



Preparation of Annual Financial Statements based on the Exemption Gazette 30013

The phase in period for application of accounting standards to the annual financial statements has been extended by notice in the Government Gazette No. 30013, dated 29 June 2007. A copy available on the MFMA website: www.treasury.gov.za/mfma and is located under Regulations and Gazettes.

This circular provides guidance on the implementation and interpretation of the Gazette and the preparation and submission of annual financial statements as required by the Municipal Finance Management Act (MFMA), No. 56 of 2003.

The circular should be read in conjunction with MFMA Circular 18 dated 23 June 2005 and MFMA Circular 36 dated 11 July 2006. Certain guiding paragraphs included in Circulars 18 and 36 have been revised due to the exemptions and deviations emanating from Gazette 30013. The following paragraphs are affected:

MFMA Circular 18

- Mandatory & encouraged accounting policies (page 3)
- Implementation by capacity (page 4)
- Format of the annual financial statements (page 4)
- Consistency in application (page 5)

MFMA Circular 36

- Specimen municipal annual financial statements (page 2)
- Consolidated specimen financial statements (page 2)
- Applicable dates for preparation for consolidated annual financial statements (page 3)
- Applicable dates for compliance with GRAP (page 3)

Exemptions granted in the Gazette

The ethos of encouraging municipalities to further the financial management and accounting reforms beyond the GAMAP requirements, as described in Circular 18, is supported. The detail behind the interpretation of the accounting policies, disclosure requirements, formats and any changes to the application of accounting standards, is available on the website: <http://oag.treasury.gov.za> located under *Annual Financial Statements - Local Government: Municipalities and Municipal Entities – Application of Accounting Standards*.

The original notice providing specific transitional and phase-in approaches to sections 122(2) and 122(3) for the implementation of the MFMA has been extended.

This means that each municipality or municipal entity has additional time to fully comply with sections 122(2) and 122(3) in the preparation of the annual financial statements.

The new compliance dates apply to the financial years tabled below.

Municipal Capacity	Preparation of consolidated annual financial statements section 122(2) <i>Applies to:</i>	Preparation of financial statements in terms of generally recognised accounting practice (GRAP) section 122(3) <i>Applies to:</i>
High Capacity Municipalities	2008/09 financial year	2008/09 financial year
Medium Capacity Municipalities	2008/09 financial year	2008/09 financial year
Low Capacity Municipalities	2009/10 financial year	2009/10 financial year
Municipal Entities	No exemption	2009/10 financial year

Impact of exemptions on the preparation and submission of annual financial statements

Where a municipality fully complies with the exemption notice, the municipality need not submit consolidated financial statements to the Auditor-General as required in terms of section 126(1)(b) of the MFMA. In this case the requirements in terms of the MFMA to submit the annual report of the municipality to oversight bodies must include the annual financial statements of all its entities, associates and joint ventures as annexure forming a substitute to the consolidated annual financial statements.

Taking advantage of this exemption means that a municipality need not fully comply with GAMAP 6, 7 and 8. However, certain paragraphs in these standards have not been exempted and must be applied. These paragraphs are:

- GAMAP 6 - paragraphs 38, 40 and 43(c)
- GAMAP 7 - paragraphs 18, 31(b) and 31(c)
- GAMAP 8 - paragraph 40 and 44

When applying the equity method in this context a municipality must refer to GAMAP 7 paragraphs 21 – 28. It should be noted that GAMAP 8, paragraph 40, does not indicate a preference for how to account for an interest in a joint venture. The options available to municipalities applying paragraph 40 of GAMAP 8 are costs or as an investment in terms of IAS 39 (AC 133).

If a municipality does not take advantage of this exemption and chooses to prepare and publish consolidated annual financial statements for the 2006/07 or 2007/08 financial years it may do so provided that the deviation conditions in the gazette have been met. In such instances all provisions within GAMAP 6, 7 and 8 apply.

High capacity municipalities

High capacity municipalities are expected to either:

- (a) take advantage of the total exemptions granted in the annexure to Gazette 30013 (provided that all conditions have been met); **or**
- (b) fully comply with the 2005/06 reporting requirements (i.e. use none of the available exemptions and apply all the effective GRAP, GAMAP and SA GAAP standards including any interpretation and relevant circulars issued by the Accounting Practices Board and SAICA);

Option (b) will be regarded as a deviation and must be dealt with as outlined in sub-regulation 3(a) and 3(b) of the Gazette (also refer to the discussion on the deviation process below).

In instances where municipalities deviate in a partial manner and are implementing the standards that are being exempted, the municipality may request approval from the relevant treasury to continue with implementation of the selected standards. Any approval for deviation will be co-signed by the National Treasury. It is important to mention that in exercising this option it may result in a different type of audit opinion. A municipality should therefore ensure that the consequences of an opinion, other than fair presentation, on the users to the financial statements are considered prior to application for deviation.

If any of the exemptions in the Annexure to the Gazette are not applicable due to the municipality or entity not having any transactions affected by the standards, then a deviation request for that standard is not necessary. For example, if a municipality is not involved in any contracting activities that fall within the scope of IAS 11 (AC 109), the municipality will not use the exemption and will not need to apply for any deviation.

Medium and low capacity municipalities

Medium and low capacity municipalities are expected to present their annual financial statements in the same format and using the same standards as produced during the 2005/06 financial year.

The exemption Gazette provides for a deviation from the 2005/06 standards. To the extent that municipalities have progressed in implementing the standards as originally envisaged, the municipality may deviate fully or partially from implementing the selected standards. The partial deviation should be limited to standards as contained in the annexure to the Gazette.

The municipality may request approval from the relevant treasury to continue with implementation of the selected standards. Any approval for deviation will be co-signed by the National Treasury. It is important to mention that in exercising this option it may result in a different type of audit opinion. A municipality should therefore ensure that the consequences of an opinion, other than fair presentation, on the users to the financial statements are considered prior to application for deviation.

If a municipality had adopted the GRAP/GAMAP/SA GAAP standards in preparation of its 2005/06 financial statements, this will not be viewed as a deviation from the exemption if the municipality continues to apply the same standards for the 2006/07 financial year and for the future financial years. Municipalities are encouraged to continue with the application of these accounting standards and should not regress to the IFMO formats.

Municipal entities

Municipal entities are required to continue applying the reporting framework used for the preparation of the 2005/06 annual financial statements but will have to comply with any new GRAP standards prescribed in terms of section 91 of the PFMA.

There are no new GRAP standards applicable for the 2006/07 and 2007/08 financial years. Notice will be provided should any new standards be required for implementation.

Early implementation of any GRAP standard that has not been prescribed in a government gazette is seen as a deviation from the exemption and must be dealt with accordingly.

Process for applying for deviation and submission of implementation plans

The process to be adopted for application by municipalities and entities for a deviation is as follows.

The contents of the application for deviation must contain:

1. The specific paragraph of a standard;
2. Clearly state whether it is partial or a full deviation being requested;
3. Briefly provide a motivation for the deviation, including the standards used for 2005/06 financial year;
4. The application to be signed by the Chief Finance Officer; and
5. The date that the deviation request and reasons for deviation will be tabled in Council

A municipality or municipal entity must apply for any deviations by 31 July 2007 for the 2006/07 financial year in order to meet the strict timelines for confirmation in writing of approvals. This will include engagements with the provincial treasury to support the application. The deadline for finalising the request which includes the co-signature of the National Treasury is **15 August 2007**. Kindly ensure that this is adhered to.

For further years, it is also important to note that early submission of requests for deviations to facilitate audit planning is necessary. This will assist the auditors in planning for the audit of the municipality or municipal entity.

Each municipality or municipal entity that has deviated from the exemptions or that has applied the exemptions must prepare a detailed implementation plan setting out its intended and actual progress towards complying with the exemptions or deviations. You are alerted to the reporting periods, namely 30 October 2007 and 31 March 2008 for submission of progress reports on implementation. The format of the implementation plan is annexed hereto as annexure A (for high capacity municipalities) and annexure B (medium and low capacity municipalities).

Please ensure that the request is emailed to lindy.bodewig@treasury.gov.za or faxed to 012 315 5568.

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