Compliance: The challenge of change by Janet Channing, MD: Metgovis and Mashilo Pitjeng, MD: TseboREAL Asset Management

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We started 2015 with a prediction of slower economic growth of 2,3%. Production growth will continue to be impeded by power shortages, high operating costs and weak global demand for commodities. Government plans to reduce the budget deficit and stabilise debt-to-GDP using a combination of expenditure reductions and higher tax revenue. VAT hikes, wealth taxes and fuel levy adjustments have been mooted as avenues to bolster revenue receipts. The bottom line is that local government must become more resilient and robust with their revenue strategies.

The current municipal revenue models are heavily biased towards billing and collections from utilities and rates revenue. These sources are augmented by various grants. Although there is some level of revenue benefits from investment assets, there are very few well-structured portfolios. The Amendment to the Municipal Property Rates Act was promulgated on 28 November 2014, effective from 1 July 2015. Municipalities must react by altering the prism through which they view their revenue strategies.

The most immediate implication is the phasing out of certain categories of public service infrastructure, PSI. The present provision allows for the first 30% of the market value of the PSI to be impermissible, that is, no rating is allowed. The amendment provides for rating on all roads, rail, water and airport categories of public service infrastructure to be phased out over a period of five years, starting 1 July 2015, with a 20% reduction. The dent in the municipal coffers will be gradual but relentless.

What replacement revenue strategies are being considered?

In terms of the MPRA amendments, municipalities must, in their next general valuation roll, comply with the prescribed categories. There is a period of seven years for compliance. That sounds like a long time away but municipalities need to plan carefully for this implementation. The most impactful change is the creation of a public service purpose (PSP) category. This is defined as any property which is owned by the State and used for public service purposes. It includes hospitals and clinics, schools, pre-schools, early childhood development centres or further education and training colleges, national and provincial libraries and archives, police stations, correctional facilities or courts of law.

The Department of Public Works is very excited. It makes sense that our hospitals, which provide facilities to care for our sick and our schools where our children are educated, should receive preferential rates. The regulations prescribing the ratio which would be applied to this category are not in the public domain. Hearsay fuelling discussion is that the rates revenue from PSP will be dramatically diminished. So we need to plan ahead.

Let us look at municipal revenue potential from real estate. There are four real estate portfolios within any municipality: A tiered approach for unpacking each portfolio results in a different perspective. Take sports and recreational facilities owned by the municipality. We are all aware that the rentals paid for these facilities are invariably way below market value. These facilities cost municipalities a fortune in maintenance and grass cutting.

Portfolio	Revenue source
Municipal-owned portfolio (asset register)	Yields and lease income, social benefits
Privately-owned assets (valuation roll) and financial system	Property rates and utilities revenue
Government-owned assets	Rates and utilities from government-owned properties
Investment assets (balance sheet)	Interest income and capital returns

The benefit to the community is intangible but invaluable. How do we turn this around? Options include renting the facility to the community or ratepayer association for a nominal amount and including the maintenance of the property in the agreement.

The best practice indicates that each of these portfolio entities should be individually analysed. A strategic plan should be developed to combine the information to achieve the objectives of revenue optimisation. Quality assurance and asset risk management need to be quantified and realised.

A NEW PERSPECTIVE FOR MUNICIPAL REAL ESTATE FINANCIAL MANAGEMENT

The amendments to the Municipal Property Rates Act are effective from 1st July 2015. Municipalities must react by altering the prism through which they view their revenue strategies. Speak to MetGovis about how we can manage your risk and maximise your municipal revenue potential. Our team of committed and experienced professionals have been working with municipalities, valuers and property professionals since 1994. We develop and implement comprehensive and integrated property solutions.

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25297 GD 03/2015