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Dear Ms Maree

2022-2023 ACCOUNTING MANUALS FOR DEPARTMENTS PUBLISHED FOR COMMENT

The South African Institute of Chartered Accountants (SAICA) welcomes the opportunity to make submissions to the OAG on the 2022-2023 Accounting Manuals for Departments published for comment.

SAICA is South Africa's pre-eminent accountancy body which is widely recognised as one of the world's leading accounting institutes. The Institute provides a wide range of support services to more than 52 000 members who are chartered accountants [CAs (SA)] and associates who hold positions as chief executive officers, managing directors, board members, business owners, chief financial officers, auditors, and leaders in their spheres of business operation.

Our work in the public sector goes beyond member support but also includes a significant focus on advocacy and capacity building to support and encourage an improvement in public finance management.

SAICA supports and appreciates the OAG providing guidance to departments to ensure that the Modified Cash Standards are applied appropriately and believes that regular maintenance through reviews and amendments to issued guidance are key to maintain the effectiveness and relevance of the guidance to better support preparers of financial statements.

For ease of reference, we include our responses as follows:

a) Annexure A - our detailed comments to the amendments to the Accounting Manuals for Departments.
b) Annexure B – our general comments on the OAG's amendments process

Members have been consulted in responding to the amendments to the Accounting Manuals and therefore the comments reflected in the annexure consider the view of the membership.

We would also appreciate the opportunity engage further and we would be willing to discuss the comments, if required. Please do not hesitate to contact Odwa Benxa (odwab@saica.co.za) in this regard.

Regards,

Natashia Soopal
Executive: Ethics Standards and Public Sector at SAICA

Odwa Benxa
Project Director: Public Sector at SAICA

ANNEXURE A – Comments on the Accounting Manuals for Departments

Legend:

[ ] Words in bold type in square brackets indicate omissions from existing guidance

__________ Words underlined with a solid line indicate insertions in existing guidance

No.	Paragraph	Comments	Recommendation
1.	**03. Financial Statements Presentation** **3.2.2 Secondary Financial Information** **Can a department provide additional information in the financial statements over and above what is required by the MCS?** According to paragraph .11 of Chapter 3 on Financial Statement Presentation, "Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, revenue and expenses set out in the Standard. The application of the Standard with additional disclosures, when necessary, is presumed to result in financial statements that achieve fair presentation." Further to this paragraph .12 states "The additional disclosures mentioned above are necessary when specifically required by this Standards, or when compliance with the specific requirements in the Standard is insufficient to enable users to understand the effect of particular	SAICA agrees with the amended guidance but have noted that there is no guidance on how the materiality concept can be applied by departments when making decisions about what additional information to include in the financial statements.	SAICA recommends that the concept of materiality be explained in accordance with the MCS Guideline on Materiality issued by National Treasury to guide the departments to promote consistency across all the departments. Alternatively, reference to the MCS Guideline on Materiality should be made in this section for the departments to refer to when applying their judgement with regards to the additional information to be included in the financial statements.

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	transactions, other events and conditions on the department's financial position and financial performance." From the above, it is clear that the MCS does not prohibit the inclusion of additional information in the financial statements that is not specifically required, and that it is in fact encouraged or even required, if the additional information: • is necessary to achieve fair presentation; • is useful and relevant to users; and • is likely to influence the decisions made by users on the basis of the financial statements, by enabling users to understand the impact of particular transactions, other events and conditions on the department's financial position and financial performance. However, any additional information included in the financial statements should not: • be misleading to the users; • reduce users' understanding of the entity's financial statements, or transactions, other events and conditions; • provide immaterial information; • obscure or make the material information in financial statements less visible; • detract from the information that is required by the Standard; • be contrary to the department's accounting policies; • be in conflict with the objective of financial statements as set out in Chapter 2 on Concepts and Principles; or • be inconsistent with the definitions, the qualitative characteristics and constraints, or the recognition criteria and measurement concepts for assets, liabilities, revenue and expenses in Chapter 2. The OAG provides standardised formats for preparation of financial statements in a form of AFS Specimen and AFS Template to achieve consistency. The preparers should not amend the format of the AFS Specimen / AFS Template (unless permitted by the OAG). Ordinarily, additional		

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	information is included in the narrative blocks provided in the AFS Specimen and the AFS Template. Furthermore, additional information can also be included in the Accounting Officer's Report of the annual report.		
2.	**11. Capital Assets** **3 Scope** **Finance lease accounting changes from 2023-24 financial year** Accounting for finance lease assets is being aligned with GRAP 13 on *Leases*. These capital assets are to be recorded, accounted for and reported in accordance with MCS Chapter 11 from the inception of the finance lease. This implies that the finance lease assets will be recorded in the asset register from the inception of the lease as a non-cash addition (the asset is received in advance and paid for in instalments as per the lease agreement) and be reported in line with relevant MCS Chapter 11 disclosure notes	SAICA supports the alignment with Standards of GRAP as this assist in preparing departments for transition to accrual accounting.	None.
3	**11. Capital Assets** **03. Scope** **Capital assets versus Inventory classification** Some departments acquire or construct capital assets for distribution (movable and immovable assets) as part of their normal operations. These capital assets should be classified as inventory only if they meet the definition of inventory as outlined in Chapter 12 on Inventories. However, immovable assets constructed or purchased for distribution which ordinarily meet the definition of inventories are still to be classified and reported on as capital assets in line with the requirements of the MCS chapter 11 until the inventory is effective. The actual	SAICA noted that the paragraphs are not clear in terms of when is inventory regarded as effective.	SAICA recommends that these paragraphs be clarified to avoid any confusion to the preparers.

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	distribution of these capital assets to the beneficiaries should comply with the requirements of PFMA section 42.		
4	**6. Accounting for Immovable Assets** 1. The valuing of specific immovable assets at R1,000 is only permitted in exceptional cases. These specific exceptional cases are listed in MCS 11.72A and explained in section 4 of Annexure A: The fair value model based on municipal valuation rolls, sales comparison, exceptional cases, and replacement cost to immovable asset registers of National and Provincial Custodians as a carrying value (Previously, Annexure A of Accounting and Reporting for Immovable Assets document that is now Appendix A of MCS Chapter 11) of this AMD. 2. Annexure A: The fair value model based on municipal valuation rolls, sales comparison, exceptional cases, and replacement cost to immovable asset registers of National and Provincial Custodians as a carrying value (Previously, Annexure A of Accounting and Reporting for Immovable Assets document that is now Appendix A of MCS Chapter 11) of this AMD is a valuation methodology that was developed by the major custodians of immovable assets. The departments are referred to it for consideration purposes. **[Certain specific exceptional cases have been excluded from this requirement for practical and cost containment reasons.]** The fair value of an immovable capital asset is usually its market value determined by an appraisal. An appraisal of the value of the asset is normally, but not necessarily undertaken by a member of the valuation profession, who holds a recognised and relevant professional qualification. As the cost of such exercise can be very high, it is recommended for use only when consideration is given to	SAICA agrees with the amendment as the valuing of immovable assets at R1000 is limited to exceptional cases and guidance is provided thereto	None.

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	<u>disposal to determine a more accurate value. For recording purposes, the value of an immovable asset can be estimated by someone with sufficient experience in the built environment.</u> <u>For some assets, it may be difficult to establish their market value because of the absence of market transactions for these assets. Some departments may have significant holdings of such assets. In certain circumstances, it may also be costly to undertake a detailed professional valuation of each individual property, particularly for those departments that act as default custodians of the state's immovable assets.</u> <u>To facilitate cost-effective compliance with the MCS and to avoid unnecessary duplication of costs across different spheres of government, departments are encouraged to as far as possible make use of existing available information (for example municipal valuation rolls) as an alternative to undertaking their own professional valuations on each individual immovable asset. Should the municipal valuation change the department should not revise the initial recognition amount except if there is evidence that the initial recognition value was erroneous.</u> A department should use <u>any other relevant</u> **[the]** principles and guidance in the Section on Fair value above in determining the fair value of a capital asset.		
5	**6.2 Leasehold / capital improvements on the existing property** In the event that there is uncertainty whether the expenditure represents an improvement (capital) or maintenance (current) the following can be considered: • Will the cost incurred enhance the service provision capacity of the asset beyond original expectation? Will	SAICA noted that the guidance is not clear with regards to what constitutes capital improvement or maintenance while departments are expected to document their own policy on how to differentiate between the two expenditures, this may result in reporting inconsistencies between departments.	SAICA recommends that there should be clear guidance to assist departments to differentiate between capital improvements and current expenditure. We further recommend that the following sentence be reworded to "Where any of the answers to the questions above result in a positive response it is an improvement rather than maintenance" to give clear direction to the departments

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	the expenditure result in an increase in performance beyond the original performance? • Will the cost incurred increase the useful life of the main asset? • Will the cost incurred increase the size of the asset or change its shape? • Will the cost incurred amount to significant savings in future? Where any of the answers to the questions above result in a positive response it is likely to be an improvement rather than maintenance. Departments are expected to **[must]** document their own policy on how to differentiate between capital improvements and current **[maintenance]** expenditure (repairs and maintenance). The policy should clearly indicate the approach to the decision-making process. All conclusions should also be documented and made available to the auditors as and when required.		which will also allow for consistent application by all departments.
6	**8. Disclosure of Capital Assets** **Deleted additions and disposals disclosure notes** The departments were previously required to report on the additions and disposals as follows: "additions to movable assets for the reporting period, showing separately: (i) cash additions; (ii) non-cash additions; (iii) capital work-in-progress current costs and finance lease payments; and (iv) items received in current period, not paid (and paid in current year, received in prior year)." "disposals of movable assets for the reporting period, showing separately:	Paragraph .96 Modified Cash Standard *Chapter 11: Capital Assets* requires that departments must disclose additions and disposals of major movable assets in the notes to the financial statements. However, the Accounting Manual states that the departments are NOT required to disclose these deleted notes on the annual financial statements. It is not clear from the Accounting Manual whether the intention is for the previously required split in the disclosure note is now required to be combined into one line item of additions and disposals respectively.	SAICA recommends that the guidance in the Accounting Manual should clearly state whether the previous split is now combined as one line item for additions and disposals, respectively. This will assist in ensuring that there is no confusion on the prepares of the financial statements.

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	(i) cost of assets sold for cash; (ii) cost of assets transferred out or destroyed or scrapped; and (iii) total actual cash received from disposals." The departments are NOT required to disclose these deleted notes on the annual financial statements. However, due to the usefulness of the information, the departments are expected to keep this information as part of the working papers to the annual financial statements	The OAG should further consider that the removal of the previously required disclosures on additions and disposals may reduce the incentive for departments to maintain movable assets registers that are accurate and complete.	
7	**13. Leases** **6.1 Finance lease in the financial statements of lessee** **Finance leases recording as assets from commencement of lease term effective 1 April 2023** Paragraph .35 of the MCS Chapter on Leases states: .35 As part of the Amendments to the Modified Cash Standard (Issued on 31 March 2022), from 1 April 2023 paragraphs .17 - .18 will be amended as follows: .17 At the [**end**] commencement of the lease term, a department that is a lessee shall measure record all the finance lease assets [**acquired**] at: (a) [**cost, being**] the fair value of the leased asset or, if lower, (b) the [**sum**] present value of the minimum lease payments made, [**including any payments made to acquire ownership at the end of the lease term, excluding interest.**] each determined at the inception of the lease.	SAICA agrees with the amendment as it is in line with Standards of GRAP 13 on Leases. However, the OAG should consider relooking at the below sentence as it may contain an error. ".17 At the [**end**] commencement of the lease term, a department that is a lessee shall *measure record* all the finance lease assets [**acquired**] at".	None.
8	**15. Related party disclosures** **4.1 Control** Departments within the national sphere of government are related parties because they operate together to achieve	SAICA agrees with the amendment as it clarifies the confusion with regards to the relationship between municipalities and Departments.	The OAG should consider updating Provincial Legislature to Parliament.

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	common objectives determined by Cabinet and Provincial Legislature. Similarly, departments within a specific province are related parties. However, a department in one province is not "related" to another department in a different province. In addition, a municipality is not necessarily a related party to a department <u>as they are not under common control. Unless there is other evidence to the contrary, such as a municipality being put under administration and reporting to the department, the transactions between a department and a municipality are not related party transactions.</u>	However, SAICA has noted that there is reference to a Provincial Legislature in the below sentence even though the sentence is explaining related party relationships within the national sphere of government: Departments within the national sphere of government are related parties because they operate together to achieve common objectives determined by Cabinet and *Provincial Legislature.* The reference should rather be to Parliament instead of the Provincial Legislature.	

ANNEXURE B – General Comments on the OAG's amendments process

No	Comment	Recommendation
1	SAICA noted that the proposed amendments to the Accounting Manuals are not accompanied by the basis or rationale for the amendments so that the preparers of financial statements and other stakeholders can understand what informs the proposed amendments, enabling them to make well informed decisions when they comment on the amendments.	SAICA recommends that the proposed amendments issued for comments should include the basis or rationale for the amendments so that the preparers of financial statements and other stakeholders can understand what informs the proposed amendments. SAICA encourages the OAG to consider amending the current process to one that is similar to the Accounting Standards Board's (ASB) when issuing proposed amendments to Modified Cash Standards, Accounting Manuals and other Guides for comments. This would entail the issuing of explanatory material that details the background and rationale of the proposed amendments to ensure that participants have all the relevant information when providing comments which would in turn ensure that the OAG receives value-adding comments.

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