



# PARTICIPANTS

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Section 11

Finance for Upgrading



# MODULE 11: FINANCE FOR UPGRADING

## Module purpose

The purpose of this module is to enable you to understand the approaches and instruments available for financing an informal settlement upgrading project or programme so that you can contribute to developing financial plans.

## Learning outcomes

After participating in the module you should be able to:

- Identify what needs to be funded as part of an upgrading project;
- Explain the Division of Revenues Act and how the money is distributed amongst grants and subsidies;
- Identify the different financial instruments that can be applied to upgrading projects;
- Determine which types of finance are appropriate and relevant for different types (categories) of upgrading projects;
- Read and understand a project budget.

## Module duration

6.5 hours

## Resources that will be used in the module

- Participant manual
- Grant Instruments for Informal Settlement Upgrading
- Example: Summary of Informal Settlement Upgrading (ISU) Strategy
- Table: Funding Requirements for Different Settlement Types.

# Table of Contents

<b>1. Funding requirements for an upgrading project</b>	<b>3</b>
1.1 Affordability issues	3
1.2 Main funding requirements	3
<b>2. Types of funding available</b>	<b>6</b>
2.1 Main types of funding	6
2.2 Source of the funding: the Division of Revenues Act (DORA)	6
2.3 Factors affecting what funding is actually required or available	7
2.4 Grants available for informal settlement upgrading	8
2.5 Funding limitations and gaps	15
2.6 Applying the grant instruments	16
<b>3. Preparing a financial plan for an upgrading project</b>	<b>18</b>
3.1 Principles for financial planning for an upgrading project	18
3.2 Making sufficient provision in an upgrading financial plan	20
3.3 Budgeting using the UISP	21
3.4 Project cash flow	24
<b>4. Preparing a financial plan for an upgrading programme</b>	<b>27</b>
4.1 Principles	27
4.2 Budgeting via MTEF	27

# 1. Funding requirements for an upgrading project

## 1.1 Affordability issues

Funding is a critical success factor for any project. Without the necessary funding a project cannot be implemented. **Sources of funding must therefore be identified right at the start of any upgrading project** (ie at the concept and early planning stages). The requirements and application processes of the targeted funder/s must be clearly understood and the likelihood of securing the funding assessed.

**When the target market has very low incomes then the funding strategy will be mainly to access subsidies and grants to cover the full cost of the project**, including acquiring the land, servicing it and supporting dwelling improvements. Most informal settlement residents have very low incomes and are not able to service home loans or other types of additional finance. Residents also typically have limited ability to pay for ongoing rates and municipal services such as water and electricity.

**Incrementally improving infrastructure and services and creating more secure tenure can make upgrading more affordable to residents and to the municipality.** Even if residents aren't able to access a full housing subsidy in the short-term, they have a more secure platform from which to access municipal services and livelihood opportunities. These provide the opportunity to make further incremental housing investments.

## 1.2 Main funding requirements

***ACTIVITY 11.1: KNOW WHAT YOU KNOW — FUNDING REQUIREMENTS***

***Activity type: Individual***

***Timing: 5 minutes***

***Purpose: To think about the funding requirements for upgrading activities.***

***Instruction: In the space below, list as many items as you can think of that must be paid for in upgrading projects.***

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**A wide range of activities need to be funded as part of an upgrading project.** These will differ depending on the type of informal settlement. The Handout Grant Instruments for Upgrading lists the grant instruments available for informal settlement upgrading. The table below sets out the different funding requirements that would apply to different types of informal settlements.

Funding requirements	Informal Settlement Type						
	Conventional Formal Full Upgrading (A)	Incremental Full Upgrading (B1 extended)	Interim Arrangements (B1)	Deferred Relocation with Interim Arrangements (B2)	Immediate relocation (C)	Greenfield project	TRA
<b>CAPITAL:</b>							
Bulk services (eg water treatment, main roads, etc)	Y	Y	Y	Y/N	N	Y	Y/N
Temp on-site eng services (water, sanitation, roads)	N	Y*	Y*	Y	Y	N	Y
Perm on-site eng services (eg water, sanitation, roads)	Y	Y*	Y*	N	Y/N	Y	Y/N
Land purchase	Y	Y	Y/N	N	N	Y	Y
Temporary or emergency house construction	N	Y/N**	Y/N**	Y/N**	N	N	Y
Owner-driven housing consolidation/improvements	N	Y/N	Y	Y/N	N	Y/N	N
Formal housing construction	Y	Y/N	N	N	N	Y	N
Key social facilities such as schools, clinics, etc	Y	Y	Y	Y	Y/N	Y	Y
<b>TECHNICAL STUDIES/PROFESSIONAL FEES</b>							
Community participation and participative planning	Y	Y	Y	Y	Y	Y	Y
Engineering design (temp or permanent)	Y	Y	Y	Y	N	Y	Y
Pre-feasibility studies eg site suitability	Y	Y	Y	N	N	Y	Y
Topographic survey	Y	Y	Y/N	N	N	Y	Y
EIA	Y	Y	Y/N	N	N	Y	Y/N
Preliminary town planning – block layout	Y	Y	Y	Y/N	N	N	Y
Full town planning	Y	Y#	N##	N	N	Y	N
Township establishment	Y	Y/N#	N##	N	N	Y	N
<b>ONGOING SERVICES, OPERATING and MAINTENANCE</b>							
Solid waste collection	Y	Y	Y	Y	Y/N~	Y	Y
Fire protection	Y	Y	Y	Y	Y/N~	Y	Y
Maintenance of services	Y	Y	Y	Y	N	Y	Y
Support for livelihoods and informal economy	Y	Y	Y	Y	Y	Y	Y
Sustained community engagement and participation	Y	Y	Y	Y	Y	Y	Y

\*Many municipalities prefer to install permanent services right from Phase 1

\*\*Whilst it is not common for emergency housing to be provided along with interim or emergency services, this does sometimes occur where there are very unsafe informal structures

#In the case of a less-formal full upgrade, the type and extent of town planning work will vary and full township establishment may not automatically follow

##Whilst full town planning and township establishment do not occur in the interim services phase, they are eventually achieved when full upgrading later occurs

~Solid waste removal and fire protection would not be required for long because relocation is imminent. If however there are delays then they should be addressed and the settlement should be reclassified as deferred relocation with interim arrangements

## 2. Types of funding available

### 2.1 Main types of funding

The following are the main types of funding which are relevant to an upgrading project:

- **Conditional grant/subsidy finance** such as:
  - Human Settlement Development Grants (SG): eg UISP, Provision of Social and Economic Amenities, Emergency Housing Programme (EH);
  - Urban Settlement Development Grant (USDG);
  - Municipal Infrastructure Grant (MIG).
- **Municipalities' own financial resources:** This is funding from the municipality's capital or operation budget and is used for example to top-up for costs of engineering services or to cover ongoing operating and maintenance costs not covered by rates and service fees. This funding is from the municipality's equitable share (see below) and funds raised from rates and services provision.
- **Residents own money:** This includes residents' own investments in the top-structure, payment for rates and services, etc.

Given the low levels of household affordability within informal settlements and the financial position of most municipalities (which have a limited income base and limited financial reserves), the use of grants is by far the most important source of funding for upgrading projects. This funding is required in respect of project development costs. Funds for the operating and maintenance phases must be sourced elsewhere.

### 2.2 Source of the funding: the Division of Revenues Act (DoRA)

The South African government raises funds through taxes and income earned, as well as borrowing. All funds raised are kept in a National Revenue Fund. Money may be withdrawn from the National Revenue Fund only in terms of an act of parliament or as a direct charge against the National Revenue Fund, when it is provided for in the Constitution or an act of parliament.

The funds raised by government are allocated to the national, provincial and local spheres of government in terms of the Division of Revenue Act (DoRA). Section 214 of the Constitution requires that the DoRA shares these funds on an equitable basis so as to support the principles of co-operative government and strengthen inter-governmental relations.

The Minister of Finance motivates and tables the national budget in parliament. The Division of Revenue Bill (for a particular year) is tabled and passed as the DoRA for that fiscal year (ie March of the current year to February of the following year). In addition to the equitable distribution of revenue, the DoRA also provides for other allocations to provinces and municipalities through conditional grants.

The allocation to municipalities is detailed after the promulgation of the DoRA by National Treasury in the Government Gazette: The Transfers to Local Government. This includes

frameworks for local government grants to public or municipal entities, frameworks for municipal infrastructure and capacity building grants, and the detail of all grants to be made to specific municipalities.

All budget schedules in the DoRA depict the financial allocation for any current year. These allocations are what the municipality can expect to receive or access. The recommended division of anticipated revenue for the subsequent two years is also included. This is what is referred to as the Medium-Term Expenditure Framework (MTEF). The MTEF provides for greater financial predictability and certainty which makes it possible for municipalities to plan into the future.

The different types of funding allocations made in the DoRA are as follows:

- **The equitable share for local and provincial governments:** The primary objective of the equitable share is to ensure that all South Africans have access to basic services. This is an unconditional transfer ie local government can decide how they want to use it. The equitable share is allocated on the basis of a formula.
- **Conditional grants:** The South African system of conditional grants generally contains three types of grants: supplementary, specific purposes and in-kind-allocations. The funds must be used for the purpose for which they were allocated.

## 2.3 Factors affecting what funding is actually required or available

The funding requirements for upgrading projects will vary significantly from one project to another depending mainly on the following key factors:

- **Settlement type:** The type of settlement will affect the funding required and the funding potentially available. For example a deferred relocation with interim arrangements (B2) settlement does not require land acquisition to be funded and may make use of grants other than Human Settlement subsidies, such as USDG or MIG. Conventional formal full upgrading and incremental full upgrading settlements will use Human Settlement subsidies and will need land to be acquired (either up-front or at an appropriate time during the upgrading process).
- **Municipal eligibility:** This will determine the type of funding that is available. For example only Metros can access USDG.
- **Beneficiary eligibility:** This will also determine the type of funding that is available because non-SA citizens will not qualify for top-structure housing subsidies.
- **Municipal accreditation status and level:** A municipality's accreditation level can impact on subsidy funding. This is especially true if level 3 is obtained where funding flows directly to the municipality, or even at level 2 where greater programme management control is delegated. As at August 2014, for a range of reasons however, none of the six Metros who have applied for level 3 accreditation have qualified.



- **Settlement specific characteristics:** Settlement-specific conditions can have a significant impact on the project plan and hence on what funding sources can or should be accessed. For example:
  - If there are complex land legal issues then additional funding might be needed for such purposes;
  - If there is an acute lack of schools or clinics then engagement with the relevant departments must be prioritised in order to secure funding/support from them;
  - If there is a high level of community organisation and savings, then an Enhanced People's Housing Process project might be preferable;
  - If significant portions of a site are unsuitable for formalisation and partial relocations will result, then funding to plan a relocations destination will be required.
- **Extent of in-house municipal capacity:** This will impact on the ability of the municipality to directly undertake work such as facilitation, engineering services design, project management. Sufficient capacity usually does not exist and this means that specialists must be procured, which would have budgetary implications. There are, however, cases where some high capacity municipalities or Metros do have certain capacity in-house.
- **Community participation:** All municipalities, irrespective of their size, must make available some capacity for community participation, even if they are not able to undertake all functions at the project-level. It is essential for municipalities to have some level of direct communication with local communities.

Participation is discussed in Module 4.

## 2.4 Grants available for informal settlement upgrading

There are a range of grant funding instruments available for informal settlement upgrading. The relevance of specific grants will be largely dictated by the category of the settlement arising from assessment and categorisation (AC), as well as the other factors outlined in section 2.3 above. It is recognised that whilst some of the policy and grant instruments necessary for incremental upgrading are already in place, there are also instances where this is not the case. An example is funding for basic services for settlements that are deferred relocation with interim arrangements (Category B2). There are also grant instruments which would benefit from refinement for example Phase 1 of the UISP or where the potential of an existing grant mechanisms is not being adequately utilised, for example Emergency Housing. It is also recognised that, in the case of infrastructure provision, the required grant funding may be provided or co-funded by non-housing sources such as the Urban Settlement Development Grant (USDG) or Municipal Infrastructure Grant (MIG).

The table below provides an overview of the grant funding instruments categorised in terms of:

- Grants which are critical or very relevant;
- Grants which are potentially relevant, but with significant limitations or only on a limited basis.

There are also grants which are unlikely to be relevant in practice, but may apply in very isolated cases. These are not included in the table:

- Social Housing Programme (SHP), provided by the Department of Human Settlements (DHS). This could be used in certain cases for relocations for higher earning informal residents.
- Individual Housing Subsidies – Non-credit Linked. These could apply to individual residents who may previously not have qualified when mass housing consolidation was delivered but now do.

More details on each of the grant funding instruments are provided in the Handout *Grant Instruments for Informal Settlement Upgrading*.

## Grants which are critical for upgrading

Type of grant and source	Relevance for informal settlement type	What can be funded	Benefits or limitations
<p><b>Upgrading of Informal Settlements Programme (UISP) grant</b> (provided by provincial DHS, as well as directly from the national DHS to accredited municipalities)</p>	<ul style="list-style-type: none"> <li>• <b>Conventional formal full upgrading (A)</b></li> <li>• <b>Incremental full upgrading (extended B1)</b></li> <li>• <b>Interim arrangements with basic services (B1)</b> in particular where there will be a continuous upgrading process leading directly into formalisation and land is rapidly available.</li> </ul> <p><i>Note: Less appropriate where upgrading will be less formal or where there will be a gap between basic services and formalisation and where land cannot be rapidly acquired.</i></p>	<ul style="list-style-type: none"> <li>• Interim basic services.</li> <li>• Land acquisition.</li> <li>• Permanent engineering services.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>UISP (like other housing subsidies) is likely to be slow and administratively burdensome.</b></li> <li>• <b>UISP is premised on early land acquisition and incremental formalisation</b> (moving continuously in that direction). Land acquisition is intended in Phase 1 (interim services). DHS is likely to expect that land can be rapidly acquired (eg land agreements in place) even before releasing interim services funding. Land acquisition however is inherently slow, challenging and costly.</li> <li>• The <b>value of funding for interim engineering services is very limited</b> – as per subsidy formula, the R3.6k available in Phase 1 (prior to land acquisition) will often be insufficient.</li> <li>• Many <b>municipalities will prefer to install permanent engineering services at the outset</b>. They will need to access sufficient funding up-front until land is acquired.</li> <li>• <b>UISP represents limited benefits over IRDP</b> especially if interim services are not envisaged or required.</li> <li>• <b>Value of engineering services for UISP is pegged well below that of greenfield IRDP developments.</b></li> </ul>

<p><b>Urban Settlements Development Grant (USDG)</b> <i>(provided by Treasury to certain accredited or high capacity municipalities)</i></p>	<ul style="list-style-type: none"> <li>• <b>Basic services (mainly interim arrangements (B1), deferred relocation with interim arrangements (B2) and potentially also incremental full upgrading (B1 extended).</b> Currently only for Metros.</li> <li>• Especially useful where land is not readily available and where there will be a hiatus before full upgrading can occur and/or where programmatic delivery across multiple settlements is necessary.</li> </ul>	<ul style="list-style-type: none"> <li>• Principally for basic services (eg water supply, roads, sanitation, etc).</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Currently only available to Metros.</b> Receives a high MTEF budget allocation.</li> <li>• <b>Does not require rapid land acquisition and rapid movement towards formalisation.</b></li> <li>• <b>Far more streamlined application and project delivery process</b> (compared to UISP/IRDP) and can also be readily applied programmatically across multiple project (separate application for each project not required).</li> </ul>
<p><b>Municipal Infrastructure Grant (MIG)</b> <i>(provided by COGTA)</i></p>	<ul style="list-style-type: none"> <li>• <b>Basic services mainly interim arrangements (B1), deferred relocation with interim arrangements (B2) and potentially also incremental full upgrading (B1 extended).</b> Especially for non-Metro municipalities who can't access USDG and where land is not readily available or there is likely to be a hiatus before full upgrading and housing delivery can occur.</li> </ul>	<ul style="list-style-type: none"> <li>• Principally for basic services (eg water supply, roads, sanitation, etc).</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Accessible to and relevant for small municipalities</b> and in particular for peri-urban settlements (in the absence of another suitable, quick grant instrument) and/or where basic services need to be rapidly delivered.</li> <li>• <b>Does not require rapid land acquisition and rapid movement towards formalisation.</b></li> <li>• <b>Far more streamlined application and project delivery process</b> (compared to UISP/IRDP).</li> </ul>
<p><b>Consolidation subsidy</b> <i>(provided by DHS)</i></p>	<ul style="list-style-type: none"> <li>• <b>Conventional formal full upgrading informal settlements for top-structure phase.</b></li> </ul>	<ul style="list-style-type: none"> <li>• Top-structures.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Usual subsidy eligibility criteria apply.</b> Informal settlement residents such as non-residents would not qualify.</li> <li>• <b>Only viable for full formal upgrades</b> – not for alternative less-formal upgrades.</li> </ul>

<p><b>Integrated Residential Development Programme (IRDP) grant</b> <i>(provided by DHS)</i></p>	<ul style="list-style-type: none"> <li>• <b>Conventional formal full upgrading informal settlements for top-structure phase.</b> Note that UISP is preferred to IRDP for full upgrading.</li> <li>• <b>Deferred relocation with interim arrangements (B2)</b> and <b>immediate relocation (C)</b> for the development of a permanent relocation site (greenfield housing development).</li> <li>• <b>Conventional formal full upgrading, incremental full upgrading and interim arrangements informal settlements for partial relocations</b> (as a last resort).</li> </ul>	<ul style="list-style-type: none"> <li>• Engineering services, land acquisition, top-structures, etc.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>The development of a full IRDP greenfield project is a slow process</b>, though typically quicker than an in situ upgrade, it would still usually exceed five years from start of concept and feasibility until final top-structure construction is completed.</li> </ul>
<p><b>Emergency Housing grant</b> <i>(provided by DHS)</i></p>	<ul style="list-style-type: none"> <li>• <b>Interim arrangements (B1)</b> and <b>deferred relocation with interim arrangements (B2)</b> for emergency basic services and top-structures (potentially also for interim arrangements on conventional formal full upgrading (A) and incremental full upgrading (B1 extended)).</li> <li>• <b>Immediate relocation (C)</b> for the establishment of a temporary relocation area (TRA) as a last resort. Potentially also for other categories where a partial relocation is urgent.</li> <li>• <b>Conventional formal full upgrading (A)</b> and <b>incremental full upgrading (B1 extended)</b> for a TRA in cases of a rollover upgrade (temporary relocations) or where there are permanent relocations (eg from road reserves).</li> </ul>	<ul style="list-style-type: none"> <li>• Emergency housing and basic infrastructure.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Essential in the case of providing temporary relocation areas (TRAs)</b> which are transitional relocation facilities. This is the most common utilisation of this grant.</li> <li>• <b>TRAs are problematic</b> and typically become permanent settlements in their own right. They should be regarded as a last resort.</li> <li>• <b>Emergency housing has typically been underutilised</b> for in situ emergency improvements (whether infrastructure or temporary housing).</li> </ul>

<b>Social and Economic Facilities</b> <i>(provided by DHS)</i>	<ul style="list-style-type: none"> <li>Principally for <b>conventional formal full upgrading (A), incremental full upgrading (extended B1) and interim arrangements with basic services (B1)</b>.</li> <li>Also deferred relocation with interim arrangements (B2) (permanent relocations sites developed using IRDP or other programmes).</li> </ul>	Medical care facilities, community halls, parks and playgrounds, sports facilities, taxi ranks and small business facilities.	Only addresses certain types of facilities (eg does not include schools). Accessibility across all provinces is not known.
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## Grants which are potentially relevant

Type of grant and source	Relevance for informal settlement type	What can be funded	Benefits or limitations
New enhanced <b>People's Housing Process grant (EPHP)</b> <i>(provided by DHS)</i>	<ul style="list-style-type: none"> <li><b>Conventional formal full upgrading (A), incremental full upgrading (extended B1)</b> for top-structure phase and associated participative planning and community-driven processes including community planning and possible community savings or other equity.</li> </ul>	<ul style="list-style-type: none"> <li>Top-structures and associated PHP social, planning and capacitation processes.</li> </ul>	<ul style="list-style-type: none"> <li><b>New enhanced policy not yet fully activated</b>, eg EPHP implementation guidelines not yet completed and released (as at Sept 2014).</li> <li><b>EPHP only kicks in for top-structure phase</b> and not during all-important planning stages of projects.</li> <li><b>EPHP premised on formalisation</b> – may not be suitable for less-formal incremental full upgrades (eg where land is not yet acquired, township establishment has not occurred, individual title has not been provided).</li> <li>Some provinces continuing with old contractor-managed PHP in the meantime.</li> </ul>

<p><b>Community Rental Units (CRU)</b> <i>(provided by DHS)</i></p>	<ul style="list-style-type: none"> <li>• <b>Conventional formal full upgrading (A), incremental full upgrading (extended B1-</b> potentially for rental housing solutions on densified upgrades (eg rollover).</li> <li>• <b>Relocations housing provision</b> (mainly for deferred relocation with interim arrangements (B2) and immediate relocation (C) but also potentially others) – for alternative rental housing on relocations sites.</li> </ul>	<ul style="list-style-type: none"> <li>• Housing – typically medium density (eg double storey/attached).</li> </ul>	<ul style="list-style-type: none"> <li>• <b>There are significant difficulties in collecting rentals from poor households who are not receiving a regular income.</b></li> <li>• <b>There are also significant affordability limitations.</b> The costs of operating and maintaining rental housing usually necessitate rentals above the affordability of very poor households.</li> <li>• <b>There are limitations in terms of entities with the requisite capacity and skills</b> to effectively manage rental housing stock for the poor.</li> </ul>
<p><b>Rural Housing</b> <i>(provided by DHS)</i></p>	<ul style="list-style-type: none"> <li>• <b>Conventional formal full upgrading (A), incremental full upgrading (extended B1</b> in cases of peri-urban informal settlements located on traditional land.</li> </ul>	<ul style="list-style-type: none"> <li>• Services, housing and associated professional services.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Most informal settlements are distinct from rural settlements</b> and rural housing subsidies do not apply.</li> <li>• <b>Rural housing is however typically quicker</b> to deliver than urban housing (traditional tenure, no town planning approvals, etc).</li> </ul>

## 2.5 Funding limitations and gaps

It is evident from the preceding sections that there are several key areas where there are funding limitations or funding gaps. These are summarised as follows:

- **Community participation and facilitation:** This needs to be sustained throughout the process of an upgrading project, which is usually over a period of many years, but there is not yet sufficient budgetary provision for it.
- **Basic (interim) engineering services:** The UISP funding provision of R3.6k will often be insufficient for these purposes.
- **Less-formal incremental upgrading:** In general, the existing human settlements grants assume that there will be formalisation. Yet it is evident that less-formal incremental upgrading is regarded as important and will often be necessary since formalisation will often not be possible. Currently the UISP is not well-suited to less-formal upgrading. Until greater UISP flexibility is in place, grants such as the USDG and MIG will need to be utilised.
- **Permanent engineering services:** On many informal settlement sites (eg those that are steep and with high densities), the usual amount allocated for B-grade engineering services will be insufficient, especially where items such as retaining walls and water-borne sanitation are necessary.
- **Project preparation and feasibilities:** Funding for this all-important project phase is not readily available.
- **EPHP:** The new EPHP is not yet fully activated and is limited to the top-structure phase, when it typically needs to start during the project planning phase to be successful. EPHP is about more than top-structures.
- **Land acquisition:** Funding for land acquisition and related professional services is not always sufficiently provided for, or available for, all project categories. For example to acquire high value well-located land for full upgrading or for land for TRAs.



## 2.6 Applying the grant instruments

### **ACTIVITY 11.2: APPLYING THE GRANT INSTRUMENTS**

**Activity type:** Group work

**Timing:** 40 minutes

**Purpose:** To identify suitable funding instruments for different developments.

**Instructions:** Refer to the handout *Grant Instruments for Informal Settlement Upgrading*.

For each of the cases in the table below:

1. Indicate the most suitable funding source or sources.
2. Explain your reasons for selecting the funding source.

Write your answers on the table below.

PROJECT	FUNDING INSTRUMENT/S	REASON
a) Full, formal upgrading project where the site can be developed, where the project is implementation-ready (land is secured), but where some relocations will be required.		
b) Basic services (water supply, sanitation, road access) on a site which is suitable for permanent settlement but which will take some time to formalise. The settlement is well-established and there are no serious health and safety threats.		
c) Provide basic services and emergency shelter improvements on a site identified for relocation. Residents will need to live there for another three years whilst a nearby greenfield housing project is completed.		
d) Conduct pre-feasibility investigations and preliminary planning work to determine site potential for development (geotechnical, land legal issues and environmental issues) to access UISP subsidies. Full incremental upgrading.		
e) Community participation and enumeration/socio-economic survey work for a full incremental upgrading project which has not yet got approved housing subsidies.		
f) Project management capacity/expertise for the entire duration of a full incremental upgrading project to co-ordinate technical studies, contracting, budgeting, subsidy applications and social activities.		
g) Purchase of informally settled land which is suitable for permanent settlement and related land legal work, if there are serious land legal issues to be resolved UISP housing subsidies are not yet secured; provincial DHS has indicated that it will only provide subsidies when the land is available to the municipality.		
h) Provision of additional schools and expansion of existing schools to meet increased residential population.		

## 3. Preparing a financial plan for an upgrading project

In this section we will be looking at financial planning, or budgeting, at the level of the settlement upgrading plan or project.

### 3.1 Principles for financial planning for an upgrading project

#### **ACTIVITY 11.3: WHAT CAN GO WRONG IN FINANCIAL PLANNING?**

**Activity type:** Facilitated group discussion

**Timing:** 15 minutes

**Purpose:** To identify what can go wrong in preparing a financial plan for an upgrading project, and what you can do to avoid or mitigate that.

**Instructions:** You will discuss the question: "What can go wrong with a budget for an informal settlement upgrading plan?"

You can make notes in the space below.

Difficulty	How it can be avoided

### The basis for the financial plan

A financial plan is a critical part of an informal settlement upgrading plan. It is informed by other parts of the upgrading plan especially those relating to the project concept and scope.

The project scope includes all the intended activities that need to

be funded to make the project succeed. The project concept, in turn, is heavily informed by the AC process and in particular the categorisation of the specific settlement.

Project planning was discussed in Module 10.

## Operating and maintenance costs

**Long-term operating and maintenance costs also need to be taken into consideration**, even if these are often not factored into the part of the upgrading plan that is tabled to potential capital funders such as the DHS or MIG. In the long run operating and maintenance costs are the biggest costs and often become a financial problem for municipalities. There must be a clear plan for how operating and maintenance costs will be provided for.

## Financial estimates

**Cost estimates form the basis of all financial plans. The accuracy of such cost estimates increases as the project moves through its various phases.** At the AC and preliminary assessment level, cost estimates are rough in nature and are usually based on typical costs for similar projects. At the stage of submitting a subsidy application or full business plan, there are usually preliminary plans and designs in place which enable much more accurate estimates to be made. However, such estimates are still not fully accurate and are only finalised once a detailed design is completed and the project has been put out to tender and procurement finalised.

## Cash flow

**Cost estimates need to take into account the project schedule (timetable), and the cash flow needs to be calculated accordingly**, in particular so that the Medium-Term Expenditure Frameworks (MTEFs) of municipalities and provincial government can be properly compiled and co-ordinated. The project plan not only needs to reflect **what** funding is required, but also **when** it will be required.

## Inflationary escalations

Often it takes many months to get a human settlements project approved and then often many years for it to be fully implemented. Costs increase over time and these increases need to be factored into the financial plan for the project. If you fail to provide for inflationary escalations the project may run out of budget before it is completed. Another reason why projects run out of funds before completion is that the project budget (financial plan) is not adequately informed by the project schedule (timetable).

## Grant budget limitations and inflexibility

To a **significant extent (and in particular in the case of human settlement grants) the budget available for certain project components is fixed and projects need to be budgeted accordingly**. Although human settlements MECs theoretically have discretion to vary amounts, this will not often occur (except sometimes in the case of special lead projects). Non-human settlements infrastructure-orientated grants (USDG and MIG) usually have greater flexibility. Where the provided amount is insufficient, then alternative funding streams will need to be explored, which will put additional pressures on the municipality. It

is difficult to co-ordinate and synchronise multiple sources of funding for one project. It is much better to be able to make use of only one funding source where possible.

### **Impact of project scale on costs and cost efficiency**

The costs of professional work and related technical studies, eg geotechnical and land legal investigations, and environmental impact assessments are only slightly greater for a project of 1 000 sites compared to project of 500 sites. Yet the project budget available is double because the funding formula provides a set amount per household or per site. So, a 500 site project is much less cost-efficient than a bigger project. Very small projects (eg less than 250 sites) often become difficult to achieve due to these non-economies of scale, unless they are batched together with other projects to achieve better economies of scale. This is one of the difficulties inherent in the human settlements funding formula, which is fixed on a per household basis.

### **Impact of project locality on actual costs**

**The project location also affects costs.** For example:

- Land costs are far higher in Metros and large towns than in small towns and peri-urban areas;
- Construction costs may rise in areas located far from centres of materials supply;
- The costs of construction skills and professional services may rise in areas where such skills are not locally available;
- Costs are higher in very hilly and steep areas or where settlement densities are high.

## **3.2 Making sufficient provision in an upgrading financial plan**

The funding required will vary depending on the type of informal settlement and the type of grant or funding targeted. In all cases there are three categories of funding:

- Capital;
- Professional services; and
- Ongoing operating and maintenance (even if this does not form part of the application for implementation funding).

The following key items are often not adequately identified and provided for in the financial plan for an upgrading project:

- **Facilitation and community participation:** This is a critical success factor in upgrading, but is typically not sufficiently budgeted for which creates significant risk.
- **Bulk services provision:** Often bulk services deficiencies are not adequately detected during the AC and pre-feasibility stages of project planning. The following bulk services issues are commonly neglected:
  - Raw water supply;
  - Water treatment;
  - Sewerage treatment.

- **Land acquisition and related technical work:** Land acquisition is typically a slow, complex and expensive process. The costs include purchasing the land (land costs vary greatly between Metros and small towns), the costs of professional work relating to land legal audits, negotiations with private landowners, facilitating transfers between government departments and even expropriation.
- **Top up costs of internal services:** Often DHS subsidy provision is insufficient to cover the entire cost of internal services, especially in Metros and major cities where water-borne sewerage is necessary or where steep slopes increase engineering costs.
- **Top up for top-structure costs:** In some cases, the DHS subsidy quantum may be insufficient to fully provide for top-structure costs, especially where non-conventional or high density housing types are required to maximise housing yields.

### 3.3 Budgeting using the UISP

A financial plan using the UISP will comprise the phases of the UISP. There are fixed amounts provided in the UISP policy, but actual costs are likely to vary from the amounts provided. In that case additional funding sources (eg municipal reserves) will be required. The table below shows the funding available if we assume a full, but incremental, upgrading using the UISP category incremental full upgrading (B1 extended) with full upgrading to follow thereafter.

The budgetary provision of the UISP up until the interim services stage may be insufficient for many situations, unless some basic interim services have already been provided and most community participation and planning work has already been completed using funds from other sources.

The R3.6 k provided for in the 2014 subsidy formula is unlikely to be sufficient for the construction of interim (temporary) engineering services. The costs for this will vary significantly from one project and site to another. Municipalities may either:

- Opt to provide only a minimal level of service;
- Utilise MIG/USDG funding;
- Motivate to the provincial MEC for special flexibility; or
- Defer the provision of services until the next phase although this will only be effective where land has already been acquired or can be rapidly acquired.

In addition facilitation/participation is not sufficiently provided for and the budget to cover the costs of all professional services on projects smaller than 500 sites is also likely to be insufficient. Even at this scale (500 sites), the fees may not be enough.

**The permanent engineering services budget may also require a top up.** On projects located on challenging sites (eg steep slopes), where densities are very high or where a higher level of service is appropriate (eg water-borne sewerage or A-level service), a significant top up from the municipality may be required (as typically occurs in eThekweni municipality).

**In the event that some bulk services are required** (eg water or sewer connectors), a separate funding source such as MIG or USDG can be accessed for such bulk services. It is possible to use one such funding source for both interim basic services, as well as associated bulk services upgrades.

<b>UISP funding available including housing consolidation phase at 01 April 2014</b>			
	<b>Subsidy per hh</b>	<b>Total 250 sites</b>	<b>Total 500 sites</b>
<b>Phase 1 (temporary services and land acquisition)</b>			
Survey, registration, participation, facilitation, dispute resolution, etc – 3% of project cost	241	60 158	120 316
Geotechnical investigation	114	28 515	57 030
Land acquisition	3 248	811 915	1 623 830
Pre-planning	979	244 660	489 320
Interim engineering services	3 681	920 173	1 840 345
<b>Total Phase 1&gt;</b>	<b>8 262</b>	<b>2 065 420</b>	<b>4 130 841</b>
<b>Phases 2 and 3 (permanent services, detailed planning and design)</b>			
Detailed town planning	513	128 305	256 610
Land surveying and pegging	380	95 043	190 085
Contour survey	76	19 010	38 020
Land survey examination fee	118	29 463	58 925
Civil engineer's fee	1 141	285 125	570 250
Site supervision fees	289	72 225	144 450
Permanent engineering services provision	23 513	5 878 345	11 756 690
Project management – 8% of total cost	2 082	520 601	1 041 202
<b>Total Phases 2 &amp; 3&gt;</b>	<b>28 112</b>	<b>7 028 116</b>	<b>14 056 232</b>
<b>Relocation grants</b>			
Transportations and loading costs for people and household effects	487		
Social service support including support for the registration of social benefits, school registration and other welfare support	368		
Relocation food support to households	606		
<b>Total maximum relocation grant per household&gt;</b>	<b>1 461</b>		

**ACTIVITY 11.4: ESTIMATING A BUDGET USING THE UISP**

**Activity type:** Group work

**Timing:** 40 minutes

**Purpose:** To draw up a budget for a UISP project, using the typical activities in the work package, and the items and amounts available from the UISP.

**Instructions:** Calculate an estimated budget for Settlement A. Complete the table that the facilitator will give you.

*Most of the settlement consists of 723 households. Most of the site has been identified for conventional formal full upgrading, but there is a section that requires immediate relocation. There are 81 households that will need to relocate. They will go to an existing TRA, from where they will relocate to a new development close by.*

1. Refer to the UISP subsidy formula set out in the table above: UISP funding available at 01 April 2014.
2. Calculate how much money is available from the UISP grant for each activity identified in the project plan (refer to the table the facilitator will give you, taken from the Gantt chart you worked with in Module 10).
3. Are there any areas where you think the UISP subsidy may not be sufficient? If so what solutions can you think of? Write your answers in the space below.

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### 3.4 Project cash flow

An upgrading project will run over a number of years. The developer will need funds to pay for work done as and when that work is completed, over the entire timeframe. **A critical part of managing and planning project finances is determining how the funding will be spent over time, ie the projected cash flow.**

To do this, a realistic project schedule (timetable) must be developed that shows how long all the main project activities will take, their interdependence (which ones must be done before others can proceed) and the overall timeframe implications. There is a risk here because there is **a tendency to significantly underestimate how long project activities take**, especially on grant-funded state delivery programmes such as infrastructure and housing.

Refer to the project timetable (Gantt chart) on page 25 below, which sets out the programme for the preparation, planning and implementation of a typical full in situ upgrade project.

On page 26 there is a simplified example of a multi-year project cash-flow for a full, but incremental upgrading using the UISP, such as the one in the Gantt chart. The example of cash flow is based on the UISP subsidy only.

### Simplified Time-table for UISP Incremental Upgrading Project - Gantt format (assuming formal upgrading)

Activity/phase	Duration (mnths)	Year 1				Year 2				Year 3				Year 4				Year 5				Year 6			
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Community engagement & participation	ongoing	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
<b>Initiation:</b>	<b>3</b>	■																							
Assessment, categorisation, response plan	3	■																							
Application / approval UISP ph1	3		■																						
<b>Phase 1 (Feasibility, temp.services, land acq.)</b>	<b>21</b>		■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Procure professional services	3			■																					
Socio-economic survey	3			■																					
Geotechnical investigation	3			■																					
Other site feasibility studies - environmental, topography, bulks services, land legal etc.	3			■																					
Land acquisition	12			■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Preliminary planning	6			■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Design interim services	6			■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Procure for construction interim services	3				■																				
Interim engineering services construction	12				■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Application/approval UISP ph2&3	3									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
<b>Phases 2 and 3 (Full services, design, approvals)</b>	<b>30</b>									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Procure professional services	3									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Topographic survey (contours+key features)	3									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Geotech survey	3									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
EIA (environmental authorisations)	6									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Detailed town planning	6									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Detailed engineering design	6									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Township establishment & planning approvals	6									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
General plan submit & approve	3									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Beacon sites	3									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Procure for construction perm. services	3									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Permanent engineering services provision	12									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
Application / approval UISP/PHP ph4	3									■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	
<b>Phase 4 (Topstructures/tenure)</b>	<b>21</b>																				■	■	■	■	
Procure for housing phase as applicable	3																				■	■	■	■	
Housing delivery/consolidation	12																				■	■	■	■	
Individual title / conveyencing	12																				■	■	■	■	
Closeout	3																				■	■	■	■	

<b>SIMPLIFIED CASHFLOW - FULL FORMAL UPGRADING PROJECT - 500 sites (UISP Human Settlement Grant funding only)</b>								
<b>Ph.</b>	<b>Activity</b>	<b>Yr1</b>	<b>Yr2</b>	<b>Yr3</b>	<b>Yr4</b>	<b>Yr5</b>	<b>Yr6</b>	<b>Yr7</b>
1	Prefeasibility, site suitability, particip., ph1 subs. applic. & approval	333 333						
	Basic/temp. services provision (incl. procurement)		1 840 345					
	Land acquisition		1 623 830					
2&3	Preliminary planning & design, ph2&3 subs applic. & approval		333 333					
	Detailed design & planning approvals (incl. procurement)			733 723				
	Services construction (incl. procurement), ph 4 subs. applic. & approval				6 661 255	6 661 255		
4	Transfers & conveyencing					325 000	325 000	
	Topstructure delivery (incl. procurement)					27 411 638	24 670 474	
	Closeout							2 741 164
	<b>Totals&gt;</b>	<b>333 333</b>	<b>3 797 508</b>	<b>733 723</b>	<b>6 661 255</b>	<b>34 397 892</b>	<b>24 995 474</b>	<b>2 741 164</b>
		<b>Yr1</b>	<b>Yr2</b>	<b>Yr3</b>	<b>Yr4</b>	<b>Yr5</b>	<b>Yr6</b>	<b>Yr7</b>

## **NOTES**

The amounts of R333 333 for Phase 1 pre-feasibility and Phases 2 and 3 preliminary planning are calculated as follows:

<b>UISP subsidy Phase 1</b>	<b>Subsidy per hh</b>
Survey, registration, participation, etc	241
Geotechnical investigation	114
Preplanning	978
<b>Total per hh</b>	<b>1 333</b>
<b>Total per 500 hh</b>	<b>666 666</b>
<b>Total per 500 split between Phase 1 and Phases 2 and 3</b>	<b>333 333</b>

## 4. Preparing a financial plan for an upgrading programme

In the previous section we looked at financial planning at the settlement upgrading plan level. In this section we will be looking at financial plans at the level of the informal settlement upgrading strategy and programme level.

### 4.1 Principles

The preparation of a multi-year financial projection for multiple projects at the programme level is a Medium-Term Expenditure Framework (MTEF). The MTEF is initially informed by estimates at assessment and categorisation level. However as further preparation and feasibility work is completed updated figures are inserted into the MTEF. The municipality's MTEF needs to be aligned with that of funders such as the provincial Department of Human Settlements and COGTA (for MIG).

### 4.2 Budgeting via MTEF

In this section two tables are provided.

The first table is the summary informal settlement upgrading plan for each settlement, which informs the MTEF. This is the same one you used in Module 5: A Programmatic Approach. It is provided for information purposes only since the response plan directly informs the MTEF.

Request the handout of this table: Budgeting via the MTEF: Summary ISU Strategy.

The second table is a simplified MTEF-level budget for the six informal settlements assessed and categorised for the upgrading programme in the first table.

As can be seen, the MTEF responds directly to the summary upgrading plans and ensures that the necessary financial resources are put in place over a multi-year period and across different funders and grant mechanisms so that the plans can be realised.

SUMMARISED INFORMAL SETTLEMENT UPGRADING STRATEGY – MUNICIPAL LEVEL												
Project details								Developmental priorities				
Sett No	Name of Informal Settlement	Categorisation	Urgent health & safety threats?	Rationale / notes	Current shacks	In situ upgr. Yield	Short term relocations	Eventual likely relocations	Basic Services, tenure, housing	Other priorities	Targeted grant instruments	
1	Settlement A	Conventional formal full upgrading (Category A) Immediate relocation (Category C)	N	Site well located close to centre of town. Well established settlement. Most of the site is suitable for formal development but some densification will be required and this is accepted by the community.	723	642	81	81	Land acquisition imminent. Subsidy application approved. Town planning completed. A temporary relocations area will be established whilst phase 2 of the current green-fields housing project is planned & completed. The TRA site is adjacent to the settlement so livelihoods implications will be minimised.	Community participation and socio-survey. Support for local informal ECD centres. Engagement with Department of Education to increase capacity of current SP and high school which cannot cope with current student numbers.	UISP/CS/EH (DHS)	
2	Settlement B	Interim arrangements (incl basic services) (Category)	Y	Site acceptably located 3km from the town centre. Settlement well established. Most of site developable. Some households need to move out of floodplain but can be accommodated elsewhere on site.	1 253	1 253	0	0	Land acquisition does not appear problematic. Project can move from B1 to full upgrade relatively easily. Assist residents to move out of floodplain into other parts of the site.	Community participation and socio-survey. Support for those involved in food gardens. Assess need for a taxi rank.	UISP (DHS)	
3	Settlement D	Interim arrangements (incl basic services) (Category B1)	N	Site well located close to centre of town. It is a high density settlement with high levels of poverty and vulnerability. Most of the site is suitable for permanent settlement but when full upgrading occurs, some relocations may be necessary at that time.	1 213	1 040	0	173	The relocations will eventually be relocated to phase 2 of the abovementioned green-fields housing project when has been planned and built.	Community participation and socio-survey. Support for those involved in food gardens. Assess need for a taxi rank.	UISP (DHS)	
4	Settlement E	Interim arrangements (basic services) (Cat B1)	N	Site characterised by significant rocky outcrops and a portion is located within a floodplain. The settlement is however well-established and geotechnically the area appears stable.	395	395	0	0	Standpipes, VIPs, basic road and footpath access, electricity supply. Although the site is not formally developable, it is very well established and unlikely to be relocated for some time.	As for settlement B (located on the other side of a district road). Improve solid waste removal.	MIG	
5	Settlement G	Interim arrangements (incl basic services) (Category B1)-eventual	Y	Site well located close to centre of town. It is a high density settlement. The entire settlement is located under a powerline and is not formally developable. The site is however otherwise stable. Levels of poverty and vulnerability are high.	221	0	0	221	Standpipes, chemical toilets, temporary electricity supply. Provision of emergency housing improvements (structured materials provision) for those households who are most destitute. Place settlement on long term relocations plan.	Solid waste removal. Engage with Department of Education w.r.t expansion of school.	EH/MIG	
6	Settlement H	Immediate relocation (Category C)	Y	The settlement is located mainly on an old landfill site and residents are exposed to toxicity and other health and safety threats. There are available sites on a Greenfields housing project adjacent to the town with construction being close to completion.	311	0	311	311	Full relocation of entire settlement to a Greenfields housing project where full services, title deeds and formal housing is in the process of being provided. In the short term undertake community education in respect of health and safety threats on site.	Ensure adequate public transport from new Greenfields site to town including access to schools and clinics.	UISP	
					4 116	3 330	392	786				

SIMPLIFIED MTEF- MUNICIPAL LEVEL											
Project details				Budget				MTEF - 3 Year			
No	Name of Informal Settlement	Categorisation	Units / sites / benef	Total budget required	Grants targeted	DHS split	MIG/USDG split	Year 1	Year 2	Year 3	Total 3yr cycle
1	Settlement A	A: Full Upgrade	642	94,579,887	UIISP/CS	94,579,887	0	5,304,000	9,024,101	9,024,101	23,352,202
		C: Relocation - TRA	81	4,787,424	EH	4,787,424	0	4,787,424	0	0	4,787,424
2	Settlement B	B1: Incr. upgrade - basic services	1,253	10,351,887	UIISP	10,351,887	0	5,175,943	5,175,943	0	10,351,887
		Ph2&3 Perm. eng services & design		35,224,918	UIISP	35,224,918	0	0	0	17,612,459	17,612,459
3	Settlement D	B1: Interim Services	1,213	10,021,420	UIISP	10,021,420	0	5,010,710	5,010,710	0	10,021,420
4	Settlement E	B1: Basic services	395	3,555,000	MIG	0	3,555,000	3,555,000	0	0	3,555,000
5	Settlement G	B2: Basic services	221	1,989,000	MIG	0	1,989,000	1,989,000	0	0	1,989,000
		B2: Emergency Housing	45	2,424,600	EH	2,424,600	0	2,424,600	0	0	2,424,600
6	Settlement H	C: Relocation - assistance	311	454,514	UIISP	454,514	0	454,514	0	0	454,514
7	Sewer treatment upgrade and extended outfall		n/a	5,325,000	MIG	0	5,325,000	1,597,500	3,727,500	0	5,325,000
8	Water treatment upgrade & connector		n/a	4,625,000	MIG	0	4,625,000	1,387,500	3,237,500	0	4,625,000
9	various	Greenfields	850	126,306,167	IRDP	126,306,167	0	5,572,838	11,834,125	11,834,125	29,241,088
			<b>5,011</b>	<b>299,644,817</b>		<b>284,150,817</b>	<b>15,494,000</b>	<b>37,259,029</b>	<b>38,009,879</b>	<b>38,470,685</b>	<b>113,739,594</b>
			<i>Units / sites / benef</i>	<i>Total budget required</i>		<i>DHS split</i>	<i>MIG/USDG split</i>	<i>Year 1</i>	<i>Year 2</i>	<i>Year 3</i>	<i>Total 3yr cycle</i>

ABBREVIATIONS: CS = consolidation subsidy (topstructure phase); EH = Emergency Housing grant; MIG = Municipal Infrastructure Grant; TRA = Transitional relocation area; UIISP = Upgrading of Informal Settlement Grant;

**ACTIVITY11.5: WHAT DID YOU GAIN?**

*Write down five useful things you learnt in this module.*

1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_
4. \_\_\_\_\_
5. \_\_\_\_\_



## Toolkit

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You will find the following resources on the Toolkit CD:

- Grant Instruments for Informal Settlement Upgrading.
- DHS Subsidy Quantum 2014-2015 Combined.

## References and Resources

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### Reference Material

- National Department of Human Settlements: Project Process Guide (2010).
- Informal Settlement Rapid Assessment and Categorisation Guideline and Summary Guideline (HDA/PPT 2014).
- Financial Interventions — Accreditation of Municipalities from Part 3 of the Housing Code.
- Project Preparation Cycle (Planning Cycle) – PPT.
- Understanding the Division of Revenue Act, Philip Davids, The Mvula Trust, <http://www.mvula.co.za/>
- USDG, National Treasury Presentation September 2012.
- MIG Policy Framework.
- MIG User Guideline.
- MIG specifications and unit cost guide.

### Useful Links

- NUSP Resource Kit: <http://www.upgradingsupport.org/content/page/nusp-resource-kit>
- Summary upgrading toolkits: [http://www.pptrust.org.za/index.php?option=com\\_docman&Itemid=127](http://www.pptrust.org.za/index.php?option=com_docman&Itemid=127)
- Project Preparation Trust informal settlement resources: <http://www.pptrust.org.za>