

31 January 2022

Ms Karen Maree

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Dear Ms Maree

2022-2023 MODIFIED CASH STANDARDS (MCS) PUBLISHED FOR COMMENT

The South African Institute of Chartered Accountants (SAICA) welcomes the opportunity to make submissions to the OAG on the 2022-2023 MCS standards 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 [AGAs(SA)] 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 believes that regular reviews and amendments to accounting standards are key to ensure that accounting standards are fit for purpose and respond to the needs of users of financial statements.

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

- (a) Annexure A - our detailed comments to the amendments to the MCS.
- (b) Annexure B - Transition from the Modified Cash Standards to accrual accounting for departments;
- (c) Annexure C - Improved process for the amendments of the MCS.

Members have been consulted in responding to the Modified Cash Standards and therefore the comments reflected in the annexures considers 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,

A handwritten signature in black ink, appearing to read 'Soopal'.

Natasha Soopal
Executive: Public Sector at SAICA

A handwritten signature in black ink, appearing to read 'Siyamdumisa Vilakazi'.

Siyamdumisa Vilakazi
Chairperson of SAICA National
Public Sector Committee

A handwritten signature in black ink, appearing to read 'Odwa Benxa'.

Odwa Benxa
Project Director: Public
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ANNEXURE A – Comments on Chapter amendments

No.	Chapter	Paragraph	Comments	Recommendation
1.	Chapter 5: APPROPRIATION STATEMENT	<p>Presentation and disclosure of a comparison of budget and actual amounts</p> <p>.14 A department shall present a comparison of the budget amounts for which it is held publicly accountable and actual amounts as a separate additional financial statement. The comparison shall present the following separately: the approved and final budget amounts; the actual expenditure;</p> <p>.15 Presentation in the financial statements of the approved and final budget amounts and the actual amounts will complete the accountability cycle by enabling users of the financial statements to identify whether resources were obtained and used in accordance with the approved budget. In addition, users can assess management decisions with regard to virements</p>	<p>Members agree with the amendment as the disclosure will allow for department disclosures to be aligned with the disclosure requirements for public entities and municipalities that are reporting on Standards of Generally Recognised Accounting Practice (Standards of GRAP); specifically GRAP 24 <i>Presentation of Budget Information in Financial Statements</i> which requires a comparison of budget amounts and the actual amounts arising from execution of the budget to be included in the financial statements of entities that are required to, or elect to, make publicly available their approved budget(s) and for which they are, therefore, held publicly accountable.</p> <p>Further, members supports the rational that presentation in the financial statements of the approved and final budget amounts and the actual amounts will complete the accountability cycle by enabling users of the financial statements to identify whether resources were obtained and used in accordance with the approved budget</p>	<p>GRAP 24, as previously referenced, also requires disclosure of an explanation of the reasons for material differences between the budget and actual amounts to ensure that entities discharge their accountability obligations and enhance the transparency of their financial statements by demonstrating compliance with the approved budget for which they are held publicly accountable.</p> <p>It would therefore be useful for a similar requirement to be included in MCS <i>Chapter 5: Appropriation Statement</i> to further enhance the transparency and accountability principle being introduced by this chapter in relation to the users of the financial statements.</p>



No.	Chapter	Paragraph	Comments	Recommendation
2.	Chapter 9: GENERAL DEPARTMENTAL ASSETS AND LIABILITIES	.06 A department may recognise a prepayment or an advance, made before 1 April 2023, in the statement of financial performance in accordance with Chapter 8 on Expenditure if the prepayment or the advance is material and was budgeted for as an expense in the year in which the actual prepayment or advance was made.	<p>Majority of members agree with the amendment.</p> <p>However, based on member consultation, some members disagreed with this amendment with the following reasons:</p> <ul style="list-style-type: none"> • They should have to recognise the prepayment as an asset; • Recognising a prepayment as an expense will be incorrect. At this stage a transaction has not occurred. This opens room for abuse on department that cannot spend their budgets timeously. As at year end, they will make prepayment on contracts where goods and service have not been delivered. The public sector has been suffering from non-performance by contractors and if this amendment is allowed it will increase the problem and not solve it. Prepayment should be the last resort. Operational failures should not be cured by amendments to the accounting standards; We need to define what constitute material prepayment or advance, otherwise the disclosure will be subjective and there will be inconsistency in the application of the standard. 	SAICA recommends that a materiality guide/ framework should be developed to assist preparers on how to apply the concept of materiality in the AFS for departments.
		Chapter 11: CAPITAL ASSETS	Members agree with the amendments.	None



No.	Chapter	Paragraph	Comments	Recommendation
		<p>.06 In addition, this Chapter does not apply to: (a) the initial recognition and initial measurement of capital assets acquired in a transfer of functions (see Chapter 19 on Transfer of Functions) or a merger (see Chapter 20 on Mergers)</p>		
		<p>.104 The scope exclusion paragraph .05 will be removed from 1 April 2023. By implication a department will record a capital asset subject to a finance lease in accordance with this Chapter on commencement of the lease term as defined in Chapter 13 on Leases.</p> <p>.105 For finance lease agreements entered into prior to 1 April 2023, the department records the capital asset retrospectively in the notes to the financial statements at the present value of the minimum lease payments (determined at the inception of the lease).</p>	<p>Members agree with the amendment. In addition, the recommendation stated below in relation to the rate implicit in the lease should be considered.</p>	<p>Refer to below recommendation.</p>
3	Chapter 13: LEASES	<p>From 1 April 2023 paragraphs .17 - .18 will be amended as follows</p> <p>.17 At the commencement of the lease term, a department that is a lessee shall measure all finance lease assets at: (a) the fair value of the leased asset or, if lower, (b) the present value of the minimum lease payments. The discount rate to be used in calculating the present value of the minimum lease payments is the interest rate implicit in the lease, if this is practicable to determine; if not, a reasonable proxy</p>	<p>Members agrees with the amendment.</p>	<p>National Treasury should consider developing guidance that provides clarity on instances where it would be impractical to determine the rate implicit in the lease. This would also assist with ensuring a consistent application of the standard.</p>



No.	Chapter	Paragraph	Comments	Recommendation
		<p>rate such as the prime lending rate at inception of the lease can be used.</p> <p>Refer also to the Transitional provisions in Chapter 11 on Capital Assets.</p>		

Annexure B – Transition to accrual basis of accounting by departments

Background

1. Section 40(1)(b) of the Public Finance Management Act, 1999 (PFMA) requires that the accounting officer for a department must prepare financial statements for each financial year in accordance with generally recognised accounting practice
2. The Accounting Standards Board (ASB) is required in terms of the PFMA, to determine generally recognised accounting practice referred to as Standards of Generally Recognised Accounting Practice (GRAP). The Board must determine GRAP for:
 - departments (including national, provincial and government components);
 - public entities;
 - trading entities (as defined in the PFMA)
 - constitutional institutions;
 - municipalities and boards, commissions, companies, corporations, funds, or other entities under the ownership control of a municipality; and
 - Parliament and the provincial legislatures.
3. The Minister of Finance has exempted national and provincial departments as well as government components which apply the MCS from complying with PFMA section 40(1)(b) for a period of five years, effective 8 April 2021. This in effect means that departments are exempted from applying the Standards of GRAP as determined by the ASB and instead are applying MCS as determined by National Treasury in terms of Treasury Regulation 18.2.
4. SAICA acknowledges the effort by National Treasury to improve reporting on the Modified Cash Standards, as well as the budget constraints with regards to resources to move to accrual accounting, however we believe that a plan needs to be developed, implemented, and strictly monitored to assist with the transition to accrual accounting. This should be shared with key stakeholders so that support and resources can be provided by stakeholders where possible to support government on this project.
5. **Benefits of accrual accounting for government¹**

Financial Position

Accrual accounting provides information on an entity's financial position and current assets and liabilities, based on the balance sheet. Government needs this information to make decisions about the feasibility of financing the provided services; plan the future funding requirements of asset maintenance and replacement; plan the repayment of existing liabilities and, thus, manage their cash position and financing requirements. Accrual accounting highlights the impact of financing decisions on net assets/equity, leading entities to take a longer-term view when making financing decisions.

¹ Arguments for introducing accrual-based accounting for public sector – Munich Personal RePEc Archive



Financial Performance

Accrual accounting provides information on revenues and expenses, including the impact of transactions where cash has not yet been received/paid. Knowing revenues is essential for assessing the impact of taxation on the government's fiscal position and the need for borrowing in the long term. Knowing expenses is necessary to assess revenue requirements, the sustainability of existing programs, and the likely cost of proposed activities and services. The income statement helps governments to focus on management by results as well as management of resources, which become more useful because performance can be measured more reliably when full costs for a period are considered.

Cash Flows

Moving to an accrual basis of accounting does not mean the abandonment of cash accounting, cash management being an integral element of accrual-based financial management framework. It is required the production of a full statement of cash flows to separately identify cash receipts and payments associated with operating, investing, and financing activities. Modern accrual-based systems have functionalities to support cash-based accounting and reporting. Accrual accounting provides comprehensive information on current and certain projected cash flows, including those associated with accounts and receivables, leading to better cash management, and assisting in preparation of more accurate cash budgets.

Reporting and Budgeting

Any reform is considered successful only when it brings about changes in the behaviour of the people the reform is targeted toward. Accrual reporting objective is to provide understandable, relevant, reliable, and comparable information, useful to a wide range of users in making economic decisions. It incorporates non-cash information, such as revaluations, write-offs, consumption of assets through depreciation, pension liabilities. Financial reports must rely on the budget and show any differences between the actual results and the budget, as well as any changes during the term.

6. The use of accrual basis of accounting further allows for the following²:
 - **Greater transparency and accountability** in government financial reporting.
 - **Better decision-making** that focuses on both the short and long-term impact of decision-making.
 - **Monitoring of government debt and liabilities** for their true economic implications through the disclosure of all liabilities, including long-term obligations of government which may encourage government leaders to make decisions that focus on long-term sustainability and not driven by short-term political incentives.
 - **Provides greater transparency which is required by the public, banks, investors, and credit providers as generally expected from the private sector.**
 - Provides for **comparability** of financial information on a global basis to assist in resource allocation, monitoring and accountability.
 - The preparation of public sector budgets and appropriations on the same basis.

² Adopted from International Federation of Accountants paper titled *The Importance of Accrual-based Financial Reporting in the Public Sector*

7. In addition to the above, a consistent accounting basis would lead to a seamless consolidation where the financial position, performance and cash flows of the state can be better presented as departments and public entities would be on the same basis of accounting.
8. SAICA therefore urges the government to move to accrual basis of accounting by departments to realise the benefits listed above.

International overview

9. In terms of International Public Sector Financial Accountability Index 2018 Status Report issued by the IFAC and The Chartered Institute of Public Finance & Accountancy (CIPFA), which contains data from 150 jurisdictions, 25% (37) governments reported in accrual accounting while 45% (67) are transitioning to accrual or already have some element of accrual in their financial reports (refer to *diagram 1* below).

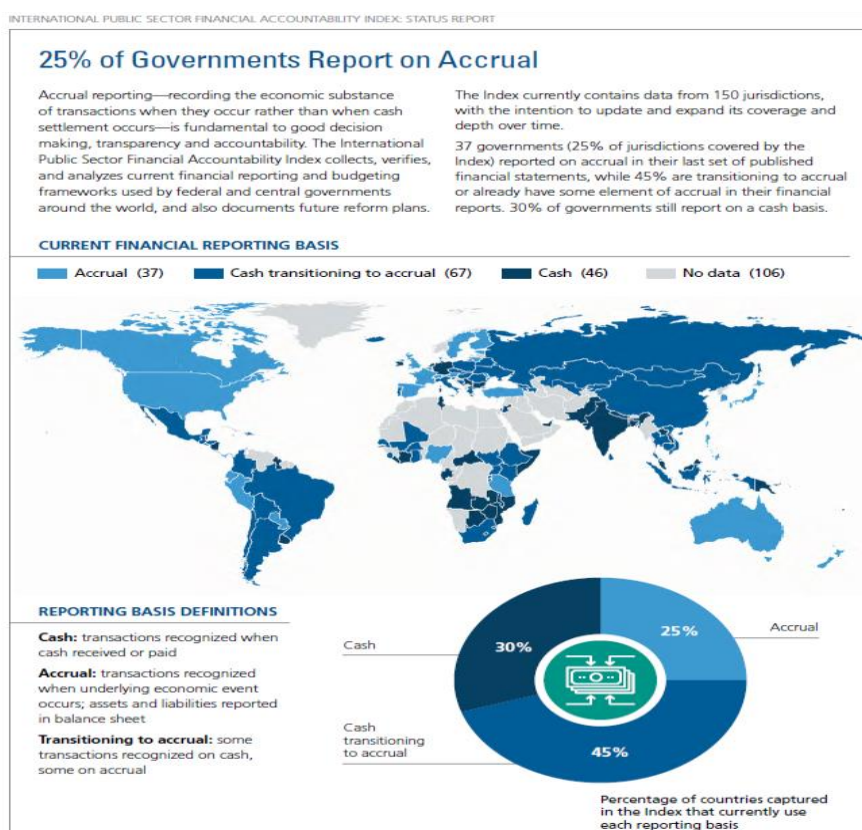


Diagram 1

10. In the same report, it was indicated that 65% of government are expected to report on an accrual basis within five (5) years (refer to diagram 2 below).

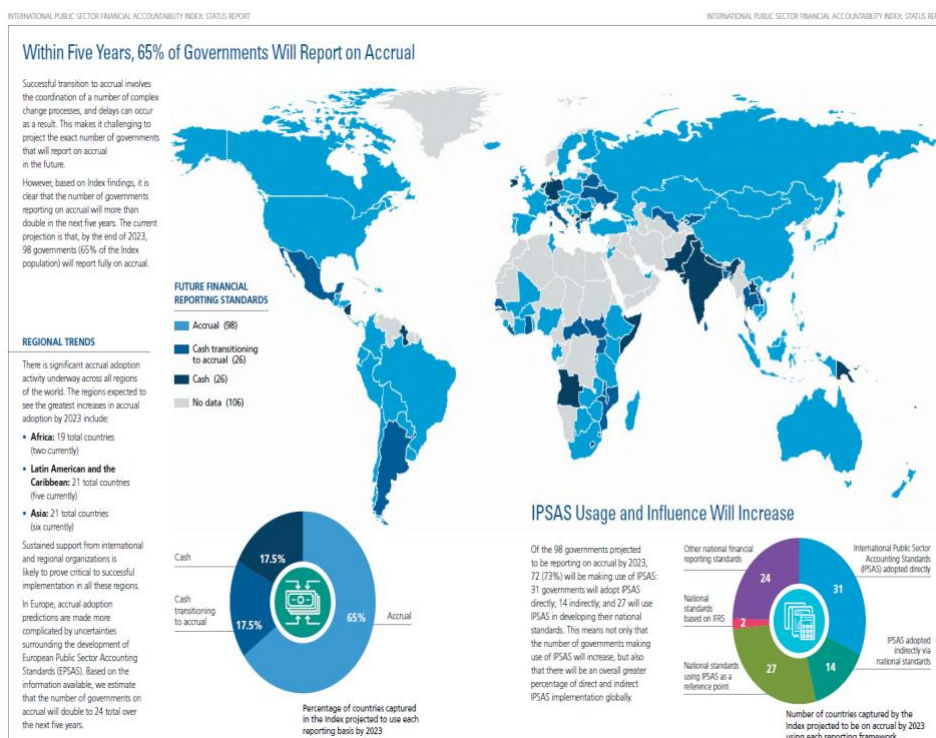


Diagram 2

11. South Africa currently applies both accrual basis and transition to accrual basis. Further, South Africa is part of the countries estimated to be on the full accrual basis by the year 2023.
12. However, due to the current PFMA section 40(1)(b) exemption, and lack of information or communication regarding the National Treasury's transition plans, South Africa may not be able to move to full accrual basis of accounting by 2023 and thus faces the risk of falling behind in international trends.
13. SAICA therefore reiterates the urge for departments to expeditiously move to an accrual basis of accounting.



Annexure C – Improving the process of amending the MCS

1. SAICA highlights the importance of accounting standards following due process.
2. The due process followed by National Treasury in developing the MCS is as follows³:
 - Research is carried out to identify and review issues associated with the topic and to consider the application of the concepts and principles to the issues.
 - The principles in the existing accounting standards, such as Generally Recognised Accounting Practice (GRAP), International Public Sector Accounting Standards (IPSAS) or International Financial Reporting Standards (IFRS), are also studied.
 - Where required, the national and provincial legislation is consulted to develop principles and or required disclosures.
 - The draft Standard is exposed for comment by interested parties including auditors, preparers, standard setters, public sector consultants and individuals.
 - The draft is published on the OAG's website for a period to allow interested parties to consider and comment on the Standard.
 - The OAG considers all comments received and makes modifications where appropriate.
 - The Standard is reviewed by the OAG periodically. The process for the amendment of the Standard will be as described in the preceding paragraphs.
 - The appendices are updated periodically to provide clarification on issues arising from time to time for example during the preparation of the departmental financial statements and or the audit thereof.
3. In contrast, the International Public Sector Accounting Standards Board (IPSASB) due process involves the below steps (summarised)⁴:
 - a. **General**
 - IPSASB meetings to discuss the development, and to approve the issue, of international standards are open to the public.
 - b. **Project Identification and Prioritization**
 - The IPSASB identifies potential new projects based on a review of national and international developments and on comments and suggestions from those who have an interest in the development of international standards issued by the IPSASB. When considering potential new projects, the IPSASB also considers the objectives of financial reporting and user needs, as described in The Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities.

³ Adopted from paragraphs .14 to .16 of *Chapter 1: Preface to the Modified Cash Standard*

⁴ IPSASB DUE PROCESS AND WORKING PROCEDURES—JUNE 2016



- To facilitate this process, The IPSASB periodically carries out a **consultation** process that informs the development of the strategy and work plan.

c. Project Commencement

A proposal to start a new project is prepared based on research and on appropriate consultation within the IPSASB, with consideration given to the costs and benefits of the anticipated output of the proposed project. The project brief is circulated to other IFAC Boards and Committees to identify matters of possible relevance to the project. The IPSASB considers and prioritizes the project brief having regard to the public interest. As appropriate, the IPSASB approves, amends, or rejects the project brief in a meeting open to the public.

d. Development of Proposed International Standards

- The IPSASB considers whether to issue a consultation paper, or hold a public forum or roundtable, to solicit views on a matter(s) under consideration. The IPSASB also considers the appropriateness of conducting a field test of the application of its proposals for a new or revised international standard. The decision to undertake any of these steps may be made at any stage before or after a draft international standard is issued for public exposure. The rationale for the IPSASB's decision in relation to these steps is discussed at an IPSASB meeting and the decision minuted. Comments received on a consultation paper, or through a public forum or roundtable, are considered in the same manner as comments received on an exposure draft.
- When the IPSASB staff is satisfied that it has a proposed draft international standard that is ready for exposure, the draft is presented to the IPSASB.
- The IPSASB votes on the approval of an exposure draft of the proposed international standard in accordance with the IPSASB's terms of reference.

e. Public Exposure

- Approved draft international standards are exposed for public comment.
- The exposure period will ordinarily be 120 days.
- Comments made by respondents to an exposure draft are a matter of public record and are posted on the IPSASB website after the end of the exposure period

f. Consideration of Respondents' Comments on an Exposure Draft

Members of the IPSASB familiarize themselves with the issues raised in comment letters on exposure drafts such that they can make well informed decisions as they finalize an international standard. The IPSASB deliberates significant matters raised in the comment letters received, with significant decisions recorded in the minutes of the meeting of the IPSASB.

g. Interaction with the IPSASB Consultative Advisory Group

The IPSASB is responsible for consulting with the IPSASB Consultative Advisory Group (CAG) on the identification and prioritization of projects to be undertaken by the IPSASB. In particular, the CAG is consulted on the IPSASB's



strategy and work plan, including project priorities and any changes therein, to help establish their appropriateness. Where the CAG has recommended a project for consideration by the IPSASB, the Chair of the IPSASB informs the PIC and the CAG of the decisions of the IPSASB.

h. Matters of Due Process

The IPSASB Chair and Technical Director provide the PIC with a summary of the application of due process for new or revised IPSASs before their release. The Chair of the CAG is responsible for advising the PIC on whether due process relating to the IPSASB's interaction with the CAG is being followed.

i. Approval of an International Standard, and Consideration of the Need for Re-Exposure

- When the staff is satisfied that it has a proposed final international standard that is ready for approval, it presents the revised content of the exposed international standard to the IPSASB for approval.
 - The IPSASB votes on the approval of the final revised content of an exposed international standard in accordance with its terms of reference.
 - Where applicable, the IPSASB sets an effective date for the application of the final international standard.
 - For each final international standard, the IPSASB issues basis for conclusions with respect to comments received on an exposure draft.
4. It can be noted that the IPSASB process is much more detailed than the National Treasury process and ensures that the process is available to the public as meetings are open to the public and minutes of the meetings are available on the website.
 5. The current process does not allow for wide consultation with stakeholders, as in some instances stakeholders are not aware of the amendments to the MCS as they are unable to locate the document on the website, and the commenting process is not printed in the government gazette as per amendments with other legislation in South Africa.
 6. SAICA encourages National Treasury to consider a standards amendment process that is similar to the IPSASB's, or locally the Accounting Standards Board.
 7. SAICA further recommends that the process for revising the MCS is documented, approved, and is made available to the public.
 8. This will ensure that the standards developed are developed with the user in mind, it will ensure that there is fair presentation in the financial statements that departments produce and that standards developed better enable users to make decisions and address users challenges.



References

1. GRAP 1: Presentation of Financial Statements

[This Standard was approved by the Public Sector Committee of the International Federation of Accountants \(asb.co.za\)](#)

2. International Public Sector Financial Accountability Index 2018 Status Report

[IFAC-CIPFA-Public-Sector-Index-2018-Status.pdf](#)

3. IPSASB Due Process and Working Procedures—June 2016

[IPSASB-Due-Process-and-Working-Procedures-June-2016.pdf \(ifac.org\)](#)

Arguments for introducing accrual-based accounting in the public sector

Munich Personal RePEc Archive

https://mpra.ub.uni-muenchen.de/18134/1/MPRA_paper_18134.pdf