAL RECOVERY PLAN

The primary objective is to design and mostly implement a recovery plan based on the challenges that are facing the Zululand District Municipality. The plan will address financial and institutional issues that have financial implication as identified by various assessments and those listed above.

This report will focus of Financial management aspects of the plan but cannot be implemented in isolation of other focus areas such as institutional stability and services delivery.

The ability of the municipality to manage resources that address the challenges mentioned will be discussed in the financial recovery plan. It is important not to lose sight of the current financial position that triggered the development of this plan.

IMPROVING FINANCIAL VIABILITY

Where the municipality find itself, we have a duty to improve the financial management systems across expenditure, revenue and financial position in order to determine the most effective way in solving the financial problems. **The plan with include mandatory parameters which will bind the Municipality in the preparation and adoption of future budgets until the long-term financial stability is achieved.**

Key components of this focused priority are:

(i) Immediately intervene on the **cash flow problem** by prioritizing payments according to their risk implication for the next two months of this financial year.

(ii) Review the current **budgeting strategy and expenditure management** in line with the budget framework endorsed by the strategic session engagement.

(iii) Review **revenue management** systems to maximise revenue generation and improve collection performance.

(iv) Review **governance practices of supply chain management** and implement proper unit and controls for optimum functionality in order to eliminate unauthorised, irregular, fruitless and wasteful expenditures.

(v) Review all **short- and long-term liabilities** as well as contingent liabilities and schedule repayment plans.

(vi) Review all **commitments** and transactions that have a potential of becoming an irregular expenditure.

(vii) A great deal of focus to be put on the implementation of Auditor general's report **action plan** and that of the internal audit.

KEY DELIVERABLES TO ENSURE FINACIAL VIABILITY

In order to ensure stability and remedy the poor financial sustainability within the municipality the following strategic projects needs to be focused on in the short, medium and long term.

Programme (i): Cash flow problems

Key deliverable project:

Immediately intervene on the **cash flow problem** by prioritizing payments according to their risk implication for the next two months of this financial year. The realisation that we may not be able to meet our commitments is the reason for the Financial recovery plan. The table below illustrates the cash flow problem.

	Estimated commitments	Estimated collection	Cash available
Opening balance			27 000 000
April	27 000 000		0
May	47 000 000	8 000 000	(31 000 000)
June	47 000 000		(78 000 000)

Delaying some of these expenditure commitments may cause crisis in the system e.g. Payroll, ESKOM, Water tankers, Security and VIP, Water treatment and maintenance.

Activities:

- **Suspend services and payments** to non-critical service providers.
- Negotiate **payment plans** with creditors.
- Institutionalise **pre-determined creditors payment** date and implement expenditure and creditors management.

- **Ring-fence grants** to account for unspent conditional grants.
- Develop cash **reserves by ringfencing VAT refund,** first allocating it to clear long outstanding creditors.

Programme (ii): Budgeting strategy and expenditure management

<u>Key deliverable project:</u>

Review the current budgeting strategy and expenditure management in line with the budget framework endorsed by the strategic session engagement.

<u>Activities:</u>

- Prepare and table 2019/20 MTREF Budget strictly in line with the **financial framework** of the strategic session.
- Finalise the **Spa agreement** discussions to reflect financial implication on outer years of the MTREF.
- Clarity on the role and establishment of **Zululand Development Agency**
- Prepare **procurement plans** to be align with the MTREF.
- Resolve on every item as presented by the **Provincial Treasury assessment** of the budget.
- Develop a **long-term Financial plan** that will link with the Vision 2030 of the Municipality.

Programme (iii): Revenue management

<u>Key deliverable project:</u>

Review **revenue management** systems to maximise revenue generation and improve collection performance

Revenue planning

- Focast on expected revenue to be based on realistic services based on past performance trends and economic realities.

Customer database

- Ensure accurate and reliable billing and consumer data.
- Administarive and political engagement with customers using technology

Tariff setting

- Public participation especially Rural communities on realistic basic charge taking into account economic conditions.
- IGR on raw water tariff to coussion the free water delivery.

Billing

- Billing system must reflect the correct billing and customer data in collaboration with credit beurau agents e.g. TransUnion.
- Communicate billing to correct customers using current technologies

Revenue collection

- Collect all revenue in line with the collection norm of above 95%
- Use of legal and tracing agencies for delinquent customers in line with the credit control policy

Metering & loss Management

- Embark on an installation of new smart water meters and improve to intergareted metering management system across the destrct.
- Ensure water distribution balancing by improving bulk meters and telemetry systems and monitor water demand management.

Indigent Management

- Develop indigent register using indipendent source of verification of indegent.
- Data cleancing

Credit control

- Critically evaluate customers for affordability to minimise bad debt risk
- Embark on water cut-off after incentives offerings

Activities:

- Draft and implement revenue enhancement strategy
  - Perform water meter audit and new smart meter installation
  - Perform customer data analysis and cleansing
  - Perform complete indigent verification process

- Conduct onsite water demand management and loss control
- Apply cost effective water tariff modelling
- Consider incentive offerings with a view to reduce outstanding debt
- Intensify legal and tracing agents applicable with the credit control policy
- Implement vigorous cut-off of services after incentives offering
- Improve monitoring and reporting towards achieving the 95% collection norm.

Programme (iv): Governance practices of supply chain management

<u>Key deliverable project:</u>

Review **governance practices of supply chain management** and implement proper unit and controls for optimum functionality in order to eliminate unauthorised, irregular, fruitless and wasteful expenditures.

<u>Activities:</u>

- Appoint the **SCM manager**
- **Align duties** of existing and seconded staff
- Develop and Implement **procurement plans**
- **Pull all SCM duties** into the SCM unit
- **Workshopping** the Bid committee members
- Isolate and dedicate Bid committee activities into **bid award room**
- Improve the **independency** of the Bid members.
- Ensure **rotation system** that is free of any interference
- Implement **electronic quotation system**
- All bid members to be subjected to **vetting**.
- Ensure complete **contract management** system
- Monitor and improve efficiencies and **turn-around time** of user department requests.

Programme (v): Short- and long-term liabilities

<u>Key deliverable project:</u>

Review all **short- and long-term liabilities** as well as contingent liabilities and schedule repayment plans.

Activities:

- Ring-fence **VAT refund as reserves** after settling all long outstanding commitments negotiated.
  - Reserves to be used for the following creditors:
    - Water Services SA
    - Department of Water and Sanitation
    - Retention

Programme (vi): Commitments

Key deliverable project:

Review all commitments and transactions that have a potential of becoming an irregular expenditure.

- Appeals on tender processes of security
- WSSA month to month contract
- Attorneys panel
- Media and communication month to month
- Allegations on Aqua Transport
- Policy review on Payments towards VIP protection
- Policy review Travelling claims of Councillors
- Pipe Jack JV Mageba capital Pty Ltd
- Communication’s retainer fees contract
- Events management Fee
- Sourcing of O+M service providers (Phindile civils, Sindiele)
- Attendance on emergencies (honeys sucker outstanding bill)
- Sourcing of Plant hire (on emergency basis)

Activities:

- Implement contract management
- Source opinion
- Report deviation and irregular expenditure
- Policy work shop
- Proactive planning on expenditure

Programme (vii): Audit action plans

Key deliverable project:

A great deal of focus to be put on the implementation of Auditor general's report **action plan** and that of the internal audit.

Activities:

- Completely implement AG's 2017/18 Action plan
- Review all Internal audit reports with the aim of implementing all recommendations
- Perform risk assessment and develop risk register.

IMPLENTATION OF THE FINANCIAL RECOVERY PROGRAMME

The financial recovery plan must be part of and be implemented as an inclusive approach in dealing with intervention proposed above focusing on specific areas. Each focus area must consist of a strategic project with clear timeframe, budget and areas of responsibility.

The Chief financial officer will be responsible for implementation reporting to the Municipal Manager. The CFO must be assisted by an appointed Project Manager who will be responsible for monitoring the day to day of the programme.

RISKS ASSOCATED WITH THE IMPLENTATION

The successful implementation of the programme has certain risks associated with the outcome. These need to be identified and mitigating processes be assigned to each project and be monitored. Some risks that are identified includes:

- The filling of critical vacancies
- The adherence to timeframes
- The willingness to embrace change
- The ability to fund some of the intervention programmes
- The cash flow is hampering the recovery process.

MONITORING

All decision regarding the implantation of the Financial recovery plan will be undertaken by the Acting Municipal Manager after approval by Council. It should be noted that the Financial recovery Plan includes short, medium and long-term activities. These activities will go beyond the term of the Acting Municipal Manager. The newly appointed municipal manager must therefore accept responsibility to ensure continuity and sustainability.

A Project Manager given the responsibility to monitor the day to day activities of the financial recovery plan will report to the office of the Municipal Manager who will then be accountable to Council for the success of the plan. Given the Municipal situation in administrative leadership, the ability and compassion of the Acting Municipal Manager, the impact in the short space of time, it is a wish that he project-manage this Financial recovery plan. Also, considering that he has been an administrator with trach record of successful intervention. Hence a recommendation for this project.

ROLES AND RESPONSIBILITIES

CONDITIONS FOR SUCCESSFUL IMPLEMENTATION

Adoption of the FRIP by Council before adoption of the 2091/20 MTREF

In a short term, an ability to close the financial year with the ability to meet critical financial obligation without disruption in service delivery.

In the medium term, the ability to reflect reserves and positive ratios on financial position before Mid-year term.

CONCLUSION