



## KZN PROVINCIAL TREASURY

### *KZN MUNICIPAL CIRCULAR NO 01A/2016*

### **APPLICATION OF REGULATION 32 OF THE MUNICIPAL FINANCE MANAGEMENT ACT, 2003: SUPPLY CHAIN MANAGEMENT REGULATIONS**

#### **1. Background**

It has been established through the implementation of the contract management system at Municipalities that the prescribed processes as stipulated in the MFMA SCM Regulation 32, in respect of procurement of goods and services under contracts secured by other organs of state, are not being adhered to and are being abused. There seems to be a general lack of understanding or confusion with regard to the process to be followed when procuring goods and services through Regulation 32 or under what circumstances the Municipality can make use of the same.

The roll out of the contract management system to Municipalities has revealed the following:

- a) Some Municipalities adopt contracts from other organs of state without entering into a contract with service providers;
- b) The scope of work is not the same with the original contract
- c) Municipalities participate in contracts that have already expired; and
- d) There is no evidence to prove that the contract was procured by another organ of the state by means of a competitive bidding process.

Based on the above mentioned findings, it became apparent that Regulation 32 is being used incorrectly by a number of Municipalities to undermine the provision of Section 217(1) of the Constitution and Section 112(1) of the Municipal Finance Management Act which requires a system that is fair, equitable, transparent, competitive, and cost effective.

This circular aims to provide Accounting Officers with guidance on the interpretation of Regulation 32 and the process to be followed. Furthermore, it also aims at creating a situation where Municipalities are deterred from flouting the rules arbitrarily.

**2. Procedure for the application Regulation 32**

Procurement by way of regulation 32 should be considered as a last resort and only if the circumstances meet the requirement of Regulation 32(1).

The Accounting Officer of a Municipality must first obtain consent from Provincial Treasury before he/she finalizes and agreement with another organ of the state and the identified service provider. The role of the Provincial Treasury would be to assess the reasons given by the Accounting Officer not to advertise the bid and to do an assessment of the relevant documents to ensure compliance.

The above procedure also gives effect to MFMA SCM Regulation 38(1) which requires the Municipality to have measures in place for the combating of abuse of the Supply Chain System.

A detailed process to be followed by municipalities in the application and Implementation of Regulation 32 is detailed in Annexure A hereto.

**3. Authority for this Circular**

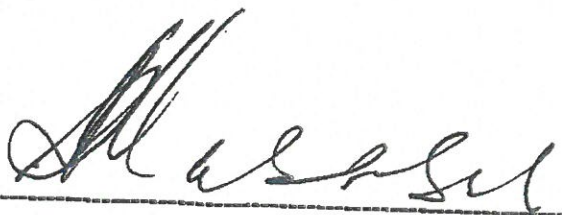
This KZN Municipality Circular is issued in terms of Sections 3(b) and 3(c)

**4. Effective Date**

This KZN Municipality Circular takes effect from the 1<sup>st</sup> May 2017.

**5. Contact Information**

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**treasury**

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Department:

Treasury

**PROVINCE OF KWAZULU-NATAL**

**ANNEXURE A TO CIRCULAR 01A/2016: APPLICATION OF REGULATION 32 OF THE MUNICIPAL FINANCE MANAGEMENT ACT, 2003: SUPPLY CHAIN MANAGEMENT REGULATIONS**

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## **1. Purpose**

The purpose of this guideline is to provide a guiding process for KwaZulu-Natal municipalities and municipal entities in the implementation of MFMA SCM Regulation 32. The guide further aims to strengthen contract management and records keeping for contract documents.

## **2. Introduction and Background**

Regulation 32 of the MFMA SCM Regulations makes provision for municipalities and municipal entities to procure goods and services from contracts secured by other organs of state. The Regulation further sets minimum requirements which must be confirmed by the accounting officer of the procuring municipality or accounting authority of the procuring municipal entity. Regulation 32 requires the accounting officer or authority to satisfy him or herself of the following:

- That the contract under which the municipality or municipal entity wishes to procure goods or services has been secured through a competitive bidding process;
- That the municipality or municipal entity has no reason to believe that the contract was not procured validly;
- That there are demonstrable discounts or benefits for the municipality or municipal entity to procure through Regulation 32; and
- That the other organ of state and service provider has consented to such procurement.

Procurement through this Regulation has resulted in substantial irregular expenditure for municipalities and municipal entities over the last financial years. The bulk of the findings relate to original contract documents not being available for audit purposes as well as difficulty faced by municipalities in proving the demonstrable discounts or benefits in terms of sub-regulation 32 (1) (c) of the MFMA SCM Regulation.

The provincial treasury has identified the absence of a clear guide for the correct implementation of Regulation 32 as an ongoing material risk for irregular expenditure in municipalities and municipal entities. The successful implementation of this guide can lead to the termination of the risk associated with Regulation 32 contracts.

## **3. Procedure for MFMA SCM Regulation 32 Procurement**

The essence of Regulation 32 procurement must be based in particular on sub-regulation 32 (1) (c) which requires that municipalities and municipal entities demonstrate discounts or benefits which the municipality or municipal entity will reap from such procurement. While important, the other requirements in terms of Regulation 32 are mostly administrative in nature.

### 3.1. Demonstrable Discounts

Demonstrable discounts can only be measured in financial terms. This means that the only method to demonstrate financial discounts is through an ordinary procurement process that will result in financial offers for a specific product/s or service/s. In the case where the municipality is or becomes aware of a contract where a lesser fee or price is paid by another organ of state, the municipality or municipal entity may then approach the organ of state for Regulation 32 procurement. The following process shall apply in the case of "demonstrable discounts."

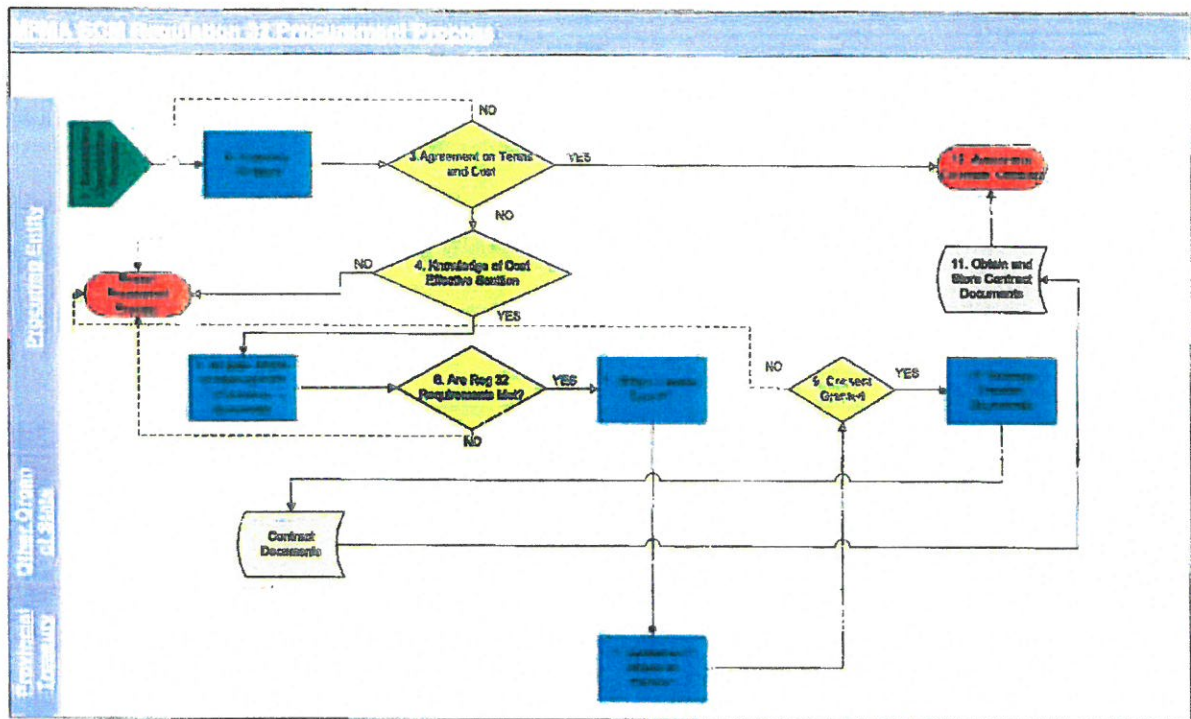


Figure 1: Process for Regulation 32

#### 3.1.1. Conclusion of Competitive Process

The trigger for demonstrating discounts is the conclusion of a competitive bidding process for procurement of goods, services and/or works. MFMA Circular 62 requires all municipalities to compile a procurement plan for procurement activity that is expected to exceed R 200, 000.00 including VAT. All projects are therefore, ordinarily, expected to go through a competitive bidding process in order to obtain the best fit solution for our requirements and to obtain competitive prices and cost effectiveness.

#### 3.1.2. Contract Negotiation

After the procurement process, the Accounting Officer/Accounting Authority or his or her delegate must negotiate the terms of the contract. The price of the contract, amongst other things, must be

concluded at this stage. The outcome of the negotiation will determine whether a contract will be concluded between the municipality or municipal entity and the preferred provider.

#### **3.1.3. Decision – Agreement Concluded**

A key decision must then be taken with regards to the next course of action:

- No – Should the municipality or municipal entity fail to conclude a contract with the preferred provider, the municipality or municipal entity may opt to cancel the process, review the requirements and re-advertise;
- No – Should the municipality or municipal entity fail to conclude a contract with the preferred provider, the municipality or municipal entity may assess whether it is aware of a more cost effective and valid contract that another organ of state may have concluded;
- Yes – Should the municipality or municipal entity and the preferred provider agree on terms, the municipality or municipal entity may then award the contract to the successful bidder.

#### **3.1.4. Decision – Knowledge of Cost Effective Solution**

A further decision has to be made depending on the outcome of 3.3 above:

- No – Should the municipality or municipal entity be unable to identify a more cost effective solution, the municipality or municipal entity may opt to review the requirements of the initial bid and re-advertise;
- Yes – Should the municipality or municipal entity identify a valid contract secured by another organ of state, the municipality or municipal entity must prepare to engage the relevant organ of state as well as the contracted provider.

#### **3.1.5. Engage the Municipality and Contracted Provider**

A key element to the validity of a Regulation 32 appointment is the Accounting Officer/Accounting Authority satisfying him or herself that all the requirements of Regulation 32 (1) (a), (b) and (d). To this end, the Accounting Officer/Accounting Authority or his or her delegated official or committee, must engage the relevant organ of state on the process followed in the appointment of the contracted provider. Furthermore, the Accounting Officer/Accounting Authority, delegated official or committee must be satisfied that both the organ of state and contracted provider consent to such appointment. At this stage, the negotiation or engagement is preliminary and informed by regulatory due diligence more than the conclusion of a contract. This means that no contractual undertakings must be made by the applying municipality or municipal entity.

#### **3.1.6. Decision – Are Regulatory Requirements Complied with**

On the basis of the engagement with the relevant organ of state and outcome thereof, the Accounting Officer/Accounting Authority must then determine whether the regulatory requirements are met:

- No - Should the Accounting Officer/Accounting Authority be unable to satisfy him or herself that all regulatory requirements are complied with, the municipality or municipal entity may opt to review the requirements of the initial bid and re-advertise;
- Yes – Should the Accounting Officer/Accounting Authority be satisfied that all regulatory requirements are complied with, the municipality or municipal entity may approach provincial treasury to obtain consent in terms of Circular 01A of 2016.

#### **3.1.7. Obtain Consent from Provincial Treasury**

The next step is for the Accounting Officer/Accounting Authority to prepare a submission to obtain consent to apply Regulation 32 procurement in terms of Circular 01A of 2016. The prepared submission should include the following;

- Background – A brief description of the initial process followed by the municipality or municipal entity prior to seeking appointment in terms of Regulation 32; and
- Review of Relevant Organ of State Documents – A descriptive process that the Accounting Officer/Accounting Authority followed to review documents to determine whether Regulation 32 would be fully complied with during procurement.

#### **3.1.8. Response from Treasury**

Provincial treasury will assess the reasons and validity of the request for consent and revert to the relevant institution within 5 working days of receipt of submission. In its assessment, provincial treasury will check whether all requirements in terms of Regulation 32 and the process outlined here above have been met. It must further be noted that submission for Regulation 32 procurement on the basis of an urgent or emergent requirement will not be considered as Regulation 36 of the MFMA SCM Regulations already provides for cases where it is impractical or impossible to follow the normal SCM process.

#### **3.1.9. Decision – Has consent been granted**

Depending on the outcome of the response from provincial treasury, the Accounting Officer/Accounting Authority must determine the next course of action;

- No – Should consent not be granted by provincial treasury, the municipality may opt to review the requirements of the initial bid and re-advertise;
- Yes – Should consent be granted, the Accounting Officer/Accounting Authority or a delegated official or committee may engage the relevant municipality for the copying of contract files as well as to initiate meetings to conclude contract

#### **3.1.10. Request Contract Documents**

Once consent has been obtained from provincial treasury, the Accounting Officer/Accounting Authority or his or her delegated official or committee must engage the relevant organ of state to submit all contract data and documents relating to the appointment of the contracted provider as well as consent for the municipality or municipal entity to procure using the same contract. Both the Accounting Officer/Accounting Authority of the granting organ of state and the contracted provider must sign the granting of consent.



#### **3.1.11. Obtaining of Contract Documents**

Once the Accounting Officer/Accounting Authority is in receipt of the relevant documents referred in 3.10 above and is satisfied that all requirements in terms of Regulation 32 are met, the Accounting Officer/Accounting Authority and/or delegated officials or committee(s) may proceed to negotiate the final terms of the agreement with the appointed provider.

#### **3.1.12. Conclude and Award Contract**

Finally, the Accounting Officer/Accounting Authority, having satisfied him or herself that the necessary due diligence was conducted by him or herself or delegated officials or a delegated committee, and that all regulatory requirements are complied with, may award the contract in terms of Regulation 32.

### **3.2. Demonstrable Benefits**

Demonstrable benefits do not necessarily translate to financial benefits or discounts. As a result, in assessing requests for consent from municipalities and municipal entities, provincial treasury will apply its mind to the individual merits of each request. It must be stressed that demonstrable benefits must be such that following a normal competitive procurement process would not yield the same or similar benefit.

## **4. Applicability and Effective Date**

This guideline is issued in terms of Circular 01A of 2016 and it applies to all municipalities and municipal entities in KwaZulu-Natal. This guide comes into effect on 01 April 2017.

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