Funding
Municipal Waste Management Services

Reporting on Waste Khoro - Durban

Presenters: Bernard Mokgabodi **|** National Treasury **| 14 Octoberr** 2013

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Presentation Outline

- General structure of the local government fiscal framework

Transfers

- Waste management funding in the local government equitable share
- Transfers for waste management infrastructure
- Review of local government infrastructure grants

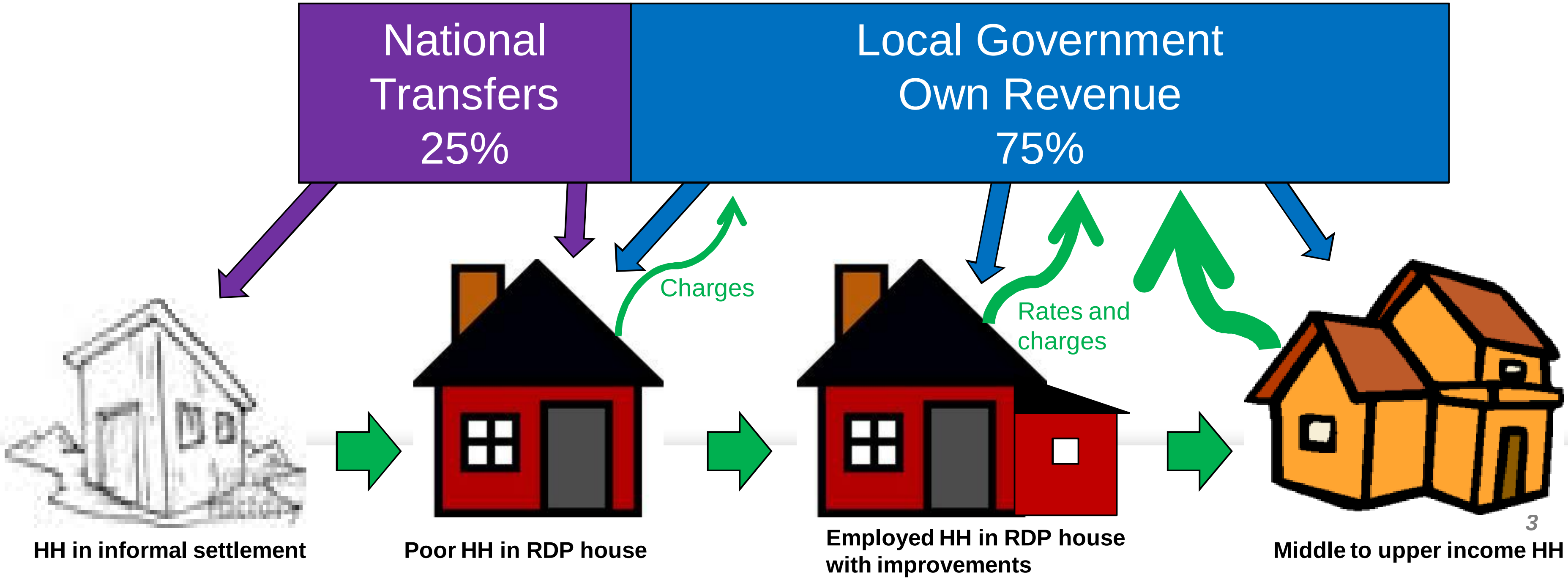
Tariffs

- Findings from National Treasury's benchmarking engagements
- Shortcomings in costing practices
- Summary of National Treasury's work to improve municipal costing

General principles for funding services in local government

- The local government fiscal framework is made up of own revenues (including service charges) and transfers
- Municipalities should charge cost-reflective tariffs for the supply of services for all users that can afford to pay
- High levels of poverty mean that funds from national revenues are needed to fund the delivery of services to poor households

Structure of the Local Government Fiscal Framework



The new LG equitable share formula structure

A new LGES formula

The local government equitable share was reviewed through a consultative process during 2012 and a new formula, based on 2011 Census data is being phased in over 5 years from 2013/14

Review was undertaken by:

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Schematic of how the new formula works:

Formula

1 **Basic Services** + 2 **Institutional and Community Services** ± 3 **Correct-ion & Stability**

How it works

1 Basic Services: **Allocation for every poor household in the country to enable municipalities to fund the cost of free basic services** (including maintenance costs)

2 Institutional and Community Services: Made up of three parts:

Institutional funding + **Funding for Community Services**

Revenue Adjustment factor
Ensures more funds go to the municipalities with less own revenue capacity
(Factor of between 0% and 100% applied)

3 Correction & Stability: Ensures guarantees are met and smoothes changes in allocations

LGES Allocation

Detail on the basic services component

- Formula funds free basic services for every household below an affordability threshold of R2300 household income per month in 2011
  - Based on value of 2 state Old Age Pensions (as proposed by municipalities) during the consultation process
  - 59% of all households in SA fall below this threshold
- Cost of services and number of households will be updated annually

FBS funding allocated for each HH through the formula:

Subsidy of R275.17 per month for a package of free basic services

Water: R86.45

Sanitation: R72.04

Energy: R56.29

Refuse removal: R60.39

Includes 10% provision for maintenance

Summary of Local Government Equitable Share allocations for waste management

- Total of R6.1 billion allocated for waste management through the LGES
- This amount includes an allocation of R60.39 per household per month for free basic refuse removal (includes 10% allocation for maintenance)
- Amount will be increased annually based on inflation

Amounts per basic service allocated through the Local Government Equitable Share

	Allocation per household below affordability threshold (Rands)			Total allocation per service (R millions)
	Operations	Maintenance	Total	
Energy	50.66	5.63	56.29	5 719
Water	77.80	8.64	86.45	8 783
Sanitation	64.84	7.20	72.04	7 319
Refuse	54.35	6.04	60.39	6 136
Total basic services	**247.65**	**27.52**	**275.17**	**27 957**

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Costing services for the LGES formula

- During consultations, stakeholders wanted detailed costing in the formula that would account for local cost drivers (e.g. topography and density)
- This proved to not be technically feasible due to a lack of credible and agreed data on what factors drive costs (and by how much) and consistent measures of these cost drivers across all municipalities

Advantages of using a single subsidy per poor household:

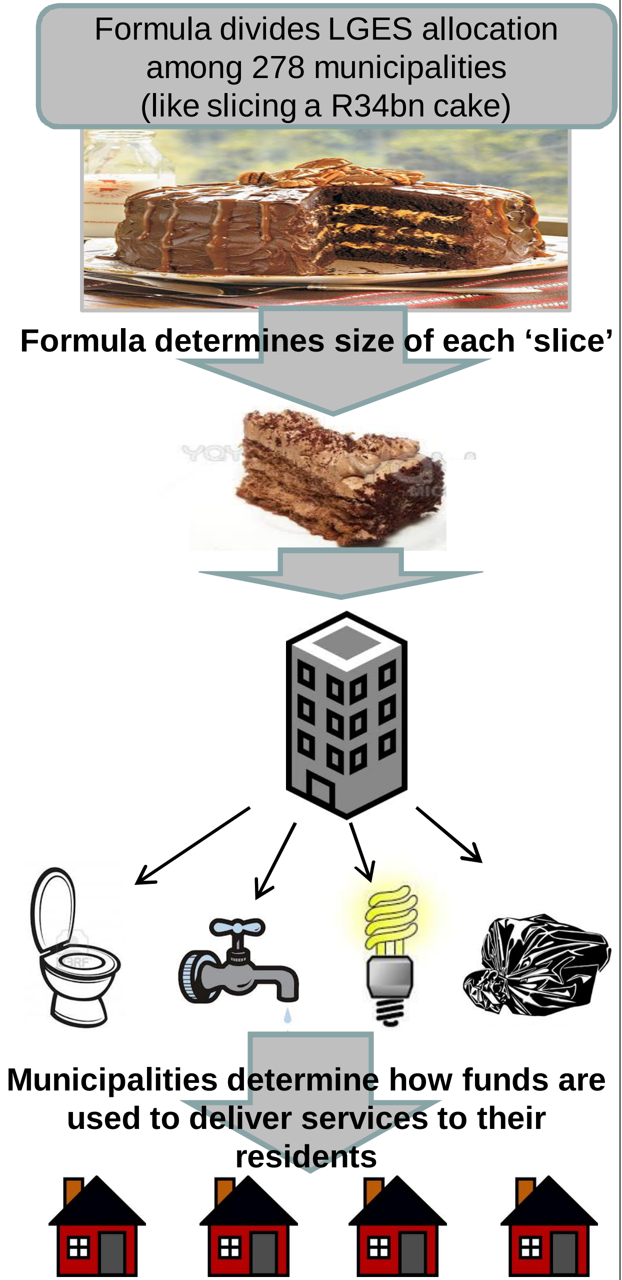
- Municipalities can use any excess funding on one service to compensate for higher costs of another service
- Recognises that policy allows for different types of waste management services to be provided in different contexts
- Allows the formula to be updated based on an estimate of the growth in the number of households

The new formula and service delivery

- Section 227 of the Constitution says:

  "Local government and each province is entitled to an equitable share of revenue raised nationally to enable it to provide basic services and perform the functions allocated to it."
- The equitable share is unconditional, but it is intended to fund the delivery of basic services
- The new formula structure:
  – is more transparent about the funds available for basic services
  – Has more realistic cost estimates
  – Will have its data updated annually
  – Includes more realistic levels of institutional and community services funding
- This will make it easier to hold municipalities accountable for how they budget for and use LGES funds

LGES DELIVERY CHAIN: From formula to services



Infrastructure grant funding for waste management

- Waste management infrastructure is funded as part of “other” basic services infrastructure in the Municipal Infrastructure Grant (MIG)
  - Because the funds in the MIG are not ringfenced municipalities can choose to spend more or less on a sector than indicated in the formula

Municipal infrastructure grant allocations per sector

Municipal infrastructure grant (formula)	Component weights	Proportion of MIG per sector	Value of component 2013/14 (R millions)
B-component	**75.0%**		**9 838**
Water and sanitation	72.0%	54.0%	7 083
Roads	23.0%	17.3%	2 263
Other	5.0%	3.8%	492
P-component	**15.0%**		**1 968**
Sports	100.0%	15.0%	1 968
E-component	**5.0%**	**5.0%**	**656**
N-component	**5.0%**	**5.0%**	**656**
Constant			**1 235**
Total			**14 352**

- Metros receive the Urban Settlements Development Grant (R9 billion in 2013/14) instead of the MIG. This can be used to fund waste management infrastructure

Review of the local government infrastructure grant system (1 of 2)

- **Minister of Finance has announced that infrastructure grants will be reviewed**

Households Without Access to Services in 2001 then 2011

Are we achieving sufficient impact?

Local Government Infrastructure Grants 2000-2012 (nominal Rand millions)

Review of the local government infrastructure grant system (2 of 2)

- Review will be consultative and collaborative (national departments and municipalities will be invited to participate)
- Data and literature analysis are underway now
- Extensive consultations and workshops will take place in early 2014
- Target is to announce the structure of a revised grant system in October 2014 (MTBPS)
- Implementation from 2015 Budget

Possible implications for waste management funding

- One of the questions the review will ask is what infrastructure needs are not provided for in the current system. Construction of landfill sites probably falls in this category
- Will need to consider how funding for landfills should be provided
  - *Project based vs formula based allocations?*
  - *Split between own revenue and grant funding needed for projects?*

Costing, tariff setting and managing sustainability

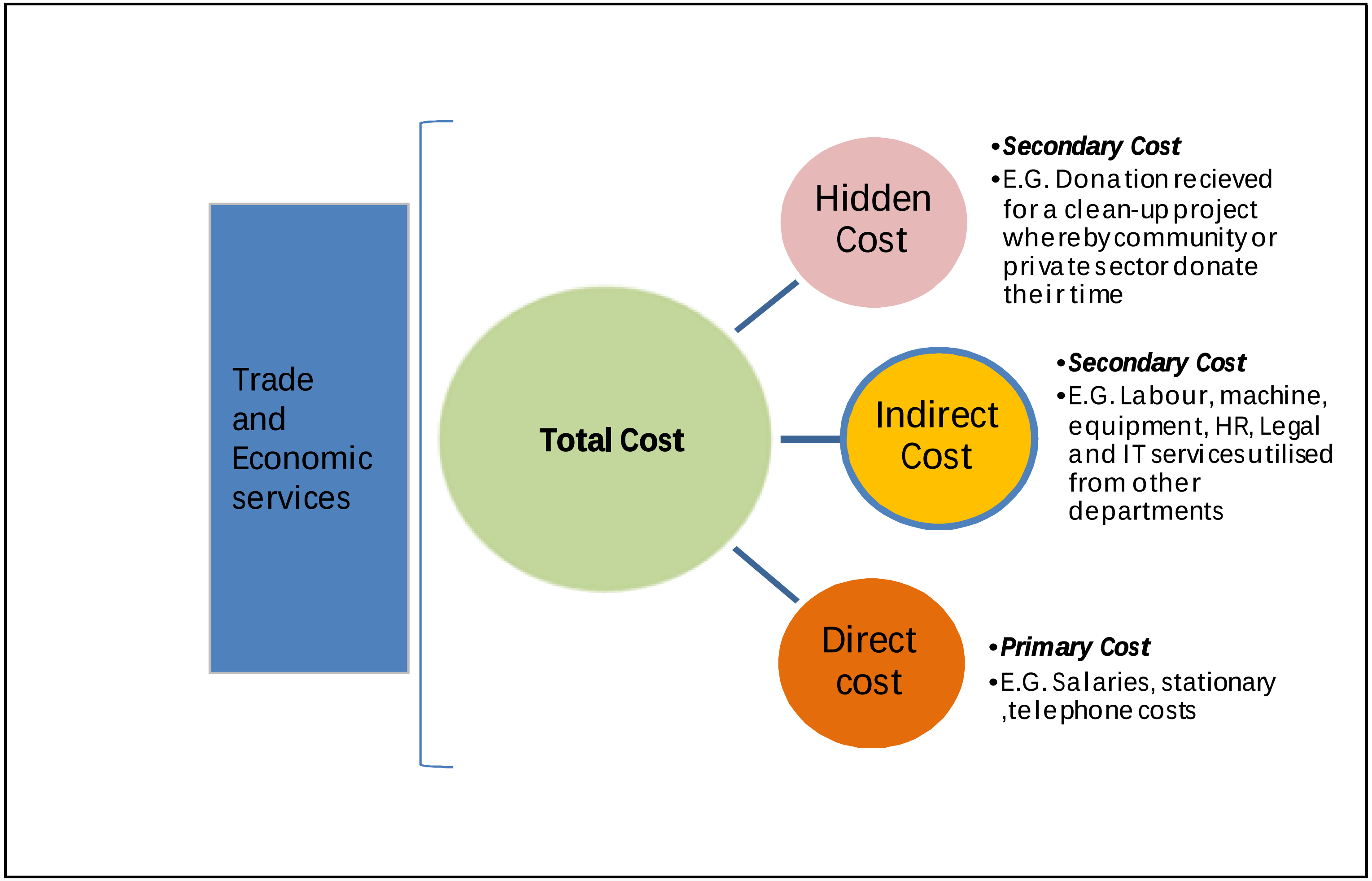
Findings of benchmarking engagements with municipalities (1)

- Basic accounting principles and costing methodologies are not applied to determine the ‘real’ cost of providing services
- Tariff determination is not informed by accurate costing that incorporates direct, indirect and hidden costs of services
- There is rarely a correlation between the annual tariffs in respect of basic services and the cost of providing such services
- The traditional approach of incremental tariff increases is widely applied
- The financial imbalance of the basic services is becoming increasingly greater with the costs exceeding the revenue generated by service charges

Findings of benchmarking engagements (2)

- Decreased cash coverage and depleted cash backed reserves is a further concern
- In general municipalities are becoming more and more grant dependent
- Cost efficiency does not seem to be a widely applied practice
- Inadequate allocations for asset renewal & maintenance

Elements of accounting for costs



Many municipalities do not have cost reflective tariffs; consequently operating at a loss

An analysis of the 17 non-delegated municipalities 2013/14 MTREF – Trading Services

Tabled MTREF 2013/14

	Electricity Services		Water Services		Waste Water		Waste		Consolidated	
R thousand	Surplus	Deficit	Surplus	Deficit	Surplus	Deficit	Surplus	Deficit	Surplus	Deficit
Metros										
City of Johannesburg	50 427		434 287		289 524		0	-525 515	774 238	-525 515
City of Cape Town	605 306		94 490		39 546		0	-775 189	739 342	-775 189
eThekwini Metro	476 693			-440 443		-129 447	0	-259 913	476 693	-829 804
Ekurhuleni Metro	0	-7 759	62 624		319 755		0	-52 607	382 379	-60 366
City of Tshwane	67 589		38 546		129 353		0	-194 703	235 488	-194 703
Nelson Mandela Bay	13 047		0	-39 561		-24 858	17 136		30 183	-64 419
Mangaung Metro	0	-143 392	0	-3 741	0	-59 144	53 228		53 228	-206 278
Buffalo City	0	-33 485		-90 078	0	-89 606	0	-3 169	0	-216 337
Secondary Cities										
Msunduzi LM	0	-248 458	0	-310 666	109 088		0	-80 885	109 088	-640 009
Rustenburg LM	143 515		0	-251 971	23 836		0	-57 113	167 350	-309 084
uMhlatuze LM	24 600		0	-31 235	0	-41 656	0	-14 113	24 600	-87 004
Mbombela LM	38 013		0	-128 639	0	-99 751	0	-69 828	38 013	-298 218
Polokwane LM	0	-16 257	0	-40 946		-3 232	0	-14 671	0	-75 105
Sol Plaatje LM	0	-26 652	17 805			-37 753	0	-2 532	17 805	-66 937
George LM	0	-21 717	10 709		10 827		7 531		29 067	-21 717
OR Tambo DM	0		0	-308 547	0		0		0	-308 547
Mafikeng LM	0	0	0	-12 579	0	-616	0	-27 287	0	-40 482
Total	1 419 189	-497 720	658 460	-1 658 407	921 931	-486 063	77 894	-2 077 524	3 077 474	-4 719 714

Note

1. Calculations are based on the tabled A2 schedules as presented at the benchmarking
2. Not all municipalities reflect the income portion for FBS under the relevant trade services.
3. Secondary costs have been included as a cost for the trade services and are allocated as follows
   a. Metros 10%
   b. Secondary cities 18%
4. All capital grant funding included in the A2 schedules have been excluded.

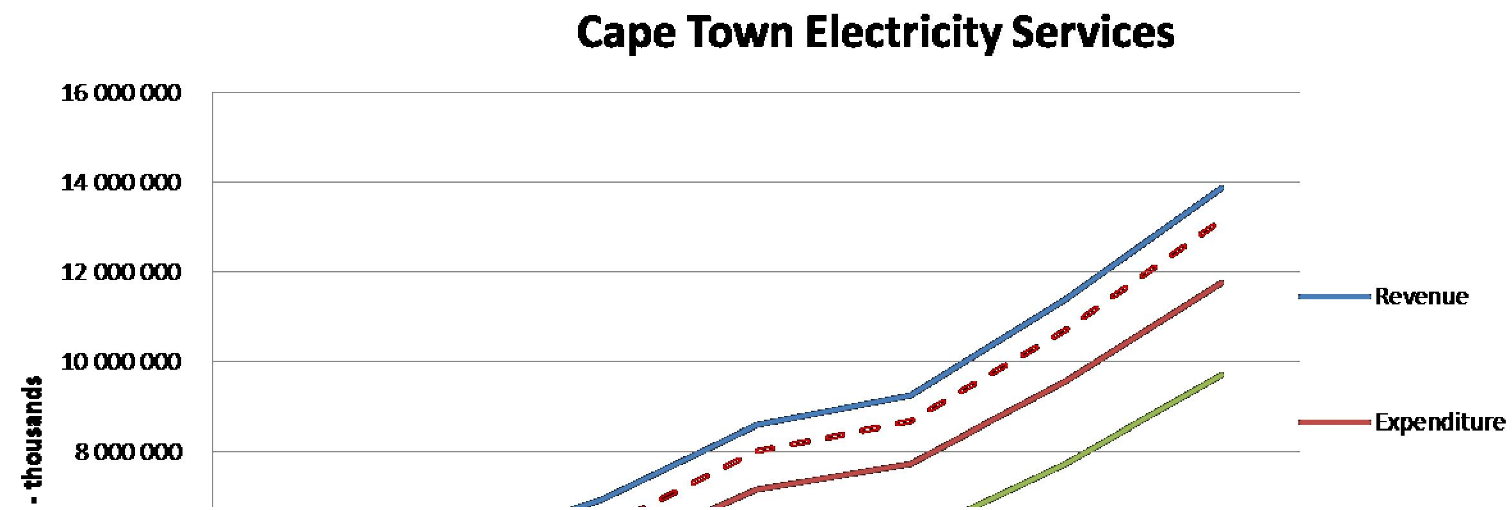
Findings of benchmarking engagements (4)

- These deficits reflected on the table above mean that municipalities are:
  - Cross subsidising tariff services with property rates
  - Depleting the limited reserves available
  - Budgeting for deficits or adopting the mythical "balanced budget approach"

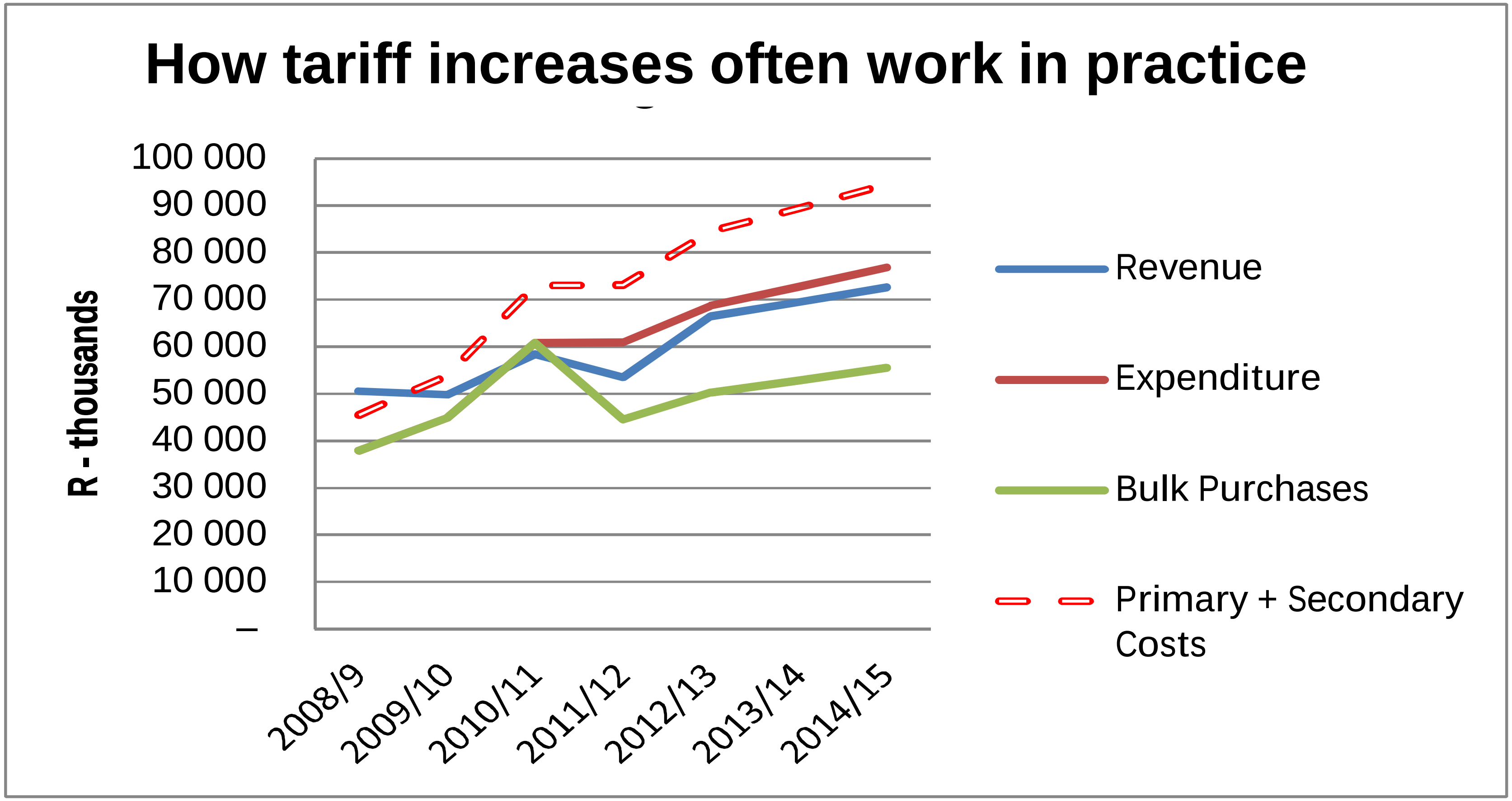
- This is detrimental to financial sustainability and consequently places service delivery at risk

Findings of benchmarking engagements (5)

How tariff increases should work



Findings of benchmarking engagements (6)



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Shortcomings in costing practices

- Engagements were held with the various financial system vendors in order to establish if their systems catered for internal cost recoveries (cost accounting).
- It must be noted that only 40 **%** of municipalities do apply some sort of cost allocation, but the manner in which they allocate direct and indirect costs is weak
- Where municipalities are attempting to cost for services, the calculations are usually limited to direct costs such as remuneration and bulk purchases, with little or no consideration for indirect costs
- The traditional approach of incremental tariff increases is widely applied
- The financial imbalance of basic services is becoming increasingly greater with costs exceeding the revenue generated by service charges.

National Treasury's work to improve tariffing

- Pilot study at uMhlathuze on costing;
- Compilation of costing guidelines;
- Assisted various municipalities with costing and tariff setting;
- Various training sessions to CFO forums & Provincial Treasuries; and
- Inclusion of an additional segment (Management Accounting) in SCOA

Thank you