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| Description: Letter Head |
| MUNICIPAL REGULATIONS ON A STANDARD CHART OF ACCOUNTS  *[SCOA for MUNICIPALITIES]* |
| Project Detail Document |
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|  |
| November 2017 (Version 6.1) |

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# PROJECT DETAIL DOCUMENT – PROJECT EXECUTIVE SUMMARY

## Project Overview

1. This section provides a summary of the research, development and consultation phase leading to the compilation of a chart of accounts for local government based on the process outline below. This process directly informed the drafting of the Municipal Regulations on a Standard Chart of Accounts, 2014 (mSCOA).
2. The draft mSCOA Regulation was published for public comments by the Minister of Finance, on 02 September 2014. Subsequent to this a formal consultation and awareness campaign was facilitated by the National Treasury. Comments received following this process informed the finalisation of Version 5 of the mSCOA Tables, the project detail document and comments register.
3. The detailed project document includes a section on each segment including a discussion on the preliminary observations from the initial research, design principles defined for the development of the segments and defined detail accounts for consultation with diverse stakeholders.

## Background to the mSCOA Project Initiative

### National and Provincial

1. In 1999, the National Treasury embarked on a budget reform programme for national and provincial government departments, with the objectives of improving accountability and modernising the accounts of government by aligning reporting with international leading practices. The ultimate aim of this reform process was to provide better quality information to legislatures to assist in the policy-making process as a vital input into expanding service delivery, and to reinforce parliament’s oversight role.
2. An important component of the budget reform programme was initiated in 1998 when National Treasury started a process of reclassifying the existing expenditure items of national and provincial government in line with the requirements of the Government Finance Statistics (GFS) developed by the International Monetary Fund (IMF). This was to ensure compliance with the requirements of the Special Data Dissemination Standard (SDDS), a minimum reporting standard set by the IMF, to which South Africa is a signatory.
3. During this process many inconsistencies in the application of existing classification standards were identified. This was mainly due to the classification rules being inconsistently applied and limited control over their application. Furthermore, departments were allowed to create their own accounting codes on the systems, leading to a vast number of codes and hundreds of duplications.
4. While the project was initiated to develop a new budget format, it soon became clear that the new reporting format would only be effective with an appropriately amended Chart of Accounts (CoA). While the budget formats outline the broad categories of planned expenditure, the chart of accounts is used to capture the detailed spending items when the budget gets implemented. Thus any change to the budget format must be supported by a corresponding change to the chart. The scope of the project was therefore expanded to include the development and implementation of a new standard chart of accounts.
5. Since 2004, the Economic Reporting Format (ERF) and SCOA are fully operational and used by all national and provincial departments. Overall, the implementation process has proceeded smoothly without any major hurdles or impediments. The successful implementation of SCOA contributed to growing positive public perception, locally and internationally, and strengthened public sector accountability and reporting.

### Local Government

1. Although the National Treasury has made significant progress in so far as the collection of municipal financial data is concerned, there still exists enormous challenges before national government will be in position to claim that the quality of municipal information is reliable, credible and relevant.
2. These challenges can be summarised as follows:
   * + - At a municipal level, National Treasury does not have access to the operating and financial systems on the same basis as National Treasury officials have access to the BAS system at a national and provincial level. As a result, National Treasury is unable to technically verify municipal information as it relates to credibility, reliability and accuracy. Consequently, National Treasury has obliged the municipal accounting officer and chief financial officer to sign-off the municipality’s information, prior to publication of any municipal financial information. Furthermore, the One Public Service debate could provide National Treasury with a unique opportunity to migrate smaller municipalities to BAS or a suitable uniform system;
       - The National Treasury does not have the equivalent of the mSCOA for local government; consequently, the classification of municipal information at a transaction level across 278 municipalities is not necessarily consistent. This challenge will be partly addressed as the accounting standards and reforms unfold and once the National Treasury prescribed an mSCOA for local government;
       - Multi-year budgeting at a municipal level is still a relatively new concept. The ability to plan and articulate communities’ needs and policy intent into plans and budgets are particularly weak. Most municipal budgets still focus on the first year of the medium-term revenue and expenditure framework (MTREF) period instead of a multi-year horizon;
       - The inability to consistently use information for decision-making purposes is one of the prevalent challenges. Owing to the complexity, this objective will take time to perfectly implement and master by all 278 municipalities; and
       - Finally, the actual budget documents produced by municipalities should correspond with the electronic version posted on a municipality’s website. The numbers contained in these documents should further correspond and balance with the information submitted as part of the standard budget return forms submitted to the National Treasury. In some cases, several different sets of numbers are received, and this obviously has an impact on the ability of the National Treasury to streamline accurate and credible publications.
3. Substantial and continuous changes in the structure of municipalities compromise the comparison of performance over time.
4. The National Treasury ultimately has the responsibility for compiling national whole-of-government accounts, including consolidated local government information for national policy and other purposes. This information is obtained from all municipalities, each of which operates according to their own organisational framework. It is necessary for National Treasury to specify a national standard for the collection of local government budget and financial information. Municipalities need to appreciate the benefit of whole of government data collection as it informs national reporting, benchmarking and fosters an improved understanding of the contribution of the local government sphere. This will be one of the key benefits of getting municipalities to budget and report according to the Government Finance Statistics (GFS) categories, since these categories transcend any structural changes in a dynamic local government environment.
5. The Municipal Budget and Reporting Regulations, 2009 (MBRR) became effective on 1 July 2009. The main objective of the MBRR is to formalise norms and standards which are envisaged to improve the credibility, sustainability, transparency, accuracy and reliability of municipal budgets.
6. The budget formats prescribed in the Municipal Budget and Reporting Regulations, 2009 go a long way in identifying the categories of municipal information required in developing a municipality’s budget. The next step is to ensure that the detailed information captured in the implementation of the budget is properly and credibly aligned. Although Local Government has its own peculiarities, the success achieved at the National and Provincial level from implementing the SCOA could be equally beneficial for Local Government in improving data quality, achieving a greater level of standardisation and uniform data sets. These are critical for ‘whole-of-government’ reporting.

### Legislative Mandate

1. Section 216 of the Constitution of the Republic of South Africa (Act 108 of 1996, substituted by section 1(1) of Act 5 of 2005) deals with treasury control and determines that national legislation must establish a National Treasury and prescribe measures to ensure both transparency and expenditure control in each sphere of government, by introducing generally recognised accounting practices, uniform expenditure classifications and uniform treasury norms and standards.
2. Section 168(1) of the Municipal Finance Management Act, 2003 (MFMA), determines that the Minister of Finance, acting with the concurrence of the Cabinet member responsible for local government, may make regulations or guidelines applicable to municipalities and municipal entities, regarding any matter that may be prescribed in terms of the Act.

### Overall Objective

1. The primary objective is to achieve an acceptable level of uniformity and quality from the collection of Local Government (Municipality and Municipal Entity) data. This will require a classification framework specific to Local Government.

### Specific Objective(s)

1. To achieve this main objective will require a classification framework specific to Local Government incorporating all transaction types, appropriation of funds, spending on service delivery, capital and operating spending, policy outcomes and legislative reporting requirements to the maximum extent possible.
2. The development of this framework must give recognition to:
   * + - international standards, guidance and best practices;
       - labels and accounts defined to have readily available the information needed for local government budgeting (annual budget, adjustment budget and the service delivery- and budget implementation plan (SDBIP)) and reporting (monthly, mid-year performance assessment and annual financial statements);
       - general alignment of financial reporting formats and the annual financial statements to key budget format reforms;
       - alignment of budget and reporting formats with the Standards of GRAP and principles within the provisions of the transitional arrangements applicable to the different categories of municipality, especially recognising that local government uniquely operates in an accrual accounting and budgeting environment;
       - consistent use of terminology across all municipalities by defining all accounts and labels in simple terms to support appropriate classification of transactions throughout all municipalities;
       - standardisation across local government by clearly outlining the information requirements which will enable municipalities and their information system suppliers to develop software and report writing formats that are automated and compliant to reporting requirements governing Local Government;
       - reporting on the “whole-of-local government”, and thus contribute to “whole-of-government” monitoring and evaluation;
       - finding a solution for the separation of the general government sector, which “consists of entities that fulfil the functions of government as their primary activity” and business activities that sell services at market prices within a local government environment, especially where the management of these functions tend to be closely interrelated with general government activities;
       - minimising the cost of compliance and information gathering; and
       - the classification framework must be kept simple and avoid unnecessary complexities to the maximum extent possible; this while ensuring the reform intent is maintained.
3. The mSCOA will be applicable to all Municipalities, Municipal Entities and “Utilities” clearly indicating their applicability and relevance to a specific environment to assist customisation.
4. The improved quality of data will enhance the budget, financial reporting and other decision-making processes impacting on local government. The classification framework was formalised by issuing the mSCOA Regulation, 2014 in terms of the Municipal Finance Management Act, 2003 (MFMA).

## Challenges and Risks

1. Excluded from the scope of this project is system development and implementation at a user level. The Project: Financial Systems and Business Processes specifically focuses on the implementation of mSCOA through a system solution. Representatives from the various categories of municipalities were engaged at specific points in the project life cycle. Prior to implementation, the framework was piloted at a selection of cross-cutting municipalities representing all systems (used in local government as at project start date) and categories of municipalities. Workshops were held to share information with users to bring across a proper understanding of the framework.
2. Implementing the mSCOA might require “system re-implementation” for some users for whom conversion might not be easy and could become costly. The best possible conversion solutions were explored by National Treasury in consultation with the system vendors. Systems currently in use by some municipalities might not be able to accommodate for mSCOA segments nor will it be cost effective to upgrade and reconfigure. Please refer in this regard the subsequent MFMA Circular 80, Municipal SCOA Circulars No. 5 and 6 that were issued in this regard and the RT25-2016 transversal contract.
3. It is recognised that the implementation of an mSCOA in municipalities may be subject to resource and other constraints such as systems, timing, capacity and skills. Obvious systems challenges requiring further consideration include:
   * + - The length of characters of the recommended standard chart may be beyond the technical capabilities of existing municipal data systems, for example, the standard chart may require a 13 segments containing 3 digits each, alpha or numeric code, whereas an existing system might be limited to a lesser number of characters.
       - The multi-dimensional chart consisting of various segments might not be easy to accommodate by the systems presently utilised by the municipality.
       - The timing of mSCOA implementation will be critical. Whilst a simultaneous change to all systems at the beginning of a financial year may be advocated by many, from a financial reporting and control perspective, the municipal budget cycle will commence many months before the start of the financial year and, depending on the municipality, may require systematic support to its development.
4. Therefore, because of these constraints, it is intended to provide a standard guidance framework to alleviate the wasteful burden of all municipalities having to discover these issues and challenges individually.
5. Critical to the feasibility of the project is aligning the classification, terminology and principles between the SCOA for Departments, Annual Financial Statement Template and Budget Reform Tables (Documents and Supporting Documents)
6. The “entity” classification used frequently in the SCOA for Departments might not be information currently retained in the financial systems of the Municipality.
7. Standardisation of the “Property, Plant and Equipment” detail specific to the Item Segment might be extremely costly and an extent of flexibility may need to be provided over a transitional period.
8. The reporting framework comprises the Standards of GRAP, Interpretations of the Standards of GRAP, guidelines and directives issued by the Accounting Standards Board (ASB) and standards and pronouncements of other standard setters that should be applied when entities prepare and present their financial statements in accordance with Standards of GRAP, referred to as the GRAP Reporting Framework in Directive 5 issued by the ASB.
9. The extent to which transitional arrangements and non-compliance related requirements will need to be provided for will be determined during the workshops to be held with interested parties during the duration of the project development phase.
10. Excluded from the scope of the SCOA for Municipalities’ project is “non-financial information” such as that required for reporting on performance information. The mSCOA therefore only deals with “financial information”.

### Aligning the MSCOA for Municipalities to the SCOA for Departments

1. At the outset, the SCOA project team had committed that “as far as possible the SCOA for Municipalities will be aligned to the SCOA for Departments”. In the table below, the first column depicts the segments proposed following the initial research and the second column the segments used in the SCOA for Departments.
2. The proposal for Municipalities includes all segments except the Asset and Infrastructure Segments as used in the SCOA for Departments. The purpose of the Asset Segment is to identify asset classes and provide details of the economic classification. Conceptually the Asset Segment should not be necessary for Municipalities, as the capitalisation principles for recognising Property, Plant and Equipment should be well vested in the accounts set-up and supporting systems presently utilised by Municipalities. The Infrastructure Segment captures information relating to Infrastructure for reporting purposes. This detail is dealt with in the Project Segment as defined for municipalities.

## Process followed and Scope of Research Conducted to date

1. The initial research on the mSCOA project commenced in October 2009 marked by three continuous and integrated phases of development. These stages in the development process are described as distinct phases as outlined below.

1. Extensive stakeholder consultation was undertaken during the development process, as required in the MFMA. Furthermore, financial practitioners are supported by the National Treasury’s mSCOA Technical Committee and the respective provincial treasuries post implementation. Preliminary indications were that the stakeholder groups would include those tabulated below.

### Phase I

1. During Phase 1 initial research were conducted by collecting information from municipalities, the National Treasury legislation, regulations, circulars and guidance to formulate the legislative framework and extract compliance criteria for guiding the mSCOA development. Updating the legislative framework is an ongoing activity due to new guidance provided throughout the development period. As indicated in the overview this framework was updated and checked for compliance prior to concluding on Phase 3.
2. The departure point for defining a classification framework for municipalities was the SCOA for Departments. The Economic Reporting Format defined for national and provincial Departments set the principles for moving towards the whole of government budget and annual financial statement reporting in the future. Critical to this consideration is that the SCOA for Departments are based on the cash basis of accounting whilst the municipalities need to be based on accrual accounting principles and in compliance with the GRAP Reporting Framework.
3. Specific attention has been given to the accounts required to bridge the differences between the cash basis of accounting and accruals basis of accounting in compliance with the GRAP Reporting Framework. To the maximum extent possible, the high level classification defined by the Economic Reporting Framework was retained for consolidation purposes.
4. Given the impact of providing for the high level classification identified by the Economic Reporting Format, the impact of this approach had to be reflected in the annual financial statements, reporting tables and the budget reporting formats.
5. Five municipalities were engaged for their participation into this research. Financial practitioners from these municipalities then participated in consultations, workgroups and sharing of information. Selected municipalities included:
   * + - Steve Tshwete;
       - Knysna;
       - City of Cape Town;
       - Polokwane; and
       - eThekwini.
6. These municipalities provided their chart of accounts to assist in the development of Version 1 of mSCOA.
7. Account descriptions and definitions were only available from one of the above Municipalities – the City of Cape Town.
8. The research conducted in this Phase predominantly resulted in concluding on the segments collectively being the mSCOA for municipalities and the overall design principles to be adhered to throughout the detailed development of mSCOA.

### Phase II

1. Phase 2 commenced with meeting all external stakeholders. The table below shows a summary of all engagements with brief comments on the activity.

| **Stakeholder Group** | **Date** | **Description and Remarks** |
| --- | --- | --- |
| 1. **Provincial Treasuries**  * Eastern Cape * Free State * Gauteng * Kwazulu-Natal * Mpumalanga * North West * Northern Cape * Limpopo | 26 January 2011  07 March 2011 | The MFMA Coordinators and Head of Departments are responsible for the coordination and communication with the municipalities in the province.   * Information session held followed by a workshop on the detail accounts provided for in the chart of accounts. * Requested comments to be provided following the detail discussions. * Next interaction: to be scheduled post April 2012. |
| 1. **National Departments**  * Agriculture, Forestry and Fisheries * Cooperative Governance and Traditional Affairs * Energy * Home Affairs * Human Settlements * Mineral Resources * National Treasury * Public Works * Rural Development and Land Reform * Statistics South Africa * The Presidency * Tourism * Transport * Water Affairs | 14 February 2011 | The national departments having an interest in the chart of accounts are invited to the Introduction/ Information Session. Depending on their interest and information requirements it was foreseen that separate meetings with some or all of the departments might be needed due to the diverse nature of those invited.   * Not well attended and no feedback or response on call for forwarding information requirements from local government. * Communication received from STATS SA and discussion meeting held in March 2011. |
| 1. **Professional and Oversight Bodies**  * IMFO * AGSA * ASB * SAICA * SALGA | 15 February 2011 | A meeting will be held to inform these professional and oversight bodies on the project and project activities and seek their comments/ input on the standard chart of accounts. Depending on the involvement of the ‘stakeholder’ separate workshops may be required.   * Attended by SARB, AGSA, IMFO, ASB and CQS. |
| 1. **Regulators**  * NERSA * SARB | 23 February 2011 | “NERSA” and the “SARB” have unique and specific requirements that might pose challenges to accommodate in the standard chart of accounts. It was foreseen that intensive interactions to address the requirements of these stakeholders may be needed:   * Attended by NERSA. Awaiting information to be considered for chart and follow-up meeting confirmation. |
| 1. **Municipalities**  * Pilots * Wider Group | 28 February 2011  17 to 18 March 2011 | At the initial research phase five municipalities were selected for participation in the development of the standard chart of accounts. Broadly the selection consisted of metros, high/ medium capacity municipalities and a district municipality. Further to the selection participation was requested from some of the City of Johannesburg Agencies due to their expertise and experience in some specialised areas.  Phase 3 consultations involved the “wider group” of municipalities. The Provincial Treasuries assisted in engaging the municipalities within the provinces.   * The meeting was attended by the selected municipalities and Ekurhuleni volunteered. The City of Johannesburg was also invited for purposes of gleaning views from agencies during the design process. * Collecting updated chart of accounts information for mapping to Version 1 of the Chart of Accounts and resolving accounts where further clarity is required from municipalities. The outcome of the mapping process informed the update of the Chart of Accounts and revised Project Summary Document end of May 2011. * Further engagements were undertaken with the City of Cape specifically relating to their chart of accounts, structure of their integrated processing system and potential impact of MSCOA on the Metro. Interactive workshops were also conducted to clarify certain mismatches in relation to MSCOA. |
| 1. **System Vendors** |  | Introducing the chart of accounts to the system vendors was integrated with the Special Project on the Local Government System Specification.   * Phase I and II dedicated meetings were held with the system vendors at the inception of the project. |
| 1. **Internal Stakeholders – National Treasury** |  | Internal stakeholders were briefed on the development to date and the way forward to seek their comments on their field of interest. A comprehensive list of representatives was compiled. |
| 1. **Advisory and Consulting Firms** |  | Consulting firms functional within the municipal environment were involved in information session(s) to share the MSCOA development. |

1. The municipalities identified in Phase I as potential pilot sites have been visited to discuss the analysis of their account information and seeking further explanations and clarity in understanding the use of a specific account. The information gathered assisted in defining all the accounts provided for in mSCOA.
2. eThekweni Metropolitan Municipality declined the invitation to participate in the development of the mSCOA for municipalities.
3. Some additional municipalities expressed an interest to participate in the development and piloting process through their respective system vendors. Critical to the successful implementation were to ensure that ‘pilots’ are broadly representative of at least the System Vendors in the market. As a result a comparison of the municipal chart of accounts and version 1 of mSCOA for the following municipalities were done:
   * + - Overberg Municipality;
       - Saldanha Municipality;
       - Umahlatuze Municipality; and
       - eThekwini Metro Municipality.
4. Phase II of the mSCOA for municipalities represented completion of a more refined version of the chart of accounts after having undertaken specific consultation. Version II of the mSCOA was completed during the third quarter of 2011.

### Phase III

#### Interaction with Specific Stakeholders

1. During this phase consultations, amongst other, included the following:

| Stakeholder | Entity | Period | Purpose |
| --- | --- | --- | --- |
| System Vendors | Samras  User group | September 2011  February 2012 | To discuss the proposals for segments for mSCOA and presented to their user groups on envisaged changes. |
| Fujitso  User group | October 2011  November 2011 |
| Sebata | February 2012 |
| Vesta | November 2011 |
| SAP SA and City of Cape Town | February 2012 |
| Municipalities | Overstrand | November 2011 | To discuss mSCOA proposal and map account detail. |
| Saldanha | February 2012 | To discuss MSCOA proposal |
| eThekweni | October 2011 | To discuss mSCOA proposal and do mapping of account detail. This municipality subsequently decided to withdraw as a pilot. |
| Umahlatuze | October 2011 | To discuss mSCOA proposal and do mapping of account detail. |
| City of Cape Town | February 2012 | Follow-up meeting from April 2011 to get views from SAP as introduced at the City of Cape Town during March 2011. |
| National Departments | Water Affairs | December 2011 | Quarterly meeting to update and discuss the progress made on the development of mSCOA. |
| Trade and Industry | February 2012 | To introduce the principles of mSCOA and discuss the requirements. Waiting for input on the requirements of the department. |
| Human Settlement | February 2012 | To introduce the principles of mSCOA and discuss the requirements. Waiting input on the requirements of the department. |
| Professional Bodies | IMFO | September 2011 | High level presentation given at the IMFO Conference on mSCOA |
| Regulators | NERSA | September 2011 – February 2012 | Held various meetings to address the NERSA Regulatory Reporting Requirements in mSCOA. Resulted in a discussion document to resolve differences that will be the subject of a future meeting with NERSA to agree on the Principles for including their requirements. |

1. Version 3 of the mSCOA was completed to the end of July 2012. This version was then broadly consulted with external stakeholders through a serious of information sessions, workshops and stakeholder-specific workgroups.
2. Specific attention was directed towards engagements with all stakeholders utilising local government financial information. The focus on National and Provincial Departments has yielded mixed results to date. At this point in time the project team only had ongoing engagements with the Department of Water Affairs, Human Settlement and Trade and Industry. Attempts to work with provincial departments yielded limited success.
3. Definitions had been added to accounts to clarify the use and assist in clearly defining the accounts and the use thereof.
4. Initial work commenced to prepare a SQL database for the purpose of testing the completeness of the classification framework and testing report extraction based on the fields populated within the sample database. This database will assist in ensuring that the classification framework provides for all dimensions required by stakeholders and specifically focus attention on the extraction of the budget reporting tables, annual financial statements, secondary cost allocation reports and management account information.

#### Pre-mSCOA Regulation

1. Phase III represents the final phase prior to implementation of the mSCOA for local government; hence requiring intensive consultation with a wider audience. These engagements included system developers, potential ‘pilot’ sites, users of local government information, regulators, professional bodies, advisors and consultants and other stakeholders active in the local government sphere.
2. Information sessions with key-stakeholders and practitioners were hosted between August and October 2012.
3. Specific attention was given in providing SALGA and COGTA with the progress and outcomes of the mSCOA development process.
4. All advisors and consultants providing services to local government were given the opportunity to directly engage with National Treasury; this session was well attended.
5. The main objective for hosting these sessions was to seek specific and general comments from practitioners and other stakeholders in finalising and concluding the mSCOA tables to inform the drafting of the regulation.
6. The comments received were considered and resulted in mSCOA Version 4 informing the drafting of the regulation, developing the SQL Database and testing the classification framework as it relates to the extraction of reporting information. Annexure A, attached, summarises the comments received, actions taken and revision made to mSCOA where applicable.
7. The successful testing of the SQL Database by simulating a small and medium size municipality from a budget, accounting and financial modelling perspectives is the first step towards formulating the specifications for the system implementation of mSCOA.
8. This “simulation” will assist in bringing more specific information to practitioners, stakeholders and advisors as part of the “formal consultation process” to finalise the regulation.
9. This phase of the project further resulted in finding “alignment” between the Budget Reporting Formats and the annual financial statements (AFS) template resolving some concerns raised by practitioners through the comments process. This principle contributed to significant changes being made to mSCOA Version 3 being the subject of the pre-engagement information sessions.
10. The Financial Modelling Project advanced to the stage where the outcomes resulted in an outline for classification and recording “secondary costing” in a uniform manner through introducing a further segment in mSCOA, referred to at that stage of the project as the “Financial Modelling Segment”/ (the Costing segment).
11. During this period the following information sessions were undertaken:

|  |  |  |  |
| --- | --- | --- | --- |
| Stakeholder Group | Date | Stakeholder | Information Session/ Direct Engagement |
| 1. Provincial Treasuries and Municipalities | 20 August 2012 | Free State Municipalities and Provincial Treasury | mSCOA Version 3 Information Session |
| 4 September 2012 | North West Municipalities and Provincial Treasury |
| 5 September 2012 | Gauteng Municipalities and Provincial Treasury |
| 6 September 2012 | Northern Cape Municipalities and Provincial Treasury |
| 11 September 2012 | Western Cape Municipalities and Provincial Treasury |
| 27 September 2012 | Mpumalanga Municipalities and Provincial Treasury |
| 1 October 2012 | Kwazulu-Natal Municipalities and Provincial Treasury |
| 2 October 2012 | Limpopo Municipalities and Provincial Treasury |
| 3 October 2012 | Eastern Cape Municipalities and Provincial Treasury |
| 1. National Departments | 24 September 2012 | All national departments invited but limited attendance at the session | mSCOA Version 3 Information Session |
| 13 September 2012 | Cooperative Governance and Traditional Affairs | mSCOA Version 3 Information Session |
| 1. Professional and Oversight Bodies | 17 September 2012 | SALGA | mSCOA Version 3 Information Session |
| 21 September 2012 | IMFO, ASB and SAICA |
| 25 October 2012 | AGSA |
| 8 October 2012 | IMFO Conference | Overview of Information Sessions |
| 1. Regulators | 20 October 2012 | NERSA and SARB | mSCOA Version 3 Information Session |
| 1. Municipalities | See A above | Wider Group |  |
| 29 – 30 October 2012 | City of Cape Town | mSCOA Version 3 Workshop Invitation from the municipality |
| 1. System Vendors | 26 October 2012 | Invited all “vendors” known to National Treasury and engaged through the “Business Process Project”. | mSCOA Version 3 Information Session |
| 1. Internal Stakeholders – National Treasury | After National Budget announcement |  | Meeting pending draft regulation, updated tables and project summary document. |
| 1. Advisory and Consulting Firms | 25 October 2012 | All known to National Treasury and from ASB Forum attendance list | Consulting firms functional within the municipal environment to be involved information session to share the mSCOA development. |

#### Public Participation on the Municipal Regulations on a Standard Chart of Accounts (mSCOA)

#### Structure of the consultation process subsequent to publication

1. As part of the formal consultation and awareness campaign, engagements were hosted as follows:

|  |  |
| --- | --- |
| Engagement Date | Stakeholder / Role-player |
| 25 September 2013 | National Treasury and respective chief directorates |
| 26 September 2013 | Provincial treasuries, national departments and the Technical Committee of Finance (TCF) Working Committee |
| 3 October 2013 | Consultants, advisors and professional bodies |
| 4 October 2013 | System vendors |
| 7 October 2013 | Metropolitan municipalities |
| 8 October to 11 November 2013 | District level engagement with municipalities |
| 6 to 13 November 2014 | Engagement with the respective pilot municipalities and system vendors |

1. The formal sessions hosted in the districts (local and district municipalities) between 8 October and 11 November 2013 were each held for an entire day and the agenda included a formal briefing session on the Regulation, Project Detail Document and classification framework.
2. The Chief Directorate: Local Government Budget Analysis (LGBA) also hosted all the IT system vendors currently operating in the space of local government from the 6 to 13 November 2013. In addition to discussing and presenting the mSCOA classification framework, these engagements were structured to evaluate the technical readiness of the various technologies applied by the system vendors in piloting the mSCOA classification framework; these engagements were well attended by both the vendors and identified pilot municipalities. There is no doubt that some of the IT system vendors may struggle to comply to the minimum requirements of the Regulations. Although the Regulations will place pressure on the IT system of vendors and their respective technical solutions, this can however not be used as an excuse not to implement this strategic reform.
3. The following table provides a breakdown of each of the respective district engagements as well as attendance numbers:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| District Municipality | Date of Workshop | Attendance |  | District Municipality | Date of Workshop | Attendance |
| Alfred Nzo | 9 Oct 2013 | 14 |  | Ngaka Modiri Malema | 29 Oct 2013 | 36 |
| Amajuba | Joint session | n/a |  | Nkangala | Joint session | n/a |
| Amathole | 21 Oct 2013 | 25 |  | OR Tambo | 8 Oct 2013 | 32 |
| Bojanala | 4 Nov 2013 | 53 |  | Overberg | Joint session | n/a |
| Cacadu | 4 Nov 2013 | 25 |  | PixleyKaSeme | 17 Oct 2013 | 26 |
| Cape Winelands | 22 Oct 2013 | 57 |  | Sedibeng | 6 Nov 2013 | 44 |
| Capricorn | 17 Oct 2013 | 32 |  | Sekhukhune | 11 Oct 2013 | 21 |
| Central Karoo | Joint session | n/a |  | Sisonke | Joint session | n/a |
| Chris Hani | 22 Oct 2013 | 21 |  | Siyanda | 10 Oct 2013 | 31 |
| Dr Kenneth Kaunda | 14 Oct 2013 | 24 |  | Thabo Mofutsanyane | 21 Oct 2013 | 18 |
| Dr Ruth Segomotsi Mompati | 30 Oct 2013 | 21 |  | Ugu | Joint session | n/a |
| Eden | 28 Oct 2013 | 50 |  | Umgungundlovu | 10 Oct 2013 | 74 |
| Ehlanzeni | 31 Oct 2013 | 37 |  | Umkhanyakude | Joint session | n/a |
| Fezile Dabi | 8 Oct 2013 | 8 |  | Umzinyathi | 22 Oct 2013 | 24 |
| Frances Baard | 16 Oct 2013 | 23 |  | Uthukela | Joint session | n/a |
| Gert Sibande | 25 Oct 2013 | 17 |  | uThungulu | 29 Oct 2013 | 70 |
| iLembe | 16 Oct 2013 | 18 |  | Vhembe | 16 Oct 2013 | 23 |
| Joe Gqabi | 23 Oct 2013 | 22 |  | Waterberg | 18 Oct 2013 | 25 |
| John TaoloGaetsewe | 31 Oct 2013 | 18 |  | West Coast | 23 Oct 2013 | 43 |
| Lejweleputswa | 15 Oct 2013 | 19 |  | West Rand | 11 Nov 20013 | 29 |
| Mopani | 15 Oct 2013 | 19 |  | Xhariep | 25 Oct 2013 | 40 |
| Namakwa | 9 Oct 2013 | 32 |  | Zululand | Joint session | n/a |

1. In total 1,071 officials attended the engagements. While participation and interaction varied between engagements, the general attitude of local government finance practitioners was that the mSCOA is a welcomed reform. Salient concerns during these engagements included:
   * + - Relatively short timeframes for implementation being 1 July 2016;
       - Inability of some of the current system vendors to accommodate the technical specifications of the mSCOA classification framework;
       - Capacity and skill constraints on the part of the municipalities to absorb the reform shock associated with change management;
       - Funding constraints; and
       - Technical complexity of the mSCOA classification framework.

#### Comments received and impact on the mSCOA classification framework

1. In total 995 comments were received; if these comments are unpacked into individual comment items, submissions exceed 2,000. Stakeholders that commented, made recommendations and raised concerns included:
   * + - 35 municipalities. Importantly, of the 8 metropolitan municipalities, 7 commented and the remaining municipalities included both local and district municipalities. This provides for coverage across all categories of municipalities;
       - Professional bodies included the South African Local Government Association (SALGA), Accounting Standards Board, and Institute of Municipal Finance Officers (IMFO);
       - Five system vendors that are active within the local government space; and
       - Four consulting and advisory service providers.
2. The following table provides for the detail of stakeholders that provided comments, made recommendations and raised concerns.

|  |  |
| --- | --- |
| Municipalities | |
| eThekwini Metropolitan Municipality | City of Johannesburg Metropolitan Municipality |
| Nelson Mandela Bay Metropolitan Municipality | City of Tshwane Metropolitan Municipality |
| Mangaung Metropolitan Municipality | City of Cape Town Metropolitan Municipality |
| Buffalo City Metropolitan Municipality | Emakhazeni Local Municipality |
| Cacadu District Municipality | Mafikeng Local Municipality |
| uMhlathuze Local Municipality | Thaba Chweu Municipality |
| Sol Plaatjie Local Municipality | Nkangala District Municipality |
| Mogale City Local Municipality | Witzenberg Local Municipality |
| Midvaal Local Municipality | Joe Gqabi District Municipality |
| Thembisile Hani Local Municipality | Gert Sibande District Municipality |
| Mossel Bay Local Municipality | Bitou Local Municipality |
| Msunduzi Local Municipality | Witzenberg Local Municipality |
| Stellenbosch Local Municipality | Saldanha Bay Local Municipality |
| Theewaterskloof Local Municipality | Breede Valley Local Municipality |
| Langeberg Local Municipality | Overstrand Local Municipality |
| Knysna Local Municipality | George Local Municipality |
| Beaufort West Local Municipality | Drakenstein Local Municipality |
| City of Cape Town International Convention Centre (CTICC) |  |
| Professional Bodies | |
| South African Local Government Association | Accounting Standards Board |
| Institute of Municipal Finance Officers |  |
| System Vendors (Financial Applications) | |
| Business Connexion | BIQ Quill |
| Payday | Fujitsu |
| SAMRAS |  |
| Consultants and Advisory Services | |
| Altimax – Accounting, Advisory and Training | Mubesko Africa |
| CQS Caseware | Ducharme Consulting |

1. In summary, the 995 comments were sorted and categorised as follows:
   * + - 10 comments were categorised as possibly impacting on the formal Regulations;
       - 217 comments were categorised as possibly impacting on the classification framework (mSCOA tables);
       - 277 comments were related to the Project Summary Document (PSD);
       - 404 comments categorised as frequently asked questions; and
       - 87 were general observations relating to the policy intent of the reform.

#### Key issues raised, and changes made to the regulations

1. Many of the comments were valuable for refining the mSCOA classification framework (mSCOA tables). The categorisation of frequently asked questions will also assist immensely with the upcoming change management and implementation phase (Phase 4) of mSCOA Project.
2. In terms of the 10 comments received directly impacting on the Regulations, most of the comments were related to grammatical considerations; only two comments required consideration in terms of the design principles.
3. Several matters of a technical nature emanated from the comments received. These have been summarised in the table below:

|  |  |
| --- | --- |
| Technical Consideration | Direct impact on MSCOA classification framework (MSCOA Tables) |
| Impact of IAS 12 on MSCOA | Yes |
| Overall compliance to accounting framework pending finalisation of reporting tables | Yes |
| Consultation with SARS in relation to VAT | Yes |
| Technical discussion and resultant position papers: |  |
| * Accrued Leave | Yes |
| * Agency Services | Yes |
| * Bad debt written-off | Yes |
| * Capitalisation Threshold | Yes |
| * Catering versus Entertainment | Yes |
| * Correction of prior period errors | Yes |
| * Detail to be included in the general ledger | Yes |
| * Discount received | Yes |
| * Self-Insurance reserve and related transactions | Yes |
| * Reserves and funds | Yes |
| * Transfers and subsidies | Yes |
| * External stakeholders i.e. NERSA, DWA etc. | Yes |
| * Month and year-end closure | No |
| * Portal access | No |
| * Transitional arrangements   + Comparative and historical Information   + Reporting requirements – phased approach | No |

1. The above technical issues will be addressed as part of mSCOA Phase 4 (change management and piloting of the mSCOA classification framework) in consultation with the Office of the Accountant General. It needs to be noted that although the technical considerations will in most cases impact on the mSCOA classification framework (mSCOA tables), it’s not envisaged to have a material impact. In most instances it’s envisaged that the position papers will provide guidelines for the consistent application by all municipalities and not result in extensive changes to the actual classification framework.

## Preliminary Observations

1. The detail substantiating the overall observation can be found in the detailed project document. In summary, the following broad observations were made by the Project team when considering the charts of accounts from the selected municipalities:
   * + - As a result of not making use of a multi-dimensional chart, information such as funds utilised, vote (functions and sub-functions), cost collectors, and project, is not readily available.
       - In order to compensate for some of these shortcomings labels are not always clear and have been developed based on “projects or activities” rather than “who or what gets paid”.
       - Labels are found duplicated in many instances.
       - Different municipalities are classifying similar transactions under different headings.
       - Numerous inter-departmental accounts were identified resulting from the absence of a defined organisational vote or sub-vote segment.
       - Asset detail information are either condensed throughout the classification or summarised with limited detail, for example operating leases, asset specific accounts and repairs and maintenance.
       - Reserves, funds and provisions together with the transfers to/ from are not in compliance with GRAP.

## Overall Design Principles

1. The mSCOA for Municipalities will operate on the basis of a “standard list of all available accounts” in an Excel Spreadsheet from which the municipality can select the relevant accounts from the respective segments.
2. Indicators will be added to guide practitioners on the use of accounts, for example some accounts might be required for all municipalities whilst other more detailed accounts might be optional depending on the data available or to be determined by the financial recording system in use.
3. The final product will include definitions for the key group of accounts to assist practitioners in achieving consistency in recording transactions of a similar type or nature between municipalities to enhance the comparability of information.
4. Inherent to the design of the classification to be applied within the segments of mSCOA the following principles need to be applied:
   * + - consideration to be given to international standards, guidance and best practices;
       - labels and accounts defined to have readily available the information needed for local government budgeting (annual budgets, adjustment budgets and SDBIP) and reporting (monthly, mid-year performance assessment and annual financial statements);
       - general alignment of financial reporting formats and the annual financial statements to key budget format reforms;
       - alignment of budget and reporting formats with the Standards of GRAP;
       - consistent use of terminology across all municipalities by defining all accounts and labels in simple terms to support appropriate classification of transactions throughout all municipalities;
       - standardisation across local government clearly outlining the information requirements that will enable municipalities and their information system suppliers to develop software and report writing formats that are automated and complaint to reporting requirements governing local government;
       - reporting on the “whole-of-local government”, and thus contribute to “whole-of-government” monitoring and evaluation;
       - finding a solution for the separation of the general government sector, which “consists of entities that fulfil the functions of government as their primary activity” and business activities that sell services at market prices within a local government environment. Especially where the management of these functions tend to be closely interrelated with general government activities;
       - minimising the cost of compliance and information gathering; and
       - the classification framework must be kept simple and avoid unnecessary complexities to the maximum extent possible, while ensuring the policy intent and overall objectives are achieved.

## Upcoming Activities – Post-regulation

1. Version 5 of the chart of accounts were completed based on the outcome of the formal consultation process on the draft mSCOA Regulation and comments received.
2. The mSCOA Technical Committee is to be established to continue with the responsibilities as envisage in the mSCOA Regulation, 2014.
3. Any changes, revisions, clarification, concerns and additions of MSCOA Version 5 would need to be addressed to the MSCOA Technical Committee through a process to be developed by National Treasury for this purpose.
4. Phase 4 initiated the next phase of the project to achieve an acceptable level towards meeting the reporting requirements prior to “release” of a final version for budget and planning 2017/18. This has been done on 4 November 2016.

## Segment Detail

### The MSCOA Segments

1. The design is based on the use of seven segments, being:
   * + - Costing
       - Funding;
       - Functions;
       - Municipal Standard Classification;
       - Project;
       - Costing
       - Regional Indicator; and
       - Item.
2. When recording a transaction, a selection must be made from each of these segments, meaning that all segments must be used for recording a single transaction.

### Understanding the mSCOA Tables

1. The details supporting the mSCOA Segments are presented in the mSCOA tables developed in Microsoft Excel.
2. Due to the size of the Item Segment the detail are presented in four separate tables featuring revenue, expenditure, gains and losses, assets, liabilities and net assets.
3. The mSCOA tables contains valuable information to understand the segment detail and assist the municipality to set-up an account structure unique to their requirements while maintaining a standard classification framework informing various reports to be customised as required by National Treasury, External Stakeholders such as NERSA, the Department of Water Affairs, annual financial statements, etc.
4. In summary the tables contain the following information with a description thereof:
   * + - Posting Level: Contains the account posting level based on a “string” providing a relative link to the reporting levels.
       - VAT (Value Added Tax) Status[[1]](#footnote-1): Include an abbreviation giving guidance on the VAT implications generally associated with the type of transaction. The explanations on the VAT Indicators will be provided in the Position Papers and Project Detail Document dealing with VAT. At time of finalising Version 6.1 this initiative had not reached its logical conclusion.
       - Account Number: The account number is based on the levels presented in the hierarchical structure of the classification within the segment. Provision is made for expansion and adding account numbers for posting level detail included by the municipality.
       - Posting Level: This indicator informs if the account is a posting level or reporting level. If “Yes” this account is the posting level and “No” indicates a non-posting level.
       - Breakdown Required: This indicator guides if “additional detail on a posting level” is required by National Treasury. If detail is provided for this will become the default posting level.
       - Principle: The “principle” gives guidance on the detail to be added and the context with in which expansion need to be considered. Depending on the Segment the additional information would be required to set the posting level.
       - Applicability: This indicator provides detail on the relevance of the account to municipalities, district municipalities and municipal entities. Further, also indicating detail added to be able to extract reporting information required by NERSA and the Department of Water Affairs.

### Code Structure

1. The code structure assigned to the various MSCOA Segments contains an alphanumerical character to define the segments followed by a numerical structure representing the various levels within the reporting structure. Summary of these could be found in the Register of Design Principles.

### Stakeholder Information required in terms of legislation other than National Treasury Legislation and Regulation

1. Inherent to the compilation of the mSCOA Classification Framework is the aim to provide in as far as possible for the information required by various stakeholders for reporting purposes.
2. The mSCOA Classification Framework Version 6.1 has identified in the mSCOA tables the information required for reporting purposes by the Department of Water Affairs, NERSA and SARS[[2]](#footnote-2). We do believe as the piloting and pending implementation of mSCOA evolves, more stakeholders will be identified realising the value of the mSCOA Classification Framework to enhance municipal compliance, quality of reported information and standardisation across the local government sector and their requirements incorporated in the mSCOA tables in a similar way.
3. The tables include indicators to identify the reporting requirements of NERSA and the Department of Water and Sanitation. The mSCOA Classification Framework makes provision for the information requirements of these stakeholders however, the mSCOA Regulation does not enforce compliance to these requirements. Accordingly the chart of accounts are set-up to accommodate those municipalities opting to comply with the stakeholder requirements and those not in a position to comply. These indicators are contained in the information column included in the excel tables on “applicability”.

## Costing Segment (Project Detail Document Section 1)

1. The content of this section needs to be read with the National Treasury Guideline on Costing Methodology. Furthermore, the purpose is not to provide comprehensive content on “costing methodology and underlying principles” but rather to contextualise the classification included in the mSCOA Costing Segment.
2. Cost is an important element of the decision-making process for setting municipal tariffs. Information about costs is relevant even when the municipality provides goods and services for free or for a nominal consideration as a result of national/ municipal policy decisions, or when tariffs are set on the basis of market prices.
3. Accrual accounting forms the basis for municipal budgeting and management information. Recognition of the need for cost accounting in “right sizing, eliminating inefficiencies and privatisation” triggered the increased use of cost accounting and the development of systems to support cost accounting. This will also motivate municipalities to use cost accounting more, which will result in more cost accounting systems being developed.
4. When starting to implement a cost system, a municipality may initially choose to only maintain limited cost information. As the municipality gains knowledge of its exact requirements and the likely costs of gathering the additional data, it can progress to a more comprehensive system. The mSCOA classification enables exactly this by providing for “minimum requirements”, but sufficient enough in detail to accommodate more sophisticated costing applications. When comparing for example, the mSCOA costing segment to the costing system of some of the municipalities, it is clear that these municipalities have a far more advanced costing system (based on “activity based costing”). mSCOA enables these municipalities to continue transacting on its advanced costing module yet meet the minimum requirements provided for in mSCOA.
5. When considering how to improve the quality of available information, the National Treasury (mSCOA Project Team) considered the advantages of using cost accounting for management purposes in addition to accrual accounting for financial reporting. In theory and research there are a number of approaches that governments in different circumstances can adopt to progressively implement cost accounting. This is a principle used to define the classification framework of the mSCOA Costing Segment.
6. Processing costing accumulates costs by individual processing “functions” and then finally by outputs of the municipality. The output of “sub-function” either becomes the input of the next “sub-function” in the production flow or becomes a part of the end product output. Normally, each “sub-function” reports its costs, the completed units, and the work-in-process volume for each reporting period. When completed units are transferred from a “sub-function” to the next “sub-function”, the costs of those units are also transferred and are eventually incorporated in the cost of the municipality’s end product, being a service.
7. Some municipalities may wish to set information requirements at the activity level, an even lower level than processes or jobs. The concept of “Activity Based Costing” is that activities consume resources, although activities may sometimes be congruent with processes, if processes are defined narrowly. “Activity Based Costing” can be used in conjunction with job-order costing or process costing to enhance the accuracy of these costing methods. This method is not encouraged by National Treasury due to the complexities involved, sophisticated system requirement and ultimately cost versus benefit considerations.
8. The cost system’s functionality needs to include a report generator with capacity to generate a variety of reports needed by management or to satisfy financial reporting requirements. To benefit from this capacity, the needed data must be inputted to the system and the rules for capturing, distributing, and calculating the information must be there.
9. The “Cost” segment provides for the classification of indirect (secondary) costs that do not directly attribute to the output and are sometimes referred to as activity based recoveries, for example labour; vehicle; plant and equipment; internal service charges (internal billings), and, departmental charges - for example office rental; audit fees; and, procurement.
10. Indirect cost (secondary cost) is initially recorded as primary cost within the “Item” segment and funded according to the indicator selected in the “Fund” segment.
11. The cost indicator within the “Costing” segment provides for the re-distribution of these primary costs between functions (no change in the funding source); together with indicators provided in the “Function” segment. The “Project” segment provides the classification link to these indicators and specific projects.

Management Accountants/ Tariff modelling. The Design Principles acknowledge a gradual approach, for example “administrative functions to commercial services will suffice”.

1. Standardisation of “cost recovery approaches” would only be of concern once municipalities are able to meet “minimum classification requirements” in recording cost allocations within the general ledger accounts and mSCOA segments.
2. At the highest level the segment structure distinguishes between “Charges” and “Recoveries” followed by accounts groups for “Departmental Charges (Support Services), Internal Billing and Activity Based Recoveries”:

**Definitions:**

**Charges/Recoveries:** Distinction is made between "charges to receiving departments and recoveries made by sending departments". The “sending department” provide goods or services to the “receiving department” based on rates/ tariffs determined internally by the municipality in terms of the municipalities costing methodology. Recording of the transaction in mSCOA thus impacts on the Function, Costing and Municipal Standard Classifications. Default will be applicable within the Regional Indicator, Funding and Item segment. The illustration below attempts to explain the concept in a simplified version not dealing with specific accounts in mSCOA.

**Department providing the service/ goods:** Debit to the “receiving department” by selecting the appropriate account from the Function and Municipal Standard Classification with the account from “Charges” from the Costing Segment.

**Department receiving the service/ goods**: Credit to the “sender department” by selecting the appropriate account from the Function and Municipal Standard Classification with the account from “Charges” from the Costing Segment.

**Departmental Charges/ Recoveries (Support Services):** This refers to the allocation of overheads to a cost centre used by multiple functions, such as Information Technology; for example, pro rata allocations based on the number of service points or users such as the electricity department. Some applications refer to assessment charges. The “receiving department” is charged by the “department providing the support services”.

**Charges:** This classification provides for the recording of the “charge-out” recognised by the receiving department.

**Recoveries:** The “provisioning department” effect a charge to the receiving department, resulting in a recovery to the department, classified as a recovery.

**Activity Based Charges/ Recoveries:** This refers to the actual allocation of resources (used or benefit method) used by various departments; for example, allocation of labour is based on time sheets, and the allocation of vehicles and plant equipment is based on log sheets. The “provisioning department” charges the user or receiving department and accordingly make a recovery.

**Charges:** This account provides for recording the “charge-out” to the receiving department.

**Recoveries:** This account provides for recording the “recovery” made by the provisioning department.

**Internal Billing:** This refers to departmental use of internal services such as electricity, water, waste water management and waste management, for example cost allocation for the electricity department’s water.

**Charges:** The classification provides for the department receiving the service or goods.

**Recoveries:** This classification provides for the department providing the service or goods.

**Default:** All transactions not relevant to the allocation of secondary cost to be classified within this account.

## Function Segment (Project Detail Document Section 2)

1. The “Function Segment” is the location within mSCOA for creating a standardised “vote” structure throughout municipalities. In addition, the segment makes distinction between “core-” and “non-core functions” or also known as “funded” or “un-/ under-funded mandates” and agency services.
2. The South African Cities Network defines an unfunded/ underfunded mandate as: “when municipalities perform the functions of other spheres of government and bear significant cost out of their own revenue sources”. These unfunded/ underfunded mandates pose an institutional and financial risk to the municipality as substantial amounts of own funding is being allocated to non-core functions at the expense of basic service delivery which is the core mandate of the municipality.
3. One of the main objectives of local government is to ensure the provision of basic services to communities. Section 153 of the Constitution requires that budgeting processes must prioritise the basic needs of the community. MFMA Circular 74 urges municipalities to prioritise the provision of basic services such as electricity, water, sanitation and refuse removal in their medium term revenue and expenditure framework (MTREF) budgets. Based on the guidance contained, municipalities may only budget for non-core functions such as nurseries, sports fields, libraries, museums, health services, etc. if:
   * + - the function is listed in Schedule 4B and 5B of the Constitution;
       - the function is assigned to municipality in terms of national and provincial legislation;
       - the municipality has prioritised the provision of basic services; and
       - it does not jeopardise the financial viability of the municipality.
4. Municipalities are urged to sign service level agreements and recover costs where unfunded/ underfunded mandates are performed on behalf of other spheres of government. However, it will not constitute an unfunded/ underfunded mandate if the municipality provides non-core services beyond what is stipulated in the service level agreement.
5. The guidance provided in MFMA Circular 74 (as discussed in the preceding paragraphs) supports the design principles adopted in the classification structure adopted for this segment within the mSCOA classification framework.

The key question to answer in classifying transactions within this segment is “against which function or sub-function” should the transaction be recorded?

1. The high-level functions included in the mSCOA classification are summarised in the table below:
2. The classification structure for the Function segment distinguishes between “Core Functions” (Section 145(1) functions as per the Constitution) and “Non-core Functions” (Section 145(4) functions as per the Constitution).
3. Essentially the functions provided are based on the MFMA Circular 12 functional classification, which is based on the international Government Finance Statistics (GFS) classification 2011.
4. The function/ sub-function approach has been adopted by municipalities for a substantial period as a reporting framework and is included in the Municipal Budget and Reporting Regulations, 2009. At present this segment is implemented mostly through the use of mapping tables designed by the system vendors, with a few municipalities adopting the function/ sub-function as their organisational structure. This approach results in the municipal standard classification being obsolete for these municipalities.
5. The general provision is contained in the Constitution, section 156, determining the powers and functions of municipalities.
6. Section 156 (1): “A municipality has executive authority in respect of, and has the right to administer a) the local government matters listed in Part B of Schedule 4 and Part B of Schedule 5 and any other matter assigned to it by national or provincial legislation and b) any other matter assigned to it by national or provincial legislation.
7. Section 156 (4): “The national government and provincial government must assign to a municipality, by arrangement and subject to any conditions, the necessary administration of a matter listed in Part A of Schedule 4 or Part A of Schedule 5 which relates to local government, if a) that matter would most effectively be administered locally and the municipality has the capacity to administer it.
8. Core Functions provides for the matters in terms of sections 156 (1) of the Constitution. These are functions performed by local government and constitutionally assigned to local government in terms of Part B of Schedule 4 and Part B of Schedule 5.
9. Non-core Function refers to the functions performed by local government that are constitutionally assigned to provincial government in terms of section 156(4) of the Constitution. Local Government are compensated for delivering these functions on behalf of provincial government and typically receive a management fee from the provincial department.
10. Non-core Functions are in certain instances commonly referred to as “Agency Services” and may contribute to unfunded or underfunded mandates. The principle underlying agency services is that the municipality performs a function (service) on behalf of another sphere of government.
11. The agency fee received by the municipality to compensate it for the cost of providing the agency service should be recognised by the municipality as receipts and not set-off against the expenditure.
12. The actual expenditure incurred to deliver the agency services must be recognised by the sphere of government (provincial) on whose behalf the function is rendered, municipality as expenses. This functional classification is therefore used for the recording of transactions relating to the provision of “agency services” by the municipality.
13. In applying the legislative requirements to the mSCOA table the provisions of section 84 of the Local Government: Municipal Structure Act, 1998 (Act No. 117 of 1998), have been used to set-up the “application indicators” to distinguish between either all or a combination of “metro, local and district” municipalities depending on the guidance available. District municipalities have indicated that some functions need to be added to the current mSCOA as non-core based on the principle that district municipalities have been assigned the function and powers for a sub-function where the local municipality in that district is defaulting on its assigned function and powers.
14. It is important to the budget and planning process and inherent to the nature of municipal services to determine tariffs for services such as waste collection, sanitation, water and electricity.
15. Providing for these services as separate functions within this segment facilitate that the revenue, expenditure, assets, liabilities and net assets underlying and supporting these functions, are linked through the Item Segment. In simple terms it facilitates the extraction of financial information specific to the functions provided for in this segment.
16. Conditional to accurate information is the internal control policies and procedures instituted by the municipalities to oversee the initiation, input, processing and output of transaction data through the financial system.
17. The two elements inherent to cost reflective tariffs is to have a collective view of not only direct-cost relating to these tariff services but also secondary (indirect) cost associated to the tariff service. For example, to provide water to the community would require meter-reading to capture the periodic use from the installed meters to the financial system to bill users. This cost adds to the value of the water provided to the community and thus needs to be reflected in the tariffs used to bill users.

## Funding Segment (Project Detail Document Section 3)

1. The Funding segment in the financial system identifies the various sources of funding available to municipalities for financing expenditure relating to the operation of the municipality for both capital and operational spending.

The key question in finding the appropriate classification code for this segment is: “against which source of funding is the payment allocated and against which source is revenue received?”

1. The introduction of this dimension in the mSCOA will facilitate the accumulation of information within the financial system to be able to report on information such as how a specific source of funding, for example “the Local Government Financial Management Grant” has been spent by extracting this specific source of funding from the Funding segment and the detail on spending items, such as employee costs, consultants, etc. from the Item segment.
2. The primary source of funding for a municipality is property rates, service charges, equitable share and other own revenue. Further to these sources of revenue a municipality also spends funds transferred from other spheres of government , namely transfers and subsidies such as appropriated by national and provincial government in terms of the Division of Revenue Act (DoRA). In order to monitor expenditure (operational and capital) against the source of fund utilised - this segment contains the sources of funds available to the municipality.
3. In addition to internally generated funds and transfers and subsidies municipalities may make use of external borrowings to finance capital projects.
4. A further source of funds available for utilisation is “cash backed reserves” as directed by the municipality’s financial policy on the introduction and utilisation of a specific reserve.
5. The source of funds available and utilised for operational and capital spending according to the approved budget, are summarised in the table below with the definitions included for the high-level categories.
6. At the highest level the segment structure distinguishes between “Non-funding Transactions, Operational and Capital”. The distinction between “operational and capital” funding sources has been introduced in Version 6.1 of the mSCOA Tables:

## Project Segment (Project Detail Document Section 4)

1. Municipalities have to use the Integrated Development Plan (IDP) as the bases to strategically plan for future development in the municipal area, drawing the IDP from the municipality’s longer term spatial development plans of 20 plus years. This planning approach involves the entire municipality as well as the public and other stakeholders in finding the best options to achieve good and sustainable long-term development.
2. The IDP has a lifespan of 5 years that is linked directly to the term of office for local councillors. After every local government election, the new council has to decide on the future of the IDP in the context of the municipality’s longer term spatial development plans. The council can adopt the existing IDP or develop a new IDP that takes into consideration these existing plans.
3. At a district municipality-level, the framework will be developed in consultation with all local municipalities within the district. This framework will ensure co-ordination, consultation and alignment between the district council and local municipalities. The framework will guide the development of the IDP process plan for each local municipality.
4. The review of information received from selected municipalities highlighted the need for a segment containing the information on the various projects. The detailed accounts included various accounts for project-related expenditure combined in a single line-item is most properly the only way in the existing account structure to accumulate financial information on important or strategic projects. The accumulation of project-related transactions in a single posting-level account results in a classification not relating to “what is bought”.
5. This segment is structured to link all operational and capital expenditure to a project whether it is a specific capital project, operational initiative or running the municipality.
6. The Project segment distinguishes projects according to the nature of the expense whether it is capital or an operational expense.

The key question to be asked in finding the appropriate classification for a transaction is: “does the transaction relate to a specific project and if so, what type of project”? This segment is to ensure that all projects in the IDP is aligned to the municipality’s budget.

1. Setting-up projects in the “Project” segment, the objective must be to link the IDP to the budget and ultimately report on each of the projects identified in the IDP. All activities of the municipality would therefore need to be aligned to “Projects” segment, including institutional costs associated with the functioning of the municipality such as cost for the administrative and staff; this allows for planning and budgeting on a project level.
2. The “Project” segment together with the “Funding”, “Regional” and “Function” segments contribute in reporting on strategies and putting into actions projects by providing for it in the budget. The “Fund” segment assists in the allocation of funding to the projects. The regional indicator provides information on “Who is going to benefit from the project”. The “Project” segment together with the “Item “segment assists in costing the project and to hold people accountable for delivery within the budget. The “Function” segment assigns responsibility to managing the project.
3. The project lifecycle will not be informed by the mSCOA; as a principle to facilitate proper planning and reporting, the system application needs to assist in providing this information. Indirectly, if it is a “multi-year project”, it will be derived from budgeting for the project over multiple periods. Refer to “Discussion of the segment” for more detail on the IDP.
4. The table presented below provides a high-level overview of the Project segment with a discussion on the classification given in the paragraphs as referenced:

**Definitions:**

**Capital:** Capital usually applies to expenditure of a "long term nature" and capitalised to the Property, Plant and Equipment group of accounts in the financial statements. Projects are therefore created along this definition of capital and the detail included under the labels for either infrastructure or non-infrastructure projects. Expenditure used to create new assets, increase the capacity of assets beyond their original design capacity or service potential, or to return the service potential of the asset or expected useful life of the asset to that which it had originally. CAPEX increases the value of capital stock.

**Operational:** Operational projects refer to current and short-term projects for which the cost is immediately recognised as an expense and funded from the municipalities' operational budget. Included in this category is “infrastructure projects” done by the municipality for transfer to another municipality, entity or households.

**Default Transactions**: Default account for transaction not relating to either capital or operational expenditure and of no specific interest in the context of this segment.

1. The “Project” segment distinguishes projects according to the nature of the expense, whether it is capital or an operational expense.
2. Transactions other than expenses (capital and operational) are recorded as “Default Transactions”. This group of accounts provide for the transaction types not specifically recorded within the capital and operational project structures for example receipts, billing-run accruals, money transfers between the primary bank account and specific purpose bank accounts and so on.
3. The definitions and explanations provided intend to clarify the use of the account contributing towards standardisation of allocations in this segment. Consideration has been given to retain the classification used in the “Project” segment for the mSCOA designed for departments for standardisation of information throughout all tiers of government.
4. “Capital” applies to expenditure of “long-term nature” and capitalised to property, plant and equipment in the financial statements. Projects are therefore created along the definition of capital and the detail included under the labels for either infrastructure or non-infrastructure projects.
5. Capital projects relates to spending from the capital budget and thus implying the debit transaction for capitalisation cost within the fixed and intangible asset section of the statement of financial position to the “Construction Work-in-progress Accounts” within the “Item: Asset” segment of the mSCOA Classification Structure. These costs would consist of primary and secondary cost elements qualifying for capitalisation in terms of the supporting Standards of GRAP.
6. At the highest-level capital projects distinguish between infrastructure projects and non-infrastructure projects:
7. Projects are classified in this category if complying with the definition of an “Infrastructure Asset”. Some assets are commonly described as “infrastructure assets” – while there is no universally accepted definition of infrastructure assets, these assets usually display some or all of the following characteristics:
   * + - they are part of a system or network;
       - they are specific in nature and do not have alternative uses;
       - they are immovable; and
       - they may be subject to constraints at disposal.

**Definition form the CIDMS:** Infrastructure Assets

Stationary systems forming a network and serving whole communities, where the system as a whole, is intended to be maintained indefinitely at a particular level of service potential by the continuing replacement and refurbishment of its components.

1. Infrastructure projects provide for existing and new:

**Definitions:**

**Existing:** Capital expenditure on existing infrastructure assets consist of renewal and upgrades.

* Renewal: Expenditure on an existing asset that returns the service potential of the asset or expected useful life of the asset to that which it had originally. Rehabilitation and Refurbishment used in earlier versions up to V5.4 and then replaced with Renewal to align to the CIDMS.
* Upgrading: The replacement of an asset or addition/ replacement of an asset component, which materially improves the original service potential of the asset.

**New:** Projects of a capital nature undertaken to create "new-infrastructure assets" as per definition of an "infrastructure asset".

1. Projects are created along the definition of capital and the detail included under the labels for either infrastructure or non-infrastructure projects.
2. Non-infrastructure project provides for transactions of a capital nature relating to key projects as identified by management such as the procurement of a new bus fleet for use as urban transport but not qualifying as "infrastructure assets" and thus provided for under "projects non-infrastructure".
3. The next level within the above categories (except for land) provides for “Land, Existing and New”. Existing Non-infrastructure make further distinction between “Renewal and Upgrading”.
4. The outline for this group of accounts are summarised in the table below and the accounts discussed in more detail as indicated by references provided.

**Definitions:**

**Existing:** Capital expenditure on existing infrastructure assets consist of renewal and upgrades.

* Renewal: Expenditure on an existing asset that returns the service potential of the asset or expected useful life of the asset to that which it had originally. Rehabilitation and Refurbishment used in earlier versions up to mSCOA V5.4 and then replaced with Renewal to align to the CIDMS.
* Upgrading: The replacement of an asset or addition/ replacement of an asset component, which materially improves the original service potential of the asset.

**New:** Projects of a capital nature undertaken to create "new-infrastructure assets" as per definition of an "infrastructure asset".

1. Default transactions are the classification required to record a transaction within all the segments of the mSCOA. Revenue, assets (excluding capitalised expenditure), liabilities and net assets need to be captured to this account.
2. “Operational projects” refer to current and short-term projects for which the cost is “immediately recognised as an expense and funded from the municipality’s operational budget”.
3. The high-level classification for operational projects is as illustrated below:
4. Operational projects relate to spending from the operational budget and thus implying the debit transaction to the Item classification for the statement of financial performance.
5. Projects need to be set-up as guided by the integrated development plan (IDP) and provide for multi-year spending if required.

**Definitions:**

**Maintenance:** All actions intended to ensure that an asset performs a required function to a specific performance standard(s) overs its expected useful life by keeping it in as near as practicable to its original condition, including regular recurring activities to keep the asset operating, but specifically excluding renewal. Maintenance also specifically excludes restoring the condition or performance of an asset following a recognised impairment event, which would be classified as either renewal or upgrading, depending on the circumstances.

**Municipal Running Cost:** Any other expenditure not relating to a specific project for example general expenses relating to the daily running and operation of the municipality.

**Typical Work Streams:** Projects are created under this group for “operational projects” for example agricultural projects, capacity building, training and development, spatial planning, etc. Typically, these “projects” consist of various expense-items contributing to the outcome or objective of an initiative. Default projects are included for guidance, but the Municipality could expand these as considered necessary.

**Infrastructure Projects:** Infrastructure projects undertaken by the District Municipality on behalf or for the Local Municipality/ National or Provincial Government.

1. The outline for this group of accounts is summarised in the table below:

**Definitions:**

**Preventative Maintenance:** Maintenance carried out at predetermined intervals, or corresponding to prescribed criteria, and intended to reduce the probability of failure or the performance degradation of an item. Preventative maintenance is planned or carried out on opportunity.

* Interval Based: Maintenance carried out at predetermined intervals.
* Condition Based: Maintenance carried out based on prescribed criteria.

**Corrective Maintenance:** Maintenance carried out after a failure has occurred and intended to restore an item to a state in which it can perform its required function. Corrective maintenance can be planned or unplanned.

* Planned: Corrective Maintenance Planned
* Emergency: Corrective Maintenance Emergency.

1. Municipal Running Cost - Operational cost typical to the day-to-day running of the municipality, for example cleaning of office buildings, security, administrative staff cost, building rental, telephone, stationery, postage, etc.
2. Typical Work Stream Projects - Projects are created under this group for “operational projects” for example agricultural projects, capacity building, training and development, spatial planning, etc. Typically, these “projects” consist of various expense-items contributing to the outcome or objective of an initiative. Default projects are included for guidance but the municipality could expand these as considered necessary.
3. MFMA Circular 58 - Municipal Budget Circular for the 2012/13 MTREF provides guidance on free basic services versus revenue cost of free services as provided for in Table A10 of the Budget Reform Returns.
4. In Table A10 municipalities are required to provide information on (i) the estimated cost of free basic services and (ii) the estimated revenue cost of free services.
5. The estimated cost of free basic services:
   * + - Covers only the free basic services according to national policy, for example 6 kl water, 50 kWh electricity, free sewerage and free weekly refuse removal;
       - Must be the actual cost to the municipality and not the revenue cost to the municipality of providing these services;
       - Includes the actual cost to the municipality of providing the free basic services to all households (which would be reflected as ‘revenue foregone’ on SA1); and
       - Includes the actual cost to the municipality of providing free basic services to targeted households (which would be reflected as ‘transfers and grants’ on SA21).
6. The estimated revenue cost of free services:
   * + - Covers all rates rebates, exemptions and discounts given to households and other customer groups either in general or specifically;
       - Covers all free services or service discounts given to households and other customer groups in relation to services for which the municipality normally charges;
       - Must be the revenue cost to the municipality of providing these rebates, discounts and free services;
       - Includes the revenue cost to the municipality of providing the free basic services to households according to national policy; and
       - Must not include the cost of debt write-off.
7. This group of accounts was previously included as “Contra Accounts” within the Item Segment Revenue and Expenditure for the purpose of including the budgeted and actual information within the mSCOA Classification Structure. The initial views on recording the underlying information in mSCOA created confusion. Subsequently the mSCOA Project Steering Committee approved the recommendation to consider the recognition of transaction values in this classification to be a movement from “municipal running cost”.
8. Revenue Cost of Free Basic Services - Covers all rates rebates, exemptions and discounts given to households and other customer groups either in general or specifically. Covers all free services or service discounts given to households and other customer groups in relation to services for which the municipality normally charges. Must be the revenue cost to the municipality of providing these rebates, discounts and free services and includes the revenue cost to the municipality of providing the free basic services to households according to national policy and must not include the cost of debt write-offs. Entry: debit cost of free basic services (expenditure), credit transfers households.
9. Cost of Free Basic Services - Covers the free basic services according to national policy, for example 6 kl water, 50 kWh electricity, free sewerage and free weekly refuse removal. Must be the actual cost to the municipality and not the revenue cost to the municipality of providing these services. Refer to the operational cost for the equal deduction for cost of free basic services.
10. At the highest level the mSCOA classification for “Property Rates Rebate” consists of the following posting-level accounts:

## Regional Indicator Segment (Project Detail Document Section 5)

1. National Treasury introduced the regional indicator on 1 April 2008 with the re-implementation of the SCOA for Departments. As part of the budget reform process and for purposes of evaluating resource allocations in government, National Treasury started to monitor the allocation of resources and actual spending at a regional level. The aim was to capture details of national and provincial government resource allocation and spending at the regional level.
2. As directed by the *Position Paper: Reporting* attention will be given in Phase 2 of the report development process on specific reporting requirements to provide emphasises on regional indicators. The local government budget reform process will further expand on the regional indicator to monitor resource allocation and spending at the local sphere of government along the same design principles for national and provincial government. This perspective is not fully provided for by the analysis of the “Function” and “Item” segments in mSCOA.

Communities need to feel and see delivery, only through planning and physical delivery can this be communicated effectively.

1. The Service Delivery and Budget Implementation Plan (SDBIP) details the implementation of service delivery and the budget for the financial year, in compliance with the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA). The SDBIP serves as a contract between the administration, the Council and the community; expressing the objectives set by the Council as quantifiable outcomes that can be implemented by the administration over the next twelve months. The SDBIP facilitates the process of holding management accountable for their performance. It provides the basis for measuring performance in the delivery of services.
2. The MFMA requires the following to be included in the SDBIP of a municipality:
   * + - The monthly projection of each source of revenue earmarked for collection;
       - The monthly projection of each vote’s expenditure (operating and capital) and revenue;
       - The quarterly projection of each vote’s service delivery targets and performance indicators;
       - The information on expenditure and service delivery in each ward; and
       - The detailed capital works plans allocated by the wards over three years; etc.
3. The MFMA requires the Municipality to compile a SDBIP for submission to the Executive mayor. MFMA Circular No. 13 further states that “…. Being a management and implementation plan (and not a policy proposal), the SDBIP is not required to be approved by Council”.
4. The Regional Indicator segment provides the mechanism for classifying municipal transactional information according to “regional indicators” for reporting in terms of the MFMA on planned and actual capital and operational expenditure on a “ward basis” in the SDBIP.
5. In addition to the SDBIP requirements, one of the key outcomes envisaged with the mSCOA Classification is the ability to extract information on financial performance/ position from the transactional database at the lowest geographical level, being wards.
6. The Regional Indicator segment facilitates the planning and recording of municipal expenditure, revenue, assets, liabilities and net assets at the lowest relevant geographical level (ward). Classification at this level provides information on communities specific to:
   * + - Spending on capital and operational projects;
       - Contributions made towards the SDBIP by the community by paying municipal bills; and
       - Projects directed towards providing indirect benefits to the community, for example local economic development, improvement of living (health, food, housing, services); etc.
7. “The lowest relevant geographical region is depicted in this Segment as “regional indicators”. Similar communities are defined based on the geographical region and represented in the mSCOA Regional Indicator segment by “regional indicators”.
8. This implies that all transactions must be recorded so that the final impact of spending, revenue collections, capital investment and wealth creation can be measured by regional indicator in order to get a geographical view of the economic impact of government activities that are focussed on beneficiaries.
9. It is envisaged that this information will enable and support enhanced analysis of:
   * + Whether services are being provided impartially, fairly, equitably and without bias, as required by the Constitution;
     + Whether progress is being made in addressing regional backlogs in social infrastructure and the access to services;
     + Whether government spending by different departments and municipalities are being properly sequenced and coordinated; and
     + Whether actual spending by government is aligned to the relevant plans of the three spheres of government; etc.

The information will also:

* + - Assist councilors and mayors to account to the communities for resources allocated and actual spending of the municipality to communities and wards; and
    - Provide specific ward information to councilors to assist in decision-making; etc.

1. At the highest level the segment structure distinguishes between “Default and Regional Identifier”. Regional Identifier consists of National/ Provincial Functions, followed by Local Government per Province:

**Definition:**

**Default:** This classification is used for the recording of transactions not relevant to this segment.

**Regional Identifier:** This classification provides “regional” indicators, in order to distinguish at the highest-level between National/ Provincial Functions and Local Government by Province.

* National Functions: This is the posting level for all transaction made within the borders of the Republic of South Africa of which the “whole of the country” is the beneficiary.
* Provincial Functions: This is the group of accounts providing for posting levels for the nine provinces. Transactions providing benefit to the community within the whole of the province is reflected at this level.
* Local Municipality: Municipalities within the District Municipality’s demarcation.

1. The “Default” label provides for the recording of transactions not contributing to a regional indicator. Subsequent to the revision of transactions to be allocated in this Segment (explained in the discussion of this segment), being a requirement for the implementation of mSCOA V6.1, the use of this account may be limited. As part of the maintenance of the mSCOA Tables the relevance of this account will have to be reassessed.
2. The core-principle of assigning transactions in line with the purpose of the Regional Indicator segment is: “to identify the lowest relevant geographical regional indicator of the intended beneficiaries/ contributor of the service”.
3. It is important to note that the location of the service provider is not relevant when it comes to capturing information in relation to the regional indicator, for example consider a payment that is made by a municipality in the Eastern Cape to a service provider situated in Gauteng for the supply of chemicals for a water treatment works. In this instance the regional indicator will not be Gauteng, where the supplier is located but the region or ward or whole of the metro/ district/ local municipality benefiting from the water treatment works.
4. At the highest-level a distinction is made between national and provincial functions; and in Local Government by Province. Agency Services defined within Item: Revenue for Agency Services provided on behalf of National Departments specifically require allocation to this indicator, as well as the cost incurred by the municipality for providing this service.
5. The Provincial Function category provides for recording transactions having an impact on the province within which the municipality resides. Agency Services defined within Item: Revenue for Agency Services provided on behalf of Provincial Departments specifically require allocation to this indicator as well as the cost incurred by the municipality for providing this service.
6. Municipalities are arranged according to their respective provinces in this category of the segment. Distinction is made by province between “metros and district municipalities” according to the list, names and numbering system used by the Demarcation Board.
7. The classification structure provides for all “district municipalities” within the specific province. The regional indicators specific to district municipalities provides for “Administrative or Head Office, Whole of the Municipality and Regions”.

**Definition:**

**Administrative or Head Office:** Transactions directly relating to the administration of the district municipality and not to the direct benefit of the community.

**Whole of the Municipality:** Services provided benefiting the whole of the district where detailed information is not available to allocate to the lower levels.

**Regions:** Providing for district municipalities to classify transactions specifically for local municipalities within the district.

1. In addition to the above noted regional indicators the municipalities within the district are provided with posting level accounts for “Administrative or Head Office, Wards or Regions (per information received from municipalities) and Whole of the Municipality”.
2. Flexibility is allowed to give justice to the respective size of the municipality, sophistication of system application and the logistical arrangements in place at a municipality.
3. The classification structure provides for all “metros” within the specific province. The regional indicators specific to metros provides for “Administrative or Head Office, Whole of the Metro and Regions/ Ward”.
4. Wards are to be included by province and municipality according to the Demarcation Board Classification for 2016. Recognition is given to the fact that these boundaries might change according to the demarcation done for municipal elections every 5 years.
5. An alternative to using “ward” may be to use the logistical area defined by the municipality for providing services to the community.
6. Flexibility is allowed to give justice to the respective size of the municipality, sophistication of system application and the logistical arrangements in place at a municipality.

## Item Segment – Introduction (Project Detail Document Section 6)

1. The decisions that are taken by users of financial statements require an evaluation of the ability of the municipality to implement sustainable service-delivery as informed by the timing and certainty of the service delivery.
2. Information about the financial performance of the municipality provides an account of stewardship of management and is useful in assessing the past and anticipated financial performance of the municipality. Information about variability of financial performance is important in this respect.
3. Information about financial performance is useful in holding management accountable for the safekeeping of the municipality’s resources and for the proper and efficient use thereof. It is also useful in forming judgements about the effectiveness with which the municipality might employ additional resources.
4. The financial position of the municipality is affected by the resources it controls, its financial structure, its liquidity and sustainability, and its capacity to adapt to changes in the environment in which it operates.
5. Information about the resources controlled by the municipality and its capacity in the past to modify these resources is useful in predicting the ability of the municipality to sustain its service-delivery in the future. Information about financial structure is useful in predicting future financing and borrowing needs; it is useful in assessing the municipality’s ability to raise further finance. Sustainability refers to the ability to continue to provide the services in the longer term.
6. The liquidity and sustainability of a national or provincial department is very much dependent on their budget allocation. Their financial position is therefore primarily affected by the budget whereas a municipality relies largely on their own revenue in the form of rates and taxes and other service charges.
7. Information concerning changes in the cash flows of the municipality is useful in order to assess its investing, financing and operating activities during the reporting period.
8. This information is useful in providing the user with a basis to assess the ability of the municipality to generate cash and cash equivalents and the needs of the entity to utilise those cash flows.
9. Information about financial position is primarily provided in a statement of financial position. Information about financial performance is primarily provided in a statement of financial performance. Information about cash flows is provided in the financial statements by means of a statement of cash flows. Changes in the residual (after deducting liabilities from assets) are provided in the statement of net assets.
10. The component parts of the financial statements interrelate because they reflect different aspects of the same transactions or other events. Although each statement provides information that is different from the others, none is likely to serve only a single purpose or provide all the information necessary for particular needs of users. For example, a statement of financial performance provides an incomplete picture of financial performance unless it is used in conjunction with the statement of changes in net assets and the statement of cash flows.
11. The Item Segment of SCOA consists of four parts being:
    * + - Revenue [Section 6.1]
        - Expenditure [Section 6.2]
        - Gains and Losses [Section 6.3]
        - Assets, Liabilities and Net Assets Section [6.4]]
12. At the highest-level, the Item Segment supports the reporting done in terms of the budget reporting format and annual financial statements. The detail levels in this segment provide the more detailed information presented in supporting schedules and notes to the budget reporting format and annual financial statements.
13. This project resulted in alignment between the budget reporting format and annual financial statements that will greatly assist the reporting on budgeted versus actual information.
14. Important to note is that the accounting policies, methodologies and principles applied in determining budgetary information need to be consistent to those applied in preparing annual financial statements.
15. The components to the Item Segment are discussed in separate sections in the body of the sections.
16. The use of the information collected through the standard classification process is not confined to budget and annual financial statements but need to address the needs of a wide group of users of local government information.
17. Consultation with various users took place throughout the research and development phase resulting in populating the charts to assist in extracting required information.
18. The expansion of detail within the mSCOA will continue as more “users” appreciate the value from this process. Standardisation of classifications adds immense value to the quality of information and consistency in reporting.
19. Because municipal functions and activities vary and consequently transactions and other events differ in terms of the impact on its ability to meet its service-delivery obligations, disclosing the components of financial performance assists in an understanding of the financial performance achieved and in making projections of future results.
20. Additional line items are included on the face of the statement of financial performance, and the descriptions used and the ordering of items are amended when this is necessary to explain the elements of performance.
21. Factors considered include materiality and the nature and function of the components of revenue and expenses.

## Item Segment – Revenue (Project Detail Document Section 6-1)

1. This component of the Item segment contains the classifications structure for revenue to inform the extraction of reporting information in various formats, for example the Budget Reporting Tables, In-year Reporting, Annual Financial Statements, the NERSA Regulatory Reporting Tables, the Department of Water Affairs reporting requirements, etc.

**Definition:**

The gross inflow of economic benefits or service potential during the reporting period when those inflows result in an increase in net assets, other than increases relating to contributions from owners.

1. The surplus attributable to minorities; surplus contributed from associates and joint ventures are not “revenue”; however by definition these are included in this component. By definition “revenue” includes “gains”. The mSCOA Classification provides for “gains” within the component of the Item Segment for “Gains and Losses”.

**Definition:**

The key question in finding the appropriate classification code for this segment is: *“what is the type and nature of the revenue accrued?”*

1. The illustration of the high-level classification structure for this segment directly relates to the main classifications required in the Statement of Financial Position in accordance with the requirements of the *Standards of GRAP 1 Presentation of Financial Statements*.
2. At the highest level thiscomponent distinguishes between:

## Item Segment – Expenditure (Project Detail Document Section 6-2)

1. This component of the Item segment contains the classifications structure for expenditure to inform extracting reporting information in various formats, for example the Budget Reporting Tables, In-year Reporting, Annual Financial Statements, the NERSA Regulatory Reporting Tables, the Department of Water and Sanitation reporting requirements, etc.

The key question in finding the appropriate classification code for this segment is: “what is the type and nature of the expenditure incurred”

1. At the highest level this component distinguishes between:

**Definition:**

Expenses are decreases in economic benefits or service potential during the reporting period in the form of outflows or consumption of assets or the incurrence of liabilities that result in decreases in net assets, other than those relating to distributions to owners.

## Item Segment – Gains And Losses (Project Detail Document Section 6-3)

1. The *Standards of GRAP 1 Presentation of Financial Statements* determines that gains and losses arising from a group of similar transactions are reported on a net basis, for example, foreign exchange gains and losses and gains and losses arising on financial instruments held for trading. Such gains and losses are, however, reported separately if they are material.
2. Accounts are defined within this component of the “Item” Segment, based on the above requirements from the Standard of GRAP. Accounts defined give consideration to separate reporting whether material or not. Consideration will be given to the separate disclosure of gains and losses if material in the setting up of reporting information and how this type of transaction will be dealt with in the preparation of annual financial statements.
3. The definition of revenue includes both revenue and gains. Revenue arises in the course of the operating activities of the municipality, and includes the items presented in “Item” Segment: Revenue. However, gains are categorised in this component separate from revenue. The classification of accounts within the components of the “Item” Segment does not drive the presentation in the budget reporting tables, in-year reporting and annual financial statements.
4. Gains represent other items that meet the definition of revenue and may, or may not arise in the course of the operating activities of the municipality. Gains represent increases in economic benefits or service potential and as such are no different in nature from revenue.
5. Gains include for example those arising on the disposal of non-current assets. The definition of revenue also includes unrealised gains; for example, those arising on the revaluation of financial instruments and those resulting from increases in the carrying amount of long-term assets.
6. When gains are recognised in the statements of financial performance or the statement of changes in net assets, they are usually displayed separately, because knowledge of them is useful for the making of economic decisions.
7. The definition of expenses encompasses losses as well as those expenses that arise in the course of the operating activities of the entity. Expenses that arise in the course of the operating activities of the entity include, for example, cost of sales or cost of services rendered, wages and depreciation refer to the “Item” Segment: Expenditure. They usually take the form of an outflow or depletion of assets such as cash and cash equivalents, inventory, property, plant and equipment. However, losses are categorised in this component separate from expenditure. The classification of accounts within the components of the “Item” Segment does not drive the presentation in the budget reporting tables, in-year reporting and annual financial statements.
8. Losses represent other items that meet the definition of expenses and may, or may not, arise in the course of the operating activities of the entity. Losses represent decreases in economic benefits or service potential and as such, they are no different in nature from other expenses.
9. Losses include for example those resulting from disasters such as fire and flood, as well as those arising on the disposal of non-current assets. The definition of expenses also includes unrealised losses, for example, those arising from the effects of increases in the rate of exchange for a foreign currency in respect of the borrowings of the municipality in that currency.
10. When losses are recognised in the statement of financial performance, they are usually displayed separately because knowledge of them is useful for the making of economic decisions. Losses are often reported net of related revenue to reflect the substance of the transaction or event.
11. Expenses are decreases in economic benefits or service potential during the reporting period in the form of outflows or consumption of assets or the incurrence of liabilities that result in decreases in net assets, other than those relating to distributions to owners.
12. At the highest-level “gains and losses” provided for the following groups of accounts:

**Definitions:**

**Gains and Losses:** Gains and losses are treated as a separate group of accounts due to the nature of these transaction. Gains arise from the proceeds of the transaction exceeding the recognised value and losses from the recognised value exceeding the proceeds realised from the transaction.

**Discontinued Operations and Disposals of Non-Current Assets:** The gain or loss recognised on the measurement to fair value less costs to sell or on the disposal of the assets or disposal group(s) constituting the discontinued operations. [GRAP 100.35(b)(iv) and .22 to .27]

**Disposal of Fixed and Intangible Assets:** The gain or loss arising from the derecognition of an asset determined as the difference between the net disposal proceeds, if any, and the carrying amount of the asset. It shall be recognised in surplus or deficit when the asset is derecognised.

**Fair Value Adjustment:** The loss arising from the change in the fair value of a financial asset or liabilities measured at fair value recognised in surplus or deficit. Included in this account would be loss on financial instruments and discounting of debtors.

**Foreign Exchange:** This item is for the recognition of a gain/ loss incurred in foreign exchange transactions.

**Impairment Loss:** Impairment is a decrease in the value of an asset to an amount that is less than the amount under the cost basis.

**Reversal of Impairment Loss:** Reversal of impairment losses recognised in surplus/ deficit in accordance with the Standards of GRAP on Impairment of Non-cash-generating Assets and Impairment of Cash-generating Asset. [GRAP103.83(c)]

**Inventory:** The amount of any write-down of inventories to net realisable value and all losses of inventories shall be recognised as an expense in the period the write-down or loss occurs.

**Water Losses:** Water losses are calculated as the difference between the system input volume and the authorised consumption. Water losses are broken down into commercial or apparent and physical or real losses.

## Item Segment – Assets, Liabilities and Net Assets (Project Detail Document Section 6-4)

1. The content of the Item Segment – Assets, Liabilities and Net Assets is presented in different tables due to the size and detail contained in the respective spreadsheets and should still be seen as a single segment. The components making up the Item Segment presented in the mSCOA Tables are:
   * + - Assets;
       - Liabilities; and
       - Net Assets.
2. The financial position of the municipality is affected by the resources it controls, its financial structure, its liquidity and sustainability, and its capacity to adapt to changes in the environment in which it operates. The Item Segment with its components for assets, liabilities and net assets hosts the classification structure for providing this information.
3. The sequence of accounts depicted in the code structure defined in the mSCOA Tables does not indicate the order or format in which items are to be presented in the annual financial statements, resulting in a contradiction to the presentation requirements provided for in the Standards of GRAP 1**[[3]](#endnote-1)**.
4. In addition, the requirement to apply judgement on whether additional items are separately presented based on an assessment of the nature and liquidity of assets, the function of assets within the municipality; and the amounts, nature and timing of liabilities does not change at the implementation of mSCOA.
5. Illustrative Financial Statements will be prepared as part of the project deliverable to provide guidance on linking the mSCOA accounts to the financial statement presentations.
6. The illustration of the high-level classification structure for this segment directly relates to the main classifications required in the Statement of Financial Position in accordance with the requirements of the *Standards of GRAP 1 Presentation of Financial Statements*.
7. The determination on classifying assets and liabilities as current or non-current need to be guided by the requirements set-out in the above Standard of GRAP read with any other requirements set-out in a Standard of GRAP. The definitions provide brief explanations in the context of mSCOA, but might not be sufficient in determining the current versus non-current classifications.

**Definitions:**

**Assets:** Assets are resources controlled by the municipality as a result of past events and from which future economic benefits or service potential are expected to flow to the municipality.

**Current Assets:** An asset shall be classified as current when it satisfies any of the following criteria:

(a) it is expected to be realised in, or is held for sale or consumption in, the entity’s normal operating cycle;

(b) it is held primarily for the purpose of being traded;

(c) it is expected to be realised within twelve months after the reporting date; or

(d) it is cash or a cash equivalent asset (as defined in the Standard of GRAP on Cash Flow Statements) unless it is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting date.

**Non-current Assets:** All other assets not classified as current according to the definition above shall be classified as non-current.

**Liabilities:** Present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits or service potential.

**Current Liabilities:** A liability shall be classified as current when it satisfies any of the following criteria:

(a) it is expected to be settled in the entity’s normal operating cycle;

(b) it is held primarily for the purpose of being traded;

(c) it is due to be settled within twelve months after the reporting date; or

(d) it does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting date. (Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification).

**Non-current Liabilities:** All other liabilities not within the above definition shall be classified as non-current

**Net Assets:** The residual interest in the assets of the municipality after deducting all its liabilities.

1. The Project Document to contain a section on VAT and how the SCOA Classification will assist in complying with the requirements in submitting VAT 401 to SARS. [↑](#footnote-ref-1)
2. The detail of this reporting requirements to be taken-up in the SCOA Project Document for the sake of completeness. [↑](#footnote-ref-2)
3. The *Standards of GRAP 1 on the Presentation of Financial Statements* requires that the municipality presents current and non-current assets, and current and non-current liabilities, as separate classifications on the face of its statement of its financial position except when a presentation based on liquidity provides information that is reliable and more relevant. When that exception applies, all assets and liabilities shall be presented broadly in order of their liquidity. [↑](#endnote-ref-1)