UBUNTU MUNICIPALITY INVESTMENT MANAGEMENT POLICY

INTRODUCTION

Section 13(1) of the Municipal Finance Management Act, Act 56 of 2003, stipulates that the Minister of Finance, acting with the concurrence of the Cabinet member responsible for local government, may prescribe a framework within which municipalities must –

(a) conduct their cash management and investments; and
(b) invest money not immediately required.

Section 13(2) of the Municipal Finance Management Act requires that a municipality establish an appropriate and effective cash management and investment policy in accordance with any framework that may be described by the Minister of Finance.

The draft Municipal Investment Regulations, published in April 2004, provides further direction in regard to the development, approval and implementation of an investment policy at a municipality.

DEFINITIONS

The Municipal Finance Management Act defines **investment** in relation to the funds of a municipality, as –

(a) the placing on deposit of funds of a municipality with a financial institution; or
(b) the acquisition of assets with funds of a municipality not immediately required, with the primary aim of preserving those funds.

The draft Municipal Investment Regulations, published in April 2004, defines **investment** as the placing on deposit of money or the acquisition of securities, using money not immediately required, with the primary aim of preserving capital in order to meet future obligations.

Municipality refers to the Ubuntu Municipality, a local municipality established in terms of Section 12 of the Municipal Structures Act, Act 117 of 1998 as amended with a plenary executive system combined with a ward participatory system in terms of Section 9(f) of the Municipal Structures Act.

Council refers to the municipal council of the Ubuntu Municipality and **councillor** to any member of the Municipal Council.
Mayor refers to a member of the municipal council elected to preside at meetings of the Council in terms of Section 37(a) of the Municipal Structures Act.

Chief Financial Officer refers to the departmental head that manages the finance function within the Municipality and includes an employee that acts in his/her stead.

Municipal Manager refers to the accounting officer of the Municipality, appointed in terms of Section 55 of the Municipal Systems Act, Act 33 of 2000, as amended.

Department refers to any organisational component within a municipality that is managed by a head of department appointed in terms of Section 56 of the Municipal Systems Act, Act 33 of 2000, as amended.

Finance Management Act refers to the Local Government: Municipal Finance Management Act, Act 56 of 2003.

Regulations refer to the draft Municipal Investment Regulations as published in April 2004 in terms of the Municipal Finance Management Act.

Structures Act refers to the Local Government: Municipal Structures Act, Act 117 of 1998, as amended.

Systems Act refers to the Local Government: Municipal Systems Act, Act 32 of 2000, as amended.

FRAMING AN INVESTMENT POLICY

Legislative Requirement

In terms of the draft Regulations as published in April 2004, each municipal council shall adopt by resolution an investment policy regarding the investment of its money not immediately required. The investment policy must –

(a) be written;
(b) emphasise primarily safety of the principal and liquidity; and
(c) include –
  - (i) delegation of authority;
  - (ii) details of the scope of the policy;
  - (iii) investment principles and ethics;
  - (iv) a list of approved investments;
  - (v) a list of qualified institutions;
  - (vi) investment diversification;
  - (vii) competitive selection of institutions;
  - (viii) internal control procedures;
  - (ix) reporting and monitoring requirements; and
  - (x) review of the policy.

Standard of Care

Investments must be made with such judgement and care, under the prevailing circumstances, as a person of prudence, discretion and intelligence would exercise in the management of his or her own affairs, not for speculation, but for investment. The primary regard in making an investment must be the probable safety of the capital; in the second instance due cognisance taken of liquidity needs and finally the probable income to be derived.

Investments of money not immediately required must be governed by the following objectives, in order of priority:

(a) Preservation and safety of the principle amount invested;
(b) Liquidity; and
(c) Yield

The standard of care to be applied therefore prioritises the needs to ensure that the Municipality is not exposed to any capital losses; therefore no investments must be undertaken that has a speculative element in it. Liquidity refers to the availability of funds from the investment when they are needed; therefore aligning investment terms with the periods of surplus funds is an important element in this regard. Yield refers to the return on the investment; in most cases this comprises of investment income. Generally speaking the yield on an investment increases with the term of the investment although in a period of generally declining interest rates this may not always be true.

Delegation of Authority

The Ubuntu Municipality has a plenary executive system; in terms of the delegation of authority policy adopted by the Council all decisions regarding the investment portfolio haven been retained by the Council. From a practical perspective, the administration of the investment portfolio is the responsibility of the Chief Financial Officer. The Council therefore must determine, with due regard for any legal requirement –

(a) the amount to be invested;
(b) the date when it is to be invested;
(c) the period during which it will be invested; and
(d) at which institution the investment will be made.

The Chief Financial Officer is responsible to provide the information for and facilitate the investment decisions made by the Council. This responsibility entails, among others, the management of the cash flow of the Municipality, securing options from registered institutions with regard to proposed investments, developing recommendations with regard to investment options available and undertaking the administration of the investment portfolio.

Scope of the policy

Cash flow management forms the key to identifying opportunities for investment from operational activities. When the annual budget for the Municipality is tabled, it must be accompanied by a cash flow projection reflecting anticipated revenue and expenditure per month for the ensuing financial year (this is required by Section 17(3)(c) of the Finance Management Act. Since revenue received and expenditure incurred are not necessarily aligned, the cash flow projection will indicate a number of cash flow surpluses (where revenue exceeds expenditure) and cash flow shortages (where expenditure exceeds revenue). Cash flow surpluses provide an opportunity to invest surplus funds at more favourable rates of return than if they are left in the Municipality’s current account. Cash flow projections must be updated on a monthly basis reflecting actual revenue received an expenditure incurred in the month of review and projecting forward to review future cash flow surpluses and shortages.

In addition to operational cash flow surpluses, funds for investment are derived from three other primary sources;

(a) Investing of funds received by the Municipality for a specific purpose or project until such time as the funds are required for disbursement to achieve the specific purpose for which they were received or to complete the project for which they were allocated;

(b) Funds allocated for specific reserve funds such as the asset replacement reserve are to be underwritten by an investment to ensure that the funds are available when required; and

(c) Any other surpluses, generated by the Municipality as part of its normal activities that have not been earmarked for a specific purpose.

The interest earned from the investments undertaken for a specific purpose of project or to underwrite a specific reserve fund accrues to the funding source concerned; in the other two cases any interest earned forms part of operational revenue that can be used to defray operational expenditure.

The investment policy of the Municipality is therefore aimed at getting the optimal return on investments, without incurring undue risks, during those periods when cash revenues are not needed for capital or operational purpose. The effectiveness of the investment policy is dependent on the accuracy of the municipality's cash management programme, which must identify the amounts surplus to the municipality's needs, as well as the time when and period for which such revenues are surplus.

The scope of the investment policy therefore covers all situations where the Municipality has funds available which are not needed immediately and could be invested. Depending on the circumstances some funds could be invested in the long term while others would only be short-term investments. Surplus funds in the current of the Municipality can be invested for short periods (a short as a single day if that is appropriate).

Investment Principles and Ethics

- Before an investment decision is made, the Council must consider the Municipality's cash needs. The Municipality must align its investment portfolio with its cash flow requirements. It is unacceptable for the Municipality to have funds tied up in an investment and then have to raise an overdraft in order to effect payment of known expenditure.

- When funds are kept in current accounts, it is possible to bargain for more beneficial rates with financial institutions with regard to deposits, for instance a call deposit. Fixed deposits have the effect of further increasing these rates of return. The most important factor is that the amount of cash held in the current account/s of the Municipality must be kept to an absolute minimum.

- The Council of the Municipality will only place investments with locally based financial institutions.

- Council may at its discretion make use of specialist advisors to provide advice on investments from time to time. Specialist advisors are not entitled to earn commission form the Municipality. Furthermore, specialist advisors may not directly invest funds on behalf of the Council; the administration of all investment transactions is the responsibility of the Chief Financial Officer.

- No member of Council or official may, either directly or indirectly, receive any return of monetary value for influencing the placement of an investment with a specific institution, excluding collateral investments made by the Municipality at an approved financial institution to enable officials to obtain housing loans.

- The responsibility and risk arising form any investment transaction vests in the Council of the Municipality.

- Where large sums of money are available for investment, the Council must ensure that these funds are invested with more than one financial institution, where practical, in order to limit the risk exposure of the Municipality. The Council must further ensure that, as far as it is practically and legally possible, the Municipality's investments are distributed so that more than one investment category is covered (for example – call deposits, money market investments and fixed deposits).

- It can be accepted as a general rule for investment that the larger the return indicated by the institution, the greater the risk to the Municipality. Although the objective in making investments on behalf of the Municipality must always be to obtain the best interest rate on offer, this consideration must be tempered by the degree of risk involved in regard to both the financial institution and the investment instrument concerned. No investment can be made with a financial institution where the degree of risk is perceived to be higher that the average risk associated with investment institutions. Deposits may only be made with registered deposit-taking institutions as indicated below.

- The Council of the Municipality may not borrow funds for reinvestment as this would require that future interest rates have to be estimated; this involves speculation and is not allowed.

- Whenever a long term loan (non-annuity) is raised by the Municipality, the Chief Financial Officer: shall ensure that an amount is invested annually at least equal to the principal sum of the loan divided by the period of the loan. The purpose of this procedure is to ensure that the capital sum to be repaid is held in an investment which investment can only be used for the redemption of the loan on the due date.

- If the Chief Financial Officer recommends to the Council that an investment is placed with a particular financial institution, he/she must ensure that the financial institution is registered in terms of the Banks Act, Act 94 of 1990, or is an approved financial institution as determined by the Minister of Finance from time to time.

- When recommending to Council that an investment is placed at a particular financial institution, the Chief Financial Officer must ensure that at least the capital amount invested will be repaid on the maturity of the investment and he/she must exercise due diligence in this regard.

List of Approved Investments

The Regulations outlined what are described as permitted investments. The following investments, as may be appropriate to the future needs for funds, may be undertaken in accordance with the provisions of the Regulations:

(a) Securities issued by the National Government;

(b) Listed corporate bonds with an investment grade rating from an internationally recognised credit rating agency;

(c) Deposits with banks registered in terms of the Banks Act, Act 94 of 1990;

(d) Deposits with the Public Investment Commissioners as contemplated by the Public Investment Commissioners Act, Act 45 of 1984;

(e) Deposits with the Corporation for Public Deposits as contemplated by the Corporation for Public Deposits Act, Act 46 of 1984;

(f) Banker's acceptance certificates or negotiable certificates of deposit of banks registered in terms of the Banks Act, Act 94 of 1990;

(g) Guaranteed endowment policies entered into with the intention of establishing a sinking fund; and

(h) Repurchase agreements with banks registered in terms of the Banks Act, Act 94 of 1990.

The Minister of Finance may by notice in the *Government Gazette* determine investments other than those listed in the Regulations in which a municipality may invest, after the suitability of the investment(s) for use by municipalities has been approved by the Financial Services Board.

List of Qualified Institutions

The list of approved investments reflected above also indicates the nature and type of institutions where municipalities can place surplus funds or funds not immediately required on investment. Notwithstanding the list of permitted investments, the Regulations require that the Municipality take all reasonable and prudent steps, consistent with this investment policy and in accordance with the standard of care stipulated above, to ensure that it places its investments with credit-worthy institutions.

When investments are placed with smaller registered financial institutions, the Chief Financial Officer is responsible to ensure that the Municipality is not exposed to too much risk. The Chief Financial Officer has to ensure that the creditworthiness and the performance of the institution has remained stable, thereby limiting the risk attached to the investment made by the Council of the Municipality within acceptable norms. In order to achieve this objective, the Chief Financial Officer is entitling to information from financial institutions from which the creditworthiness can be determined. This information must be obtained by the Chief Financial Officer and analysed at least on an annual basis. Where such analysis indicates that the creditworthiness of a financial institution has declined to an unacceptable level of risk, the Chief Financial Officer must recommend to Council that any investments with the institution be liquidated.

Investment Diversification

The Council of the Municipality must take all reasonable and prudent steps, consistent with this investment policy and according to the standard of care outlined above, to diversify its investment portfolio across financial institutions, types of investment and investment maturities. The following guidelines must be adhered to ensure appropriate investment diversification:

- Long-term investments should be made with an institution of minimum BBB rating (where BBB refers to lower risk institutions);
- Short-term investments should be made with an institution of minimum B rating (where B refers to higher risk institutions than stipulated for long term investments);
- Not more than 20% of available funds for investment should be placed with a single financial institution; and
- The amount invested at a financial institution should never exceed 10% of the relevant institution’s shareholder funds (capital and reserves).

Competitive Selection of Institutions

After determining whether there is cash available for investment and establishing the maximum term for each potential investment, the Chief Financial Officer must develop a recommendation to Council of the way in which the investment is to be made.

Quotations should be obtained form a minimum of three financial institutions, bearing in mind the limits of the term for which it is intended to invest the funds. Should one of the institutions offer a better rate for a term other than what the Municipality had in mind but which can be accommodated, the other institutions approached should also be asked to fix a rate for that term.

It is acceptable to ask for quotations telephonically, by facsimile or by electronic mail, as interest rates generally change on a regular basis and time is the determining factor when investments are made. However, once a quotation has been received by any of the means noted, it must be confirmed by the institution in writing immediately (an original document). The person responsible for requesting quotations as required by this policy must complete the quotation register and record the following –

- Name of the institution;
- Name of the person at the institution providing the quoted rate;
- Period of the investment;
- Interest rate quoted;
- Payment of interest consideration, if applicable – interest received or an maturity of the investment; and
- Any other terms, stipulations or requirements indicated by the institution.

Once the required number of quotations has been obtained, the Chief Financial Officer must review the quotation register and prioritise the quotations received. The Chief Financial Officer is required to review only those quotations as received and no attempt must be made to influence institutions to further compete with each other as far as their rates and terms are concerned. The interest rates quoted by a financial institution for a proposed investment are not to be divulged to competitive institutions.

A recommendation is then prepared for Council to make a decision with regard to the proposed investment; once the decision has been made the institution concerned will be informed. Where the investment decision is not in accordance with the most favourable quotation received, the Chief Financial Officer shall endorse on the most favourable quotation the reason/s for not taking up the investment. An endorsement shall also be made in the quotation register indicating which quotation has been accepted for a particular investment. All quotations received are to be retained and filed for audit purposes.

The Auditor General requires that the financial institution where the investment is placed provide the Municipality with a certificate for each investment. The Chief Financial Officer must ensure that the investment certificate received is a genuine document, issued by the financial institution concerned, and the investment capital must only be paid over to the institution with which it is invested.

Internal Control Procedures

The Municipality is required to maintain an investments register, reflecting the details of all investments made by the Council of the Municipality – the control and updating of the investment register is the responsibility of the Chief Financial Officer. The investment register must reflect at least the following pertinent information –

- Name of the financial institution where an investment has been placed;
- The capital amount invested;
- The date on which the investment was made;
- The interest rate applicable on the investment;
- The date of maturity of the investment;
- The amount of interest earned on the investment;
- The capital amount received from the financial institution;
- Details of the reinvestment of funds, where applicable; and
- Any other relevant remarks or comments on the investment.

It is the responsibility of the Chief Financial Officer to ensure that the investment register and the accounting records of the Municipality are reconciled on at least a monthly basis.

Interest, corrected calculated, must be received timeously from the financial institution concerned, and together with any capital redeemed, if applicable. The Chief Financial Officer or his/her delegate must ensure that the interest received on investments made is calculated correctly by the financial institution/s concerned.

The investment register must be reviewed by the Chief Financial Officer at least twice every calendar month to determine any investment made by the Municipality that mature within the next two weeks. Once the Chief Financial Officer has established that the funds invested are not immediately required to defray expenditure, the process of obtaining quotations and framing a recommendation to Council to make a decision to reinvest the funds commences. Should the invested funds be required to defray expenditure, they will be applied accordingly once the investment matures and an endorsement made to that effect in the investment register.

Investment documents and certificates are to be safeguarded by keeping them stored in a fire resistant safe, access to which is appropriately restricted. The following documents must be safeguarded:

- Fixed deposit letter of confirmation or investment certificate;
- Any receipts issued by financial institutions for capital invested;
- Copy of an electronic transfer or cheque requisition confirming the investment of funds;
- The investment register;
- The quotation register;
- All reports issued in respect of the investment portfolio held by the Municipality with particular reference to comparative reports prepared; and
- Any certificates issued by financial institutions confirming that no commission was paid on the placing of the investment.

Reporting and Monitoring Requirements

The reporting requirements on the investment portfolio of the Municipality are prescribed by the Regulations. In terms of the Regulations, the accounting officer of the Municipality must, within 10 working days of the end of each month, submit to the Mayor a report describing in detail the investment position of the Municipality as at the end of the month. The report prescribed in the Regulations must contain at least a statement, prepared in accordance with generally accepted municipal accounting principles, that gives the –

(a) beginning market value of the investment portfolio for the reporting period;
(b) additions and changes to the market value of the investment portfolio during the period;
(c) ending market value of the investment portfolio for the reporting period; and
(d) details of fully accrued or received interest / yield on the investment portfolio for the reporting period.

The Council of the Municipality must, within 30 days after the placement of an investment with a maturity of 2 months or longer, publish in a local newspaper in circulation within its area of jurisdiction, fully details of the investment that has been made.

At the end of each financial year the Chief Financial Officer shall obtain certificates of confirmation from institutions where investments are held by the Municipality – these are to be made available to the Auditor General for inspection purposes.

At the end of each financial year the Chief Financial Officer shall obtain a certificate from every financial institution with which funds were invested by the Municipality, certifying that no monetary consideration of whatever nature was paid in respect of the placement of investments with the institution and that no advantage accrued or will accrue to any member of Council or municipal official as a result of investments made by the Municipality.

Review of the Policy

This investment policy must be reviewed when changes in legislation impact on the prescriptions contained within the policy; nevertheless, the investment policy should be reviewed and updated, if required, at least on an annual basis.

NOTE:

1. *It is important to ensure that the application of this discount incentive does not result in a loss in income for the municipality.*

2. *If a discount of utility services is offered by the Municipality it must be reviewed periodically to evaluate the financial and administrative the impact of this incentive in real terms.*

3. *Discounts on utility services should only come into effect after the emerging business is in full operation.*

ANNEXURE "B"

APPLICANT REQUIREMENTS

An applicant seeking to qualify for any of the above incentives will have to submit the following documents to the Council:

1. In the case of a company copies of their registration documents and the company's founding documents.

2. In the case of a close corporation copies of their registration documents.

3. Copies of the applicable industrial or commercial licenses.

4. Proof of tax registration and a tax clearance certificate where applicable.

5. Rates and utility accounts.

6. Bank account numbers.

7. Latest audited financial statements or any other appropriate financial documentation on the financial status of the applicant.

8. A business plan detailing the new economic activity or the expansion of an existing economic activity.

9. Any other relevant information that may be required by Council to allow it to arrive at an informed decision.