



Fezile Dabi

District Municipality

Commitments Policy

Date of approval by council:

Council Resolution number:

DEFINITIONS:

Commitment: An undertaking made to commit substantial expenditure at a future date. Such undertakings are deemed constructive obligation and must be disclosed in the financial statements of the municipality even if the expense has not yet been incurred to have become an actual liability.

Approved and Contracted Commitments: where the expenditure has been approved and the contract has been awarded at the reporting date.

Approved but not yet contracted commitments: where the expenditure has been approved and the contract has yet to be awarded or is awaiting finalization at the reporting date.

Capital Expenditure: expenditure incurred to purchase, upgrade or construct physical assets such as buildings for which there will be a long-term benefit. Long-term is defined as longer than one year.

Current Expenditure: the purchase of goods and services for which there will be a short-term benefit and incurred in the normal course of business. Short-term is defined as less than one year.

Constructive obligation: is an obligation that derives from a municipality's actions where:

- (a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the municipality has indicated to other parties that it will accept certain responsibilities; and
- (b) as a result, the municipality has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

1. OBJECTIVES

- a) To ensure that appropriate recognition criteria and measurement bases are applied to commitments.
- b) To ensure that appropriate, sufficient information is disclosed in the notes to the financial statements of the municipality relating to commitments.
- c) To ensure that only genuine commitments are disclosed in the financial statements of the municipality.

2. LEGISLATIVE CONTEXT

Section (62)(1) of Municipal Finance Management Act, 56 of 2003 (MFMA) stipulates that the accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure:

- a) *that the resources of the municipality are used effectively, efficiently, economically and transparently;*
- b) *that full and proper records of the financial affairs of the municipality are kept;*
- c) *that the municipality has and maintains effective, efficient and transparent systems-*
 - i. *of financial and risk management and internal control; and*
 - ii. *of internal audit complying with and operating in accordance with any prescribed norms and standards;*
- d) *that irregular and fruitless and wasteful expenditure and other losses are prevented;*
- e) *that expenditure is in accordance with the operational policies of the municipality; and*
- f) *that disciplinary or, when appropriate, criminal proceedings, are instituted against any official of the municipality who has allegedly committed an act of financial misconduct or an offence in terms of Chapter 15.*

3. POLICY PRINCIPLES

- a) Commitments are not recognised in the statement of financial position as a liability or as expenditure in the statement of financial performance but are included in the disclosure notes.
- b) The Chief Financial Officer must be informed of any material commitment that may arise during the course of the business of the municipality.
- c) The Chief Financial Officer shall, at financial year end, perform an assessment to identify any material commitments so as to ensure the completeness, relevance and accuracy of the commitments that must be recorded and reported at financial year end.

4. COMMITMENTS

4.1 General

Commitments (operating and capital) that must be accounted for shall only relate to those for which an official purchase order was issued or through the execution of a contractual obligation entered into in the name of the municipality.

In the case of a contractual obligation, it is also preferable that the user departments must initiate and facilitate the issuing of an official purchase order in accordance with municipality's Supply Chain Management Policy and Procedures for a commitment to be recognized.

The municipality may enter into a contract on or before the reporting date for expenditure over subsequent accounting periods e.g. a contract for construction of infrastructure assets, the purchase of major items of plant and equipment or significant consultancy contracts. In these events, a commitment shall exist at financial year end as the municipality has contracted for expenditure but no work has started and no payments have been made.

4.2 Financial Year End Commitments

Funding appropriated in an approved budget or adjustment budget for capital works and / or purchases shall be committed in accordance with the Supply Chain Management Policy as well as this Policy.

Funding commitments made by way of official order, contractual or other expenditure obligations (e.g. loans agreements, lease agreements, etc.), which remain substantially, partially or wholly uncompleted (i.e. not commenced) at the end of the applicable financial year shall be reviewed for validity.

Certain issued purchase orders, particularly those which relate to once-off purchases for ordinary operating expenditure, which have been outstanding for more than 60 days and not yet executed at financial year end, shall be officially cancelled at financial year end.

A register of orders to be cancelled must be maintained throughout and updated with each cancellation and must be submitted to the Chief Financial Officer for review and approval prior to any cancellation being effected.

Orders shall be cancelled by the a duly delegated official, after approval thereof by the Chief Financial Officer.

When user departments become aware that commitments for 'recurrent services or multi-year contracts' will necessitate a financial commitment crossing over to the next financial year, the departmental manager must advise the Chief Financial Officer (or delegate) of this likelihood and the reasoning thereto.

Commitments register shall be maintained which will contain all the financial commitments of the municipality throughout the financial year.

Any funds not specifically carried forward by commitment are lost in a budgetary sense at the end of the financial year and it will remain the responsibility of the user departments to re-budget afresh for those services or goods for which orders were cancelled or the budget was not utilized at the end of the financial year.

In calculating commitments the following should be taken into account pertaining to tenders awarded:

- the period of the tender awarded;
- amounts already paid pertaining to that tender/contract;
- amounts for which invoices have been received and which are therefore included in accruals should be deducted;
- commitments loaded on the procurement and contractors register system;
- commitments not loaded on the procurement and contractors register system;

5. DISCLOSURES

The municipality shall disclose as a note to the financial statements, the nature and amount of each material class of capital expenditure commitment as well as non-cancellable operating leases contracted for at the reporting date. Commitments for the supply of inventories, where a liability under a contract or purchase order has not yet been recognised, shall not be disclosed as a commitment.

The foregoing disclosure requirement does not divest the municipality from maintaining a commitments register for material, operating commitments for each financial year.

6. REVIEW AND APPROVAL

This policy and underlying strategies will be reviewed at least annually, or as necessary, to ensure its continued application and relevance.

ANNEXURE A: EXAMPLE OF THE REQUIRED DISCLOSURE NOTE FOR CURRENT AND / OR CAPITAL COMMITMENTS:

	200x/0x	200x/0x
Current expenditure		
Approved and contracted		
Approved but not yet contracted		
Capital expenditure		
Approved and contracted		
Approved but not yet contracted		
Total commitments		
The expenditure will be financed from:		
External Loans		
Capital Replacement Reserve		
Government Grants		
Own Resources		

ANNEXURE B: GUIDANCE TO DETERMINE WHETHER A COMMITMENT EXISTS AT REPORTING DATE.

Commitments represent goods/services that have been ordered, but for which no delivery has taken place at the reporting date. These amounts are not recognized in the statement of financial position as a liability or as expenditure in the statement of financial performance, but are however disclosed as part of the disclosure notes.

- Items are classified as commitments where the municipality commits itself to future transactions that will normally result in the outflow of resources.
- Contracts that are entered into before the reporting date, but for which goods and services have not yet been received are disclosed in the commitments disclosure note to the financial statements.
- Material contracts entered into after the reporting date but prior to the approval of the financial statements must be disclosed under subsequent events and in the report of the Accounting Officer.
- Other commitments for which disclosure is necessary to achieve a fair presentation should be disclosed in a note if both the following criteria are met:
 - contracts should be non-cancellable or only cancellable at significant cost (for example, contracts for computer or building maintenance services); and
 - contracts should relate to something other than the routine, business of the municipality – therefore salary commitments relating to employment contracts or social security benefit commitments are excluded.