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National Treasury
REPUBLIC OF SOUTH AFRICA

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Dear Mr Mhlongo

By Email: MhlongoPN@umhlathuze.gov.za

FEEDBACK ON OBSERVATIONS, AND KEY RECOMMENDATIONS EMANATING FROM THE BUDGET ASSESSMENT ENGAGEMENT HELD ON 15 MAY 2025

National Treasury would like to thank the City for the productive engagement we had on Thursday, 15 May 2025 at the national Treasury offices. This letter intends to record the high-level issues and major recommendations, which emanated from the engagement. The document is intended to provide an early version of what will be covered in the main report as explained in the meeting.

The recommendations and decisions should find expression in the City's 2025/26 MTREF budget to be adopted by Council. The purpose of the Budget Engagement was to review the City's tabled 2025/26 Medium-term Revenue and Expenditure Framework as informed by the broader municipal planning and development framework.

The engagement provides the City with an opportunity to obtain guidance from various units within the National Treasury (NT) and relevant sector departments to provide comments on the tabled municipal budget and advise on arrears requiring further review and consideration.

A summation of the observations, recommendations and resolutions emanating from the discussions are presented below.

KEY OBSERVATIONS

Attendance

The NT would like to acknowledge the level of commitment and transparency demonstrated by the leadership of the municipality during the engagement.

The meeting was well represented by the leadership of the City, namely, The honourable Mayor, the City Manager (CM), Chief Financial Officer (CFO), Chief Operations Officer (COO), Deputy City Managers of various portfolio and other senior officials. The Sector Departments in attendance were



the Department of Planning, Monitoring and Evaluation, Department of Cooperative Governance (DCoG), Department of Water and Sanitation, and the South African Cities Network.

A summation of the observations, recommendations and resolutions emanating from the discussions is presented below.

Institutional Arrangement: Sound

- The City's governance structures are functional and the administration as well as the political principals have built a resilient organisation. The City has the most stable coalition in the local government sphere for the tenure of 2021/26 which was demonstrated by the smooth tabling of the 2025/26 IDP and MTREF budget.
- The City's political and administrative domain are stable, and interface was observed during the engagement.
- The City's Political Management Committee (TROIKA), Mayoral Committee, and the Municipal Structures Act Section 79/80 Portfolio Committees are functional and provides the required oversight over the administration of the City.
- The Audit Committee, Performance Audit Committee and the Enterprise Risk Management Committee are functional and provides the necessary oversight.
- The City is led by the permanent CM since 01 April 2025, the Deputy CMs are in place except for the DCM Community Service of which became vacant on 1 April 2025. It was noted that two DCM positions employment contracts are ending in October and December 2025, respectively.
- The Honourable Mayor expressed concerns around the tabling of a budget with a deficit and indicated that the deficit was reduced and added that water losses remain a challenge especially in the Ingonyama Trust Land water supplied arrears. It was noted that City is not opposed to water metering and there are continuous engagements to commerce to roll out of smart meters to curb the high losses which impact the whole of the Institution.
- The City is experiencing challenges whereby large power users are moving out of the grid to opt for alternative source of energy which is a thorny issue that threatens the sustainability of the Institution given that electricity is the amongst the main sources of revenue for the City.
- The City understand the cash constraint environment facing the whole of government and its impact on the City.
- Underfunded mandates continue to impact negatively on its cash resources and the community needs services as they cannot differentiate the duties of Local government and provincial government.
- The National Treasury (NT) noted the vacancy rate of 25 per cent at Top management; senior management 12 per cent of funded positions while middle Management – 19 per cent of funded positions.
- The NT noted that the City has a moratorium on filling Senior and Middle Management positions as part of expenditure management. The critical staff at a lower level are not affected by the moratorium to enable continued service delivery.



- All Senior Managers fulfilled the minimum competency levels and two are awaiting the statement of results from the Local Government Sector Education and Training Authority.
- The City has transition from development to support as it relates to the SAP Enterprise resource planning to automate its processes and to comply with the *mSCOA* requirements. The challenge is the costs of support that are exceeding the initial cost of the financial system.
- The City is commended for considering adopting the institutional arrangements for reforming the trading services aimed at addressing operation inefficiencies. The City plans to prepare separate financial statements for the trading services.
- The employee related costs are proposed at 22.8 per cent of the total expenditure of the 2025/26 budget which is within the norm of 25 per cent to 40 per cent and the City stabilized expenditure on overtime, only planned overtime is approved and are still looking at other avenues to restructure this area.
- The contracted services amount to 8.2 per cent of the total expenditure in the proposed 2025/26 budget. This is out of the norm range between 2 per cent and 5 per cent and the City is committed to manage this area.
- The City raised a concern about the provincial roads that are managed by the Department of Transport as they are seldom maintained and stated that engagements are underway to manage this aspect.
- The City outlined that some of the challenges raised requires the assistance from the other spheres of government. Amongst the challenges raised include:
 - The Ingonyama Trust Land water supplied areas;
 - Human Settlements grant management and insufficient funding;
 - Grants for efficient water and wastewater management;
 - unintended results of the Independent Power Producers on the sale of electricity;
 - Support for local economic development;
 - Eskom electricity supplied areas – for effective debt and credit control management and in processing new connection quicker; and
 - Underfunded mandates for libraries, disaster management, museums etc.
- The City has a process to cascade the Institutional Performance Management System.
- The City is using DDM to raise some of the critical issues that are in the purview of other stakeholders and has built a relationship with the Business Sector for partnering on mutual beneficial areas.

Financial Health: Sound

- The City's proposed budget was assessed as funded over the 2025/26 MTREF.
- The NT raised its concerns about the proposed budget which projected operational deficit over the MTREF budget. The NT alluded that the practice of an operating deficit will set the municipality to a failure and reverse all the historic gains. The city has committed to improve on its operations henceforth.



- The projected revenue collection rate is 95 per cent, and the City has strategies to enhanced revenue collections on all supplied areas including in the traditional land areas and to effective and efficiently manage the operational expenditure.
- The projected cash coverage above one month was seen as a positive and the City was advised to work on moving towards three months. The current ratio is projected above 1.5 which is good so long the current assets always exceed the current liabilities. It is pleasing that the liquid assets exceed the current liabilities.
- The trading services are operating on a deficit except for electricity and refuse thus far and the City is worried about the reduction in electricity sales. The decrease in electricity sales is due to a drop in commercial and industrial consumption because of the transition taken by large manufacturers and commercial businesses to alternative sources of energy and due to a forced transition caused by load shedding. Other customers opt for gas and solar as an alternative source of power. The other major issue is that the local economy has not picked up to the extent anticipated for the City to get more consumers of electricity.
- The City was advised to ensure that projected cash and cash equivalents at year-end amounted are realised.
- The City is trying to rebuild its reserves despite the declining cash coverage and cash and cash equivalents. The City stated that it will turn the situation around as there is a Long-Term Financial Plan that was independently developed which includes reduction of operational expenses by 5 per cent and the reduction of borrowings to manage debt going forward.
- The City has a cost containment policy in place and all the cost drivers are analysed and monitored to manage the expenditures. The City highlighted the cost associated with the security services as most of the critical assets are safeguarded by a human body, however, the City is exploring alternative systems to leverage from, to reduce the costs.
- The City follows a rigorous process to write-off uncollectable debt which is mainly in the rural areas which are Eskom supplied. The City is rolling out the prepaid water meters in rural areas to manage water consumption.
- The council took a resolution to prioritising employees and councillors that are residing in the traditional areas to pay for municipal services. The City is trying to locate the businesses (such student accommodations) in the traditional areas that are connected to the infrastructure system of the City. The City is engaging the relevant stakeholders such as the University of Zululand and unlock payments and curb the exploitation of the loopholes in the system.

Financial Governance: Sound

- The City followed a vigorous public participation process on the reviewed IDP and MTREF Budget. Several participatory sessions were conducted with Amakhosi, Ward Committees, NGOs, Community Development Workers, Business Sector, Sector Departments, and other stakeholders to solicit their views and inputs on the budget.
- IDP Public Participation Report was produced which was analysing community issues and was considered by Council as part of finalising the reviewed IDP and budget.



- There is a clear alignment of the City's priorities with that of the other spheres of government. The City adopted the DDM and is actively participating in the respective DDM platforms thru its respective assigned Champions at different levels.
- The City is exploring investment opportunities and have partnered with strategic partners to improve services and to grow the City. The Economic Development facilitates business support initiatives in partnership with other stakeholders such as Department of Small Business Dee
- The City demonstrated the synergy between its priorities and those emanating from the public participation process.

Service Delivery: Fragile

Service delivery pillar was assessed to be fragile due to the following key indicators which cannot be ignored:

- The projected total capital expenditure to total expenditure (capital plus operational) amounted to 4.6 per cent which is below the norm range between 10 per cent and 20 per cent and was raised as a concern. This ratio is a key service delivery indicator as it measures the prioritisation of expenditure towards current operations versus future capacity in terms of Municipal Services. NT's interpretation is that lower projections of CAPEX spending by the municipality in infrastructure holds potential risks to service delivery as the population burdens the current infrastructure on the ground. See our comments below in Blue.
- The City explained that the reduction in the infrastructure investment was properly planned as part of building the capital replacement reserves over a certain period and to ensure sustainability NT understood the reduction of other grants which affected capital expenditure budget, the reduction of other grants such as Human Settlement Grant and Water Services Infrastructure Grant (WSIG) was also noted. The City raised a concern that they were penalised erroneously on WSIG and have written to the NT for reconsideration. The NT advised that a response will be provided. See our comments below in Blue.
- The NT highlighted the variances on the number of households provided with free basic services as compared to the basic service component of the local government equitable share (LGES). The City was advised that more information should be provided in the budget document on this area, as it was understood that in actual the city provides support that exceeds what the LGES provides to the indigents. Agree and will improve the information on the final budget document.
- The City's water losses observed in the 2022/23 and 2023/24 financial year were worrisome being above 50 per cent. The norm is between 15 per cent and 30 percent, respectively. The poor management of illegal connections, leaks, metering were highlighted as a challenge. The explained strategies to manage this area going forward. The electricity losses are projected to be within the norm which is a positive indicator. Agree.



- The City has 19 per cent of sanitation backlogs and is moving with high speed on water access and metering. The City has 6 water tankers and is outsourcing 4 on an emergency basis or ad hoc basis during emergencies. Most other water takers are at the workshop for repairs and maintenance, and the overall status is that the available for service varies per month. **Agree but is NT promoting water tinkering?**
- There are backlogs on both the municipal supply and ESKOM supply area of electricity. Five substations operate beyond capacity compromising the quality and reliability of supply to residential and commercial customers. **See our comments below in Blue.**

NT also observed the following key indicators

- The projected capital budget is funded from grant transfers, borrowing and internal funds (55.6 per cent; 39.5 per cent; and 4.9 per cent respectively) which was observed to be a good mix of funding. The same trend will remain throughout the MTREF with peripheral shifts.
- The borrowing has reduced in comparison with the prior years. The City explained that it planning to build reserves but being conservative on borrowing and on the internally generated funding over the 2025/26 MTREF budget.
- The projected renewal / upgrading of existing asset is 53.7 per cent of total capital exp (NT's guideline is 40 per cent) will decrease and increase over the MTREF outer years which is good as indicates that the city prioritise the existing assets.
- The City was advised to appropriate budget for depreciation and assets impairment. The City explained that their repairs and maintenance percentage is lower than the norm because land from part of the formular.
- The City explained that its capital budget is multiyear and the changes that are seen being above 10 per cent is because of a change in their capital strategy to enable the City's sustainability.
- The City has a Sewer Master Plan that if funded in the 2025/26 MTREF budget. The Wastewater Treatment works are experiencing a challenge due to flooding because of heavy rains and there is a need for upgrades while being cognisant of the cash constraints.
- The City is commended for releasing land and unoccupied building for ease of use by the Community to drive LED support.
- The City urged the NT to review and reconsider the rating on the service delivery pillar given the detailed explanation on areas raised as in short supply during the engagement. The NT explained that the Fragile in terms of this report means that most indicators are good but worrying signs are showing which the City is advised to prioritise. The NT proposed that the City provide more information on areas seen as showing worrying signs before the final main report is finalised to consider the request for reconsideration. **The NT is requested not to use a reduction in capital allocation to the Budget as a primary determinant of service delivery fragility. The capital reduction is in line with both our National Status of the GDP together with the Local Domestic Economy at uMhlathuze. In addition, in line with international asset management standards of an 8% PPE as an operational budget allocation for repairs and maintenance the MTREF has 7.6% allocated which is only marginally below this First World standard. If NT wish**



to retain the fragility stance, then it be requested that such stance be qualified in relation to issues of actual service delivery inefficiencies that were highlighted in the Service delivery presentations.

NT is further requested that matters that relates to housing function which is not the City's function to be part of the assessment when the City has no control over the funding, to part of the fragile assessment. Similarly, with the WSIG funds which were erroneously withheld by National Treasury, the City is of the view that NT reconsider making that to be part of assessing service delivery when in actual fact the municipality had spent the entire allocation.

With regards to electricity supply, the City does not have any backlogs in its licenced area of supply and therefore this can not be attributed to fragile assessment. The backlogs the City mentioned is where Eskom is responsible for electrification, which outside the City's mandate nor its control.

- Overall, the city was commended for the good process and output of the review IDP and tabled 2025/26 MTREF budget and for the pleasant working relationship.

CONCLUSION

- The City thanked all participants for the continued support and for the useful and fruitful engagement.
- The NT appreciates the City's efforts in terms of preparation, sharing of information timely, and willingness to engage in a frank, honest, and robust manner in the engagement. The NT also thanked the Honorable Mayor for his attendance and for observing the proceedings.

RECOMMENDATIONS

- The NT Budget Engagement meeting to begin with the previous year recommendations and resolutions to track and measure progress and avoid repeating same recommendations.
- The NT will process the letter received regarding the WSIG and report back to the City in due course;
- The City to write a letter to the NT on the proposed reform to standardise the cost related to the procuring and acquisition of goods and services from the market to manage the high cost of purchase by the government generally;
- The City to consider developing and approving a policy to give authority to implement the targeted approach to collect revenues in the traditional land supplied areas and ensure a through consultation process;
- The City to consider the transversal contract for smart meters to address the viability of water service;
- The NT and the City to engage on the technical aspects raised related to the assessed budget;
- The NT to continue looking for a lasting resolve on the underfunded mandates;



- The NT to look at further ways to assist municipalities with available conditional grants for municipal infrastructure development'; and
- The City to continue discussions with other Sector Departments on aspects that cut across different spheres of government and parastatals such as ESKOM;
- The City is advised to consider tabling this summation at the municipal council for noting.

Yours faithfully

MATJATJI MASHOESHOE
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DATE:

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