

**REPORT ON THE ADM BUDGET ADJUSTMENTS FOR THE FINANCIAL  
YEAR 2011/2012**

[File No. 5/1/R]  
[Author: Chief Financial Officer: YZ/sck]

**ADJUSTMENT TO THE 2011/2012 BUDGET**

**PURPOSE**

To seek the Executive Mayor's approval for:

- 1) An adjustment to the 2011/12 budget, to increase the provision for bad debts by R94 758 592.

**AUTHORITY**

The Municipal Finance Management Act 56 of 2003 (MFMA).

**LEGAL/STATUTORY REQUIREMENTS**

Section 29 of the Municipal Finance Management Act dealing with unforeseen and unavoidable expenditure stipulates:

- (1) The mayor of a municipality may in emergency or other exceptional circumstances authorize unforeseeable and unavoidable expenditure for which no provision was made in an approved budget.*
- (2) Any such expenditure –*
  - a) Must be in accordance with an framework that may be prescribed;*
  - b) May not exceed a prescribed percentage of the approved annual budget;*
  - c) Must be reported by the mayor to the municipal council at its next meeting; and*
  - d) Must be appropriated in an adjustments budget.*
- (3) If such adjustments budget is not passed within 60 days after the expenditure was incurred, the expenditure is unauthorized and section 32 applies.*

**REASONING/BACKGROUND**

During the audit of the 2011/12 annual financial statements, the Auditor General did a reasonability test on the existing Provision for Bad Debts, resulting in an adjustment to this provision being necessary.

### **Audit Outcome**

The outcome as per Communication of Audit Finding Number 24, Item 2, dated 7 November 2012, is that the existing provision for bad debts is under stated by an amount of R94 758 592.

This unforeseen, unavoidable expenditure was not provided for in the 2011/12 approved budget, and therefore needs to be provided for in terms of an adjustment to the budget to avoid unauthorised expenditure. Section 29 of the MFMA allows for the Mayor to approve such expenditure, and it will be included in the agenda of the next Council meeting, scheduled for 14 December 2012.

The increase in the provision is not a physical outflow of cash. It will be funded from the reserves, which are cash backed. The level of reserves as at end of June 2012, amounted to R817 402 704, as supported by Annexure 3, the reconciliation of reserves as at 30 June 2012.

### **STAFF IMPLICATIONS**

There are no staff implications.

### **FINANCIAL IMPLICATIONS**

An increase in the Provision of Bad Debts for 2011/12 financial year in the amount of R94 758 592.

### **OTHER PARTIES CONSULTED**

Office of the Auditor General

### **CONCLUSION**

The approval of the adjustment to the 2011/12 budget to cover the additional provision for bad debts will avoid unauthorized expenditure.

**ANNEXURES**

Annexure 1: Communication of Audit Finding Number 24

Annexure 2: Extract of the MFMA

Annexure 3: Reconciliation of reserves and commitments back by cash/investments

Annexure 4: Approval Memo

**RECOMMENDATIONS**

- That Council ratifies the approval of the Executive Mayor of the adjustment to the provision of bad debts in the amount of R94 758 592, to be funded from reserves.



Annexure 1

AUDITOR-GENERAL  
SOUTH AFRICA

The Chief Financial Officer  
Amathole District Municipality  
PO Box 320  
East London  
5200

7 November 2012

Reference: Communication No. 24 of 2012

Dear Mr Zote

**Communication of audit findings from the regularity audit of the Amathole District Municipality for the year ended 2012-06-30**

1. In performing the audit of receivables, accumulated surplus and bad debts, the matters detailed in the annexure came to our attention.

**Required**

2. You are requested to indicate your agreement with the facts stated in these findings. Should you disagree with the findings, provide documentary evidence to the contrary for each finding.
3. All comments/evidence should be provided to us within 3 working days of the date of this letter.

Yours sincerely

Michelle Wait  
Audit Manager  
ELO8

Enquiries: Michelle Wait  
Telephone: (043) 709 7200  
Fax: (043) 709 7300  
Email: [michellep@agsa.co.za](mailto:michellep@agsa.co.za)

**Acknowledgement of receipt by management:**

Received by \_\_\_\_\_

Date \_\_\_\_\_

Annexure 2

## Receivables

### 1. Provision for bad debt: understatement

#### Audit finding

In terms of s62(1)(c)(i) of the Municipal Finance Management Act No 56 of 2003, the accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure -

- (c) that the municipality has and maintains effective, efficient and transparent systems -
- (i) of financial and risk management and internal control;

During the audit of the provision for doubtful debts the following large difference between the amount disclosed per financial statements and the auditors reasonability test was noted:

The reasonability test was performed by tracking age analysis balances at year end for current, 30, 60, 90, 120 and 150 days after 30 June 2012 and comparing estimated receipts to debtors balances tested in order to obtain a recoverability ratio.

The recoverability ratio for the tested year end balances up to 150 days equated to 20.22%, leaving a ratio of 79.78% as possibly unrecoverable.

The amount recalculated as the estimated provision for doubtful debts was calculated as follows:

Debtors per Age Analysis x 79.78% = Impairment Expense (R166 371 326.15)

Amount recognised by ADM: R87 495 634 (less the R15 882 899.55 proposed journal reversal)

Difference: R94 758 591.70 understatement in provision for bad debt.

Management failed to review and compare the final provision amount included in the financial statements and reasonability test to ensure that the provision appears reasonable.

Based on the reasonability test the provision for doubtful debts may be understated resulting in receivables being overstated in the financial statements.

#### Internal control deficiency

Financial and performance management: Implement proper record keeping in a timely manner to ensure that complete, relevant and accurate information is accessible and available to support financial and performance reporting.

#### Recommendation

Management should review and compare the final provision amount included in the financial statements and reasonability test to ensure that the provision appears reasonable

#### Management response

- Journal will be processed debiting bad debt expense and crediting provision for bad debts accounts for R94 758 591.70.

Name: Nkosinathi Soga

Position: Senior Manager – Revenue

Date: 12/11/2012

## Annexure 2

**28. Municipal adjustments budgets.**—(1) A municipality may revise an approved annual budget through an adjustments budget.

(2) An adjustments budget—

- (a) must adjust the revenue and expenditure estimates downwards if there is material under-collection of revenue during the current year;
- (b) may appropriate additional revenues that have become available over and above those anticipated in the annual budget, but only to revise or accelerate spending programmes already budgeted for;
- (c) may, within a prescribed framework, authorise unforeseeable and unavoidable expenditure recommended by the mayor of the municipality;
- (d) may authorise the utilisation of projected savings in one vote towards spending under another vote;
- (e) may authorise the spending of funds that were unspent at the end of the past financial year where the under-spending could not reasonably have been foreseen at the time to include projected roll-overs when the annual budget for the current year was approved by the council;
- (f) may correct any errors in the annual budget; and
- (g)

Annexure 2

- (a) must be in accordance with any framework that may be prescribed;
- (b) may not exceed a prescribed percentage of the approved annual budget;
- (c) must be reported by the mayor to the municipal council at its next meeting; and
- (d) must be appropriated in an adjustments budget.

(3) If such adjustments budget is not passed within 60 days after the expenditure was incurred, the expenditure is unauthorised and section 32 applies.

**31. Shifting of funds between multi-year appropriations.**—When funds for a capital programme are appropriated in terms of section 16(3) for more than one financial year, expenditure for that programme during a financial year may exceed the amount of that year's appropriation for that programme, provided that—

- (a) the increase does not exceed 20 per cent of that year's appropriation for the programme;
- (b) the increase is funded within the following year's appropriation for that programme;
- (c) the municipal manager certifies that—
  - (i) actual revenue for the financial year is expected to exceed budgeted revenue; and
  - (ii) sufficient funds are available for the increase without incurring further borrowing beyond the annual budget limit;
- (d) prior written approval is obtained from the mayor for the increase; and
- (e) the documents referred to in paragraphs (c) and (d) are submitted to the relevant provincial treasury and the Auditor-General.

**32. Unauthorised, irregular or fruitless and wasteful expenditure.**—(1) Without limiting liability in terms of the common law or other legislation—

- (a) a political office-bearer of a municipality is liable for unauthorised expenditure if that office-bearer knowingly or after having been advised by the accounting officer of the municipality that the expenditure is likely to result in unauthorised expenditure, instructed an official of the municipality to incur the expenditure;
- (b) the accounting officer is liable for unauthorised expenditure deliberately or negligently incurred by the accounting officer, subject to subsection (3);
- (c) any political office-bearer or official of a municipality who deliberately or negligently committed, made or authorised an irregular expenditure, is liable for that expenditure; or



Annexure 3



Reconciliation of reserves and commitments backed by cash/reserve/commitments		Ref
Cash resources		
Investments	471 109 426	1
Cash at bank (per cashbook)	346 293 276	2
	<b>817 402 704</b>	
Commitments		
Unspent conditional grants	-169 834 335	3
Internally funded projects	-82 353 736	4
Trade and other payables	-174 441 256	5
Post employment benefit provision	-127 033 659	6
Finance leases	-770 270	7
Operating lease liability	-471 582	8
Consumer deposits	-1 772 978	9
Leave provision	-13 167 467	10
Other provisions	-1 044 604	11
Funding for deficit budget - 2011/12	-6 216 242	12
	<b>-577 104 080</b>	
Net cash	<b>240 298 624</b>	
Minimum levels - 3 months working capital	222 963 735	
Cash for discretionary allocation (over utilisation)	17 334 889	
Comments		

Annexure 4


**AMATHOLE DISTRICT MUNICIPALITY**

40 Cambridge Street • East London • South Africa • 5201

PO Box 320 • East London • 5200

Tel: +27 (0) 43 701 4000 • fax: +27 (0) 43 742 0337

**MEMORANDUM**

TO:	The Executive Mayor	FROM:	Chief Financial Officer
CC:			
SUBJECT	BUDGET ADJUSTMENT FOR UNFORESEEN AND UNAVOIDABLE EXPENDITURE 2011/2012		
REF:	1/1/R	DATE:	22 November 2012

**PURPOSE**

To seek the Executive Mayor's approval for:

- An adjustment to the 2011/12 budget, to increase the provision for bad debts by R94 758 592.

**AUTHORITY**

The Municipal Finance Management Act 56 of 2003 (MFMA).

**LEGAL/STATUTORY REQUIREMENTS**

Section 29 of the Municipal Finance Management Act dealing with unforeseen and unavoidable expenditure stipulates:

- (1) *The mayor of a municipality may in emergency or other exceptional circumstances authorize unforeseeable and unavoidable expenditure for which no provision was made in an approved budget.*
- (2) *Any such expenditure –*
  - a) *Must be in accordance with a framework that may be prescribed;*
  - b) *May not exceed a prescribed percentage of the approved annual budget;*
  - c) *Must be reported by the mayor to the municipal council at its next meeting; and*
  - d) *Must be appropriated in an adjustments budget.*

Annexure 4

*(3) If such adjustments budget is not passed within 60 days after the expenditure was incurred, the expenditure is unauthorized and section 32 applies.*

#### **REASONING/BACKGROUND**

During the audit of the 2011/12 annual financial statements, the Auditor General did a reasonability test on the existing Provision for Bad Debts, resulting in an adjustment to this provision being necessary.

#### **Audit Outcome**

The outcome as per Communication of Audit Finding Number 24, Item 2, dated 7 November 2012, is that the existing provision for bad debts is under stated by an amount of R94 758 592.

This unforeseen, unavoidable expenditure was not provided for in the 2011/12 approved budget, and therefore needs to be provided for in terms of an adjustment to the budget to avoid unauthorised expenditure. Section 29 of the MFMA allows for the Mayor to approve such expenditure, and it will be included in the agenda of the next Council meeting, scheduled for 14 December 2012.

The increase in the provision is not a physical outflow of cash. It will be funded from the reserves, which are cash backed. The level of reserves as at end of June 2012, amounted to R817 402 704, as supported by Annexure 3, the reconciliation of reserves as at 30 June 2012.

#### **STAFF IMPLICATIONS**

There are no staff implications.

#### **FINANCIAL IMPLICATIONS**

An increase in the Provision of Bad Debts for 2011/12 financial year in the amount of R94 758 592.

Annexure 4

**CONCLUSION**

The approval of the adjustment to the 2011/12 budget to cover the additional provision for bad debts will avoid unauthorized expenditure.

**RECOMMENDATIONS**

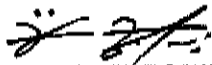
- It is recommended that the Executive Mayor approves the adjustment to the provision of bad debts in the amount of R94 758 592, to be funded from reserves
- This matter be reported to Council on 14 December 2012

**ANNEXURES**

Annexure 1: Communication of Audit Finding Number 24

Annexure 2: Extract of the MFMA

Annexure 3: Reconciliation of reserves and commitments back by cash/investments



**YIMILE ZOTE:**  
**CHIEF FINANCIAL OFFICER**

Annexure 4

COMMENTS BY MUNICIPAL MANAGER

---



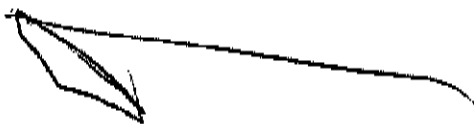
---



---



---



CHRIS MAGWANGQANA  
MUNICIPAL MANAGER



RECOMMENDED / NOT RECOMMENDED

COMMENTS BY THE MAYOR

---



---



---



---

NOMASIKIZI KONZA  
EXECUTIVE MAYOR



APPROVED / NOT APPROVED

ANNEXURE L

AUDITOR-GENERAL  
SOUTH AFRICA

The Chief Financial Officer  
Amathole District Municipality  
PO Box 320  
East London  
5200

7 November 2012

Reference: Communication No. 24 of 2012

Dear Mr Zote

**Communication of audit findings from the regularity audit of the Amathole District Municipality for the year ended 2012-06-30**

1. In performing the audit of receivables, accumulated surplus and bad debts, the matters detailed in the annexure came to our attention.

**Required**

2. You are requested to indicate your agreement with the facts stated in these findings. Should you disagree with the findings, provide documentary evidence to the contrary for each finding.
3. All comments/evidence should be provided to us within 3 working days of the date of this letter.

Yours sincerely

Michelle Wait  
Audit Manager  
ELOB

Enquiries: Michelle Wait  
Telephone: (043) 709 7200  
Fax: (043) 709 7300  
Email: [michellep@agsa.co.za](mailto:michellep@agsa.co.za)

**Acknowledgement of receipt by management:**

Received by \_\_\_\_\_

Date \_\_\_\_\_

*Auditing to build public confidence*

**Auditor-General** Republic of South Africa

Annexure 4

**Receivables**

**2. Provision for bad debt: understatement**

**Audit finding**

In terms of s62(1)(c)(i) of the Municipal Finance Management Act No 56 of 2003, the accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure -  
(c) that the municipality has and maintains effective, efficient and transparent systems -  
(i) of financial and risk management and internal control;

During the audit of the provision for doubtful debts the following large difference between the amount disclosed per financial statements and the auditors reasonability test was noted:

The reasonability test was performed by tracking age analysis balances at year end for current, 30, 60, 90, 120 and 150 days after 30 June 2012 and comparing estimated receipts to debtors balances tested in order to obtain a recoverability ratio.  
The recoverability ratio for the tested year end balances up to 150 days equated to 20.22%, leaving a ratio of 79.78% as possibly unrecoverable.  
The amount recalculated as the estimated provision for doubtful debts was calculated as follows:

Debtors per Age Analysis x 79.78% = Impairment Expense (R166 371 326.15)

Amount recognised by ADM: R87 495 634 (less the R15 882 899.55 proposed journal reversal)

Difference: R94 758 591.70 understatement in provision for bad debt.

Management failed to review and compare the final provision amount included in the financial statements and reasonability test to ensure that the provision appears reasonable.

Based on the reasonability test the provision for doubtful debts may be understated resulting in receivables being overstated in the financial statements.

**Internal control deficiency**

Financial and performance management: Implement proper record keeping in a timely manner to ensure that complete, relevant and accurate information is accessible and available to support financial and performance reporting.

**Recommendation**

Management should review and compare the final provision amount included in the financial statements and reasonability test to ensure that the provision appears reasonable

**Management response**

**Auditor's conclusion**

Chamae  
Dr expense - bad debts  
Cr Provision for bad debts



## ANNEXURE 4

**28. Municipal adjustments budgets.**—(1) A municipality may revise an approved annual budget through an adjustments budget.

(2) An adjustments budget—

- (a) must adjust the revenue and expenditure estimates downwards if there is material under-collection of revenue during the current year;
- (b) may appropriate additional revenues that have become available over and above those anticipated in the annual budget, but only to revise or accelerate spending programmes already budgeted for;
- (c) may, within a prescribed framework, authorise unforeseeable and unavoidable expenditure recommended by the mayor of the municipality;
- (d) may authorise the utilisation of projected savings in one vote towards spending under another vote;
- (e) may authorise the spending of funds that were unspent at the end of the past financial year where the under-spending could not reasonably have been foreseen at the time to include projected roll-overs when the annual budget for the current year was approved by the council;
- (f) may correct any errors in the annual budget; and
- (g) may provide for any other expenditure within a prescribed framework.

(3) An adjustments budget must be in a prescribed form.

(4) Only the mayor may table an adjustments budget in the municipal council, but an adjustments budget in terms of subsection (2) (b) to (g) may only be tabled within any prescribed limitations as to timing or frequency.

(5) When an adjustments budget is tabled, it must be accompanied by—

- (a) an explanation how the adjustments budget affects the annual budget;
- (b) a motivation of any material changes to the annual budget;
- (c) an explanation of the impact of any increased spending on the annual budget and the annual budgets for the next two financial years; and
- (d) any other supporting documentation that may be prescribed.

(6) Municipal tax and tariffs may not be increased during a financial year.

[Sub-s. (6) substituted by s. 13 of Act No. 12 of 2007.]

Wording of Sections

(7) Sections 22 (b), 23 (3) and 24 (3) apply in respect of an adjustments budget, and in such application a reference in those sections to an annual budget must be read as a reference to an adjustments budget.

**29. Unforeseen and unavoidable expenditure.**—(1) The mayor of a municipality may in emergency or other exceptional circumstances authorise unforeseeable and unavoidable expenditure for which no provision was made in an approved budget.

(2) Any such expenditure—



Annexure 4

- (a) must be in accordance with any framework that may be prescribed;
- (b) may not exceed a prescribed percentage of the approved annual budget;
- (c) must be reported by the mayor to the municipal council at its next meeting; and
- (d) must be appropriated in an adjustments budget.

(3) If such adjustments budget is not passed within 60 days after the expenditure was incurred, the expenditure is unauthorised and section 32 applies.

**31. Shifting of funds between multi-year appropriations.**—When funds for a capital programme are appropriated in terms of section 16(3) for more than one financial year, expenditure for that programme during a financial year may exceed the amount of that year's appropriation for that programme, provided that—

- (a) the increase does not exceed 20 per cent of that year's appropriation for the programme;
- (b) the increase is funded within the following year's appropriation for that programme;
- (c) the municipal manager certifies that—
  - (i) actual revenue for the financial year is expected to exceed budgeted revenue; and
  - (ii) sufficient funds are available for the increase without incurring further borrowing beyond the annual budget limit;
- (d) prior written approval is obtained from the mayor for the increase; and
- (e) the documents referred to in paragraphs (c) and (d) are submitted to the relevant provincial treasury and the Auditor-General.

**32. Unauthorised, irregular or fruitless and wasteful expenditure.**—(1) Without limiting liability in terms of the common law or other legislation—

- (a) a political office-bearer of a municipality is liable for unauthorised expenditure if that office-bearer knowingly or after having been advised by the accounting officer of the municipality that the expenditure is likely to result in unauthorised expenditure, instructed an official of the municipality to incur the expenditure;
- (b) the accounting officer is liable for unauthorised expenditure deliberately or negligently incurred by the accounting officer, subject to subsection (3);
- (c) any political office-bearer or official of a municipality who deliberately or negligently committed, made or authorised an irregular expenditure, is liable for that expenditure; or



# AMATHOLE DISTRICT MUNICIPALITY

Commitments for the 12 months ending 30-Jun-2012

ANNEXURE E

Receipts	Net	
Balance forward		
Investments	1	471 109 420
Cost of bank (per cashbook)	2	344 293 276
		437 402 704
<b>Commitments</b>		
Unspent conditional grants	3	-1 69 834 335
Internally funded projects	4	-62 353 736
Trade and other payables	5	-174 441 254
Post employment benefit provision	4	-187 033 609
Finance leases	7	-770 270
Operating leases liability	8	-471 582
Contractor deposits	9	-1 772 978
Leave provision	10	-13 167 467
Other provisions	11	-1 044 804
Funding for deficit budget - 2011/12	12	-6 216 242
		-577 104 000
Net cash		240 298 634
Minimum level - 3 months working capital		222 945 335
Cost for discretionary allocation/over-allocation		-17 332 889

Comments