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INVENTORY MANAGEMENT POLICY

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INDEX

| | | |
|-----|--|----|
| 1. | DEFINITIONS AND ACRONYMS..... | 4 |
| 2. | POLICY STATEMENT..... | 5 |
| 3. | PREAMBLE..... | 5 |
| 4. | PURPOSE..... | 6 |
| 5. | OBJECTIVES..... | 6 |
| 6. | SCOPE..... | 7 |
| 7. | THE INVENTORY MANAGEMENT LIFE-CYCLE..... | 7 |
| 8. | GENERAL RULES APPLYING TO THE AREAS OF STOCKHOLDING..... | 8 |
| 9. | INVENTORY PROCEDURES | 9 |
| 10. | APPOINTMENT OF RESPONSIBLE OFFICIALS | 10 |
| 11. | ORDERING OF INVENTORY | 10 |
| 12. | RECEIPT OF INVENTORY | 10 |
| 13. | STORAGE OF INVENTORY | 10 |
| 14. | ISSUE OF INVENTORY | 12 |
| 15. | OBSOLETE INVENTORY | 12 |
| 16. | INVENTORY COUNT..... | 13 |
| 17. | INVENTORY RECORDS..... | 13 |
| 18. | REPORTING..... | 14 |
| 19. | CLASSIFICATION OF INVENTORY | 15 |
| 20. | STOCK LEVELS | 15 |
| 21. | REVIEW OF STOCK LEVELS..... | 15 |
| 23. | SAFEGUARDING OF INVENTORY | 16 |
| 24. | RECOGNITION..... | 16 |
| 26. | LEGISLATIVE AND REGULATORY FRAMEWORK | 17 |
| 27. | STAKEHOLDER ENGAGEMENT..... | 17 |
| 28. | IMPLEMENTATION: ROLES AND RESPONSIBILITIES..... | 18 |
| 29. | MONITORING AND EVALUATION | 18 |
| 30. | CONCLUSION | 18 |
| 31. | EFFECTIVE AND REVISED DATE | 18 |
| 32. | ANNEXURES..... | 19 |

1. DEFINITIONS AND ACRONYMS

1.1 Statutory and Regulatory

This Procedure applies to the following meanings and interpretations:

| # | TERM | DESCRIPTION |
|------|----------------------|---|
| 1.1 | Accounting Officer | means the Municipal Manager for the Municipality as contemplated in section 60 of the Local Government: Municipal Finance Management Act, 56 of 2003. |
| 1.2 | CFO | means the Chief Financial Officer designated in terms of section 80(2) (a) of the Local Government: Municipal Finance Management Act, 56 of 2003 |
| 1.3 | Cost | shall comprise costs of purchase, costs conversion and other costs incurred in bringing the inventories to their present location and condition. |
| 1.4 | Delegated authority | means the official who is given the authority for relevant functions in terms of the municipality's written delegations. |
| 1.5 | Good received note | means a document which is used to acknowledge the receipt of goods in good condition and correct quantities. |
| 1.6 | Inventories | are assets: In the form of material or supplies to be consumed in the production process, In the form of materials or supplies to be consumed or distributed in the rendering of services Held for sale or distribution in the ordinary course of operations, or In the process of production for sale or distribution |
| 1.8 | Municipality | shall mean the Thulamela Municipality. |
| 1.9 | Net Realisable | Is the estimated selling price in the ordinary course of operations less the estimated costs of completion and estimated costs necessary to make the sale exchange or distribution. |
| 1.10 | Obsolete inventory | Means items, goods or materials that are no longer needed, usable or saleable due to various reasons such as items that have expired, are redundant or damaged. |
| 1.11 | Re-order level | means the level of inventory at which inventory is re-ordered. |
| 1.12 | Requisition form | means a written request to supply specified inventory. |
| 1.13 | Store | means a place where inventory is stored and reserved for future use, or a source from which supplies may be drawn. |
| 1.14 | Inventory controller | means an official responsible for the requisition, receipt, issue, recording, safeguarding of inventory and cost-effective and efficient management of inventory. |

2. POLICY STATEMENT

The accounting officer of a municipality who is the Municipal Manager in this instance, must take all reasonable steps, in terms of section 65(2) of the Municipal Finance Management Act (Act 56 of 2003), to ensure that:

- 2.1 The municipality has and maintains an effective system of expenditure control, including procedures for the approval, authorization, withdrawal and payment of funds.
- 2.2 The municipality has and maintains a management, accounting and information system which —
 - 2.2.1 recognizes expenditure when it is incurred.
 - 2.2.2 accounts for creditors of the municipality; and
 - 2.2.3 accounts for payments made by the municipality.
- 2.3 The municipality's available working capital is managed effectively and economically in terms of the prescribed cash management and investment framework.
- 2.4 The municipality's policy is implemented in a way that is fair, equitable, transparent, competitive and cost-effective.

3. PREAMBLE

- 3.1 Any institution involved in the production of goods or delivery of services may require certain materials, supplies or finished goods in order to carry out its function. In certain cases, these items may be ordered as and when is needed and be applied immediately to their purpose. In other cases, these items may need to be held for a period of time in a warehouse/storeroom or on the job site.
- 3.2 Like any asset, inventory needs to be efficiently managed and decisions need to be made whether inventory should be held, and how much to hold.
- 3.3 The Inventory Management Framework, issued by National Treasury in 2009, articulates the importance of inventory management as follows:

- 3.3.1 Public Sector institutions should manage inventory in such a way that they are able to maximize a return on their investment in order to deliver more services or a higher level of service to the communities they serve. Thulamela municipality as an organ of state uses public funds to acquire goods or materials.
- 3.4 Therefore, the importance of inventory management in the public sector is therefore based on the need to:
- 3.4.1 Demonstrate accountability for public resources;
- 3.4.2 Improve transparency and credibility of information used for making policy choices; and Improve efficiency.
- 3.5 Therefore, improving inventory management can lead to increase in investment revenue or freeing up of resources to be used elsewhere due to a reduction in stock held in inventory and a reduction in losses due to theft, wastage, damage, spoilage or misuse.
- 3.6 Like many other government institutions, Thulamela municipality operates in an environment characterized by limited resources. It is natural for managers to forgo inventory management efforts in lieu of more pressing needs. However, any institution irrespective of the size of its inventory, will gain from inventory management which can mean lower purchasing and inventory holding costs, better quality of products while a reduction in losses or otherwise freeing up resources to be utilized in other areas may lead to increasing the rate of delivery of basic services.

4. PURPOSE

- 4.1 The purpose of this policy is to provide a framework for transparent and responsible management of municipal inventory by ensuring that inventory levels are adequate to meet municipal needs while minimizing excess stock and improving service delivery.

5. OBJECTIVES

The policy aims to achieve the following objectives which are to:

- 5.1 Provide guidelines that employees of the Municipality must follow in the management and control of inventory, including safeguarding and disposal of inventory.

- 5.2 Procure inventory in line with the established procurement principles contained in the Municipality's Supply Chain Management Policy.
- 5.3 Eliminate any potential misuse of inventory and possible theft.
- 5.4 Implement appropriate internal controls and effective inventory management system to ensure that goods placed in stores are secured and only used for the intended purposes.
- 5.5 Determining and setting of inventory levels that includes minimum and maximum stock levels and lead times whenever goods are placed in stock.
- 5.6 Monitoring and review of service provider's performance to ensure compliance with specifications and contract conditions.

6. SCOPE

- 6.1 This policy applies to Thulamela Municipality's inventory received by the Inventory Controller and issued to users.
- 6.2 This policy specifically excludes:
 - 6.2.1 Pharmaceutical inventory, livestock and face value forms; and
 - 6.2.2 Equipment and other assets not defined as inventory.

7. THE INVENTORY MANAGEMENT LIFE-CYCLE

- 7.1 Inventory management is the process of efficiently and effectively overseeing and managing the constant flow of inventory units to prevent inventory from becoming too high, or dwindling to levels that could put the operations of the municipality at risk.
- 7.2 Assets and Inventory section assists Departments to ensure that the operational requirement of the Municipality is broken down into its lowest level of units required. Various inputs are required to fulfill this function for example defining stock holding, bill of materials and procurement and production lead times. These inputs are defined and quantified using various inventory management strategies and techniques.
- 7.3 The process of inventory classification results in items being classified as assets or inventory after evaluating it against asset and inventory classification criteria. The quantification of cost forms part of periodic financial maintenance which includes the

initial measurement of costs. Recognition and measurement ensure that all the costs associated with the inventory item is identified and recognized in the accounting records of the municipality.

- 7.4 As the life cycle of an inventory item continues, various actions could be required for example, reconciliations, disposals or write off. The movement of inventory as they go through the various stages of the operation is critical. Tracking materials as they are used to execute a service also helps to identify the need to adjust reordering quantities before inventory approaches minimum order quantities.
- 7.5 As with every valuable asset, item control needs to be in place to ensure that the item is physically safeguarded against theft and against physical deterioration. Therefore, strict physical control and store management policies need to be in place. Store management also includes the efficient management of a store to maximize efficiency and minimize cost.
- 7.6 As all processes are subject to review and improvement, Inventory management needs to be monitored through regular review. Performance measurement assesses the effectiveness of inventory management processes and identifies improvement areas.

8. GENERAL RULES APPLYING TO THE AREAS OF STOCKHOLDING

- 8.1 No unauthorized person shall obtain entry to the premises, buildings, rooms or areas where goods are kept, unless accompanied by an authorized stores official.
- 8.2 The delegated stores official must keep a set of keys for all cabinets, cupboards, padlocks and other storage places, separately in a secure place.
- 8.3 Inventory items must be stored in appropriate facilities in accordance with the manufacturer's specifications/ legal requirements and municipal by laws.
- 8.4 Inventory items must be grouped in terms of the level of physical protection required e.g. hazardous or perishable;
- 8.5 Breakable items must be stored in such a manner that breakages are limited to the absolute minimum;

- 8.6 Fire extinguishing equipment must be available in all stores. Such apparatus shall be serviced regularly by reputable service providers and the date of service indicated thereon.
- 8.7 Shelf utilization must be effective and shelves must not be overloaded, whilst injudicious high stacking exceeding the fire and safety regulations, is forbidden;
- 8.8 Continuous attention must be paid to the possible presence of rodents and insects, which can damage inventory and storage facilities. Storerooms must be rodent-proof;

BINNING

- 8.9 Only duly appointed stores official will determine/ authorize changes of the binning location;
- 8.10 All materials must be stored within a recognized bin within the storeroom, and this must be reflected on the corresponding system whether manual or electronic.
- 8.11 The delegated store official completing the binning procedure must bin the material correctly, in the indicated bin location, as per the binning transfer order or Goods Receipt Slip presented per material;
- 8.12 Bin locations which are found to be full, or have a different material located therein, must be brought to the attention of the store official who must suggest an alternative bin location;
- 8.13 Under no circumstances will an alternate bin location for the material be allocated unless otherwise instructed by the system or delegated store official authorized to do so; and
- 8.14 For any binning exceptions that occur, corrections must be authorized by the delegated store official.

9. INVENTORY PROCEDURES

The procedures for inventory must be followed to ensure that:

- 9.1 Inventory is safeguarded at all times;
- 9.2 There are accurate records of quantities on hand at all times;

- 9.3 Optimum inventory levels are maintained to meet the needs of users;
- 9.4 Only authorized issues of inventory are made to users; and
- 9.5 Items placed in store are secured and only used for the purpose for which they were purchased for.

10. APPOINTMENT OF RESPONSIBLE OFFICIALS

- 10.1 The CFO must appoint, in writing, officials to perform the duties of an Inventory Controller in terms of this Policy.
- 10.2 Adequate segregation of duties between the requisition, receipt, recording, storage and safekeeping of inventory and the management and control thereof must be maintained to avoid the potential occurrence of errors and fraud.

11. ORDERING OF INVENTORY

- 11.1 Standard Supply Chain Management procedures as per the approved Supply Chain Management policy are to be implemented.

12. RECEIPT OF INVENTORY

- 12.1 All inventory must be received by the completion of a goods received note and processed on the financial management system.

13. STORAGE OF INVENTORY

- 13.1 Inventory must be stored in a secured, exclusive use area, under lock and key.
- 13.2 The area must be used exclusively for the storage of inventory, with limited authorized access only.
- 13.3 Inventory must be positioned to facilitate efficient handling and checking.
- 13.4 All items must be stored separately, with proper segregation.
- 13.5 Inventory must be clearly labelled for easy identification. Inventory tag/bin cards or inventory labels may be used to identify each item and to aid in the physical verification of the items.

- 13.6 Where practically possible, all items of the same type and reference must be stored together as per the description on the inventory records.
- 13.7 Items with limited shelf life must be rotated on a first in first out basis, in accordance with paragraph .35 of GRAP, to reduce the occurrence of expired or obsolete stocks.
- 13.8 Due diligence and care must be exercised to prevent damage of, or deterioration of inventory.
- 13.9 Due regard must be given to any safety standards which may apply to the storage of certain inventories.
- 13.10 Steps must be taken to ensure safe custody of items, including precautions against loss or theft.
- 13.11 The Inventory Controller or Delegated Official responsible for the custody and care of inventory must ensure that in his/her absence such items, where applicable, are securely stored.
- 13.12 The responsibility for the custody of the storeroom keys must be allocated by the delegated authority to an official who is accountable for its use.
- 13.13 No unauthorized persons/officials shall obtain entry to premises, buildings or containers where inventory is kept, unless accompanied by the responsible official.
- 13.14 Whenever a change in the Inventory Controller occurs, an inventory count must be conducted.
- 13.15 An independent official shall be nominated in writing by the delegated authority to assist the official handing and taking over with the checking of the inventory and any discrepancies.
- 13.16 Should the above not be complied with, the official taking over shall be liable for any discrepancies.

The following fire protection precautions must be adhered to:

- 13.17 Inventories of an inflammable or dangerous nature shall be stored and handled in such a manner that persons or property are not endangered and in compliance with the requirements of any local authority;

13.18 The area must be clearly signposted; and

13.19 Fire extinguishing equipment must be placed in the area where inventories are held and must be serviced regularly.

14. ISSUE OF INVENTORY

14.1 Only the Inventory Controller is authorized to issue inventory from the storeroom.

14.2 Inventory must only be issued in terms of the approved requisition form of the Municipality.

14.3 All requisition forms must be ruled off immediately below the last item to prevent items being added once the requisition is authorized by the responsible manager

14.4 The official receiving the inventory must acknowledge the receipt of stock items requested, by signing the Stock Issue Register prepared by the Inventory Controller.

14.5 Inventories must be issued and used for official purposes only.

15. OBSOLETE INVENTORY

15.1 The preparatory work for the disposal of obsolete inventory must be undertaken by the Inventory Controller and verified by the Assets Manager or Assets Accountant.

15.2 The delegated authority may approve the write-off of inventory, if satisfied that:

15.2.1 The inventory has expired and is redundant;

15.2.2 The inventory is of a specialized nature and has become outdated due to the introduction of upgraded and more effective products;

15.2.3 The inventory cannot be used for the purpose for which it was originally intended; or

15.2.4 The inventory has been damaged and is rendered useless.

15.3 All disposed of items must be updated in the inventory records/register/database for the purposes of proper management and control.

15.4 Damaged goods which are noticed during the stock take should be recorded on the count sheet and be reported accordingly.

16. INVENTORY COUNT

- 16.1 Items may be subject to an inventory count Biannual (twice a year).
- 16.2 Where the quantity of inventory is too large for the count to be completed on a single occasion, inventory counts may be carried out on a rotational basis with a full inventory count at the end of each financial year.
- 16.3 All approved Municipal procedures and processes must be complied with during the inventory count.
- 16.4 The Inventory Controller must submit a report to the CFO after investigating any discrepancies between the inventory records/register/database, bin/tag cards or inventory labels and the physical inventory.
- 16.5 The CFO must submit a report with the findings to the Accounting Officer, in order to have the matter reported to the Council of the Municipality for the write-off of any inventory losses, or the write –up of surpluses.
- 16.6 The inventory record, register, database or system must be updated accordingly.

17. INVENTORY RECORDS

- 17.1 All relevant information must be included for the proper management and control of all inventory items. It is recommended that details include but are not limited to:
 - 17.3.1 Bin code/number
 - 17.3.2 Item description;
 - 17.3.3 Quantity and value of stock on hand;
 - 17.3.4 Quantity and value of stock received;
 - 17.3.5 Quantity and value of stock issued;
 - 17.3.6 Re-order level;
 - 17.3.7 Optimum inventory level;
 - 17.3.8 Quantity and value of obsolete stock; and

17.3.9 Opening/closing balance.

17.3.10 An inventory register/valuation must be printed monthly and the hard copy filed in order to maintain a proper audit trail.

18 REPORTING

18.1 Manager: Assets and Stores or delegated official should provide a report, which must include information relating to:

18.1.1 Total value of monthly issues

18.1.2 Total value of stock on hand

18.1.3 Outstanding deliveries.

18.2 A report must be submitted at least Biannual (twice a year) to the Chief Financial Officer and/or the Assets Manager detailing the following:

18.2.1 Any inventory shortages or surpluses and the reasons for such;

18.2.2 Any inventory deficits proposed to be written-off; and

18.2.3 Any obsolete inventory items.

18.3 Inventories purchased during the financial year must be disclosed at cost or net realizable value in the disclosure notes of the Financial Statements of the Municipality.

18.4 In terms of GRAP the financial statements shall disclose:

18.4.1 the accounting policies adopted in measuring inventories, including the cost formula used,

18.4.2 the total carrying amount of inventories and the carrying amount in classifications appropriate to the entity,

18.4.3 the carrying amount of inventories carried at fair value less costs to sell,

18.4.4 the amount of inventories recognized as an expense during the period,

18.4.5 the amount of any write-down of inventories recognized as an expense in the period in accordance with paragraph .43,

18.4.6 the amount of any reversal of any write-down that is recognized as a reduction in the amount of inventories recognized as an expense in the period in accordance with paragraph .43,

18.4.7 the circumstances or events that led to the reversal of a write-down of inventories in accordance with paragraph .43, and

18.4.8 the carrying amount of inventories pledged as security for liabilities.

19. **CLASSIFICATION OF INVENTORY**

Inventory shall be classified as follows:

| INVENTORY CATEGORIES | CONSUMABLE CATEGORIES |
|----------------------|---|
| Unsold Properties | Land Inventory |
| Materials & Supplies | Electrical, Cleaning Material, Buildings material, Spare Parts. |
| Supplies | Stationary |

20. **STOCK LEVELS**

The following should be determined to maintain optimum stock levels and set the following:

20.1 Slow moving or obsolete stock

20.2 Re-order Level

20.3 Maximum Level

20.4 Minimum Level

21. **REVIEW OF STOCK LEVELS**

21.1 To manage the stores operations effectively, the end user department should continually review their stock holding based on the information such as number of stock issues, levels of service achieved, total value of stock held and stock turnover.

21.2 Once yearly, the stock level reviews are conducted with the end user department to maintain accurate minimum, maximum, and re-order levels and to always ensure the availability of stock/materials for the end-users to reach their set goals or targets.

21.3 Redundant and obsolete stock should be identified and cleared regularly by the end user department.

23. SAFEGUARDING OF INVENTORY

23.1 Inventory shall at all times be safeguarded and kept in a secured area.

23.2 Only authorized officials will have access to stores and no person other than inventory or logistics personnel or any person designated by the Chief Financial Officer, may have control over the administration of inventory.

23.3 All theft on inventory items shall be reported to the South African Police Services.

24. RECOGNITION

25.1 MEASUREMENT AT RECOGNITION

25.1.1 Inventories that qualify for recognition as assets shall initially be measured at cost.

25.1.2 Where inventories are acquired at no cost, or for nominal consideration, their costs shall be their fair value as at the date of acquisition.

25.2 MEASUREMENT AFTER RECOGNITION

25.2.1 Inventories shall be measured at the lower of cost and net realization value, except where paragraph .18 of GRAP 12 applies.

25.2.2 Inventories shall be measures at the lower of cost and current replacement cost where they are held for:

25.2.2.1 distribution at no charge or for a nominal charge, or

25.2.2.2 consumption in the production process of goods to be distributed at no charge or for a nominal charge.

25.3 RECOGNITION AS AN EXPENSE

25.3.1 When inventories are sold, exchanged or distributed, the carrying amount of those inventories shall be recognized as an expense in the period in which the related revenue is recognized. If there is no related revenue, the expense is

recognized when the goods are distributed, or related service is rendered. The amount of any write-down of inventories to net realizable value and all losses of inventories shall be recognized as an expense in the period the write-down or loss occurs. The amount of any reversal of any write –down of inventories arising from an increase in net realizable value, shall be recognized as a reduction in the amount of inventories recognized as an expense in the period in which the reversal occurs.

25.3.2 Some inventories may be allocated to other assets accounts, for example, inventory used as a component of self-constructed property, plant or equipment. Inventories allocated to other assets in this way are recognized as an expense during the useful life of that asset.

26. LEGISLATIVE AND REGULATORY FRAMEWORK

In terms of the MFMA, the Accounting Officer for a municipality must:

26.1 Be responsible for the effective, efficient, economical and transparent use of the resources of the municipality as per section 62 (1)(a);

26.2 Take all reasonable steps to prevent unauthorized, irregular and fruitless and wasteful expenditure and other losses as per section 62(1)(d);

26.3 Be responsible for the management, including the safeguarding and the maintenance of the assets, and for the management of the liabilities, of the municipality as per section 63(1)(a) and (b).

26.4 In terms of GRAP 12:

26.4.1 Inventories shall be recognized as an asset if, and only if,

26.4.2 it is probable that future economic benefits or service potential associated with the item will flow to the entity, and

26.4.3 the cost of the inventories can be measured reliably.

27. STAKEHOLDER ENGAGEMENT

27.1 All the relevant stakeholders, internal and external, will be consulted through the development and implementation of this policy.

28. IMPLEMENTATION: ROLES AND RESPONSIBILITIES

28.1 All the respective departments within the municipality must ensure adequate implementation of this policy. The CFO is responsible for enforcing this policy and continuously ensuring monitoring and compliance and ensure that the corrective steps are taken where necessary.

28.2 INVENTORY CONTROLLER - responsible for the requisition, receipt, issue, recording, safeguarding of inventory and cost-effective and efficient management of inventory.

29. MONITORING AND EVALUATION

29.1 The Chief Financial Officer through the Assets and Inventory manager must monitor the implementation of the policy on a regular basis. Monitoring and evaluation of Inventory focuses on monitoring inventory levels, identifying trends and patterns on areas for improvement where the effectiveness and efficiency in achieving the objectives are analyzed and assessed and adjustment is made in areas that need improvement. This will enable the municipality to adjust over a certain period of time to enhance stakeholder's satisfaction.

30. CONCLUSION

30.1 In conclusion the Inventory Management Policy outlines and addresses critical matters raised in the purpose and the objectives. The provisions in the policy contents highlights the need for the municipality to adhere to the key issues narrated which will address challenges encountered and lead to effective and efficient implementation of the policy.

30.2 Thulamela Local Municipality commits to making resources available, monitoring and evaluate the effectiveness of the policy, thus encouraging all relevant stakeholders to familiarise themselves with the policy.

31. EFFECTIVE AND REVISED DATE

31.1 This policy shall be effective once approved by the council and shall be reviewed on an annual basis or amended from time to time as and when the need arises to ensure that it is in line with the municipality's strategic objectives and with legislation.

32. ANNEXURES

32.1 Business Process Map

32.2 Standard Operating Procedure