



Thabani Zulu & Co

CHARTERED ACCOUNTANTS (SA)

The Accountant

ADDRESSING THE CHALLENGES OF FINANCIAL MANAGEMENT
AND PLANTING THE SEED FOR GOOD GOVERNANCE

The public service is challenged by financial administration issues. These extend from inaccurate financial reporting that leads to inappropriate decisions, to delayed reporting which makes the very decisions inefficient.



▶ DEFINING FINANCIAL MANAGEMENT



▶ THE ROLE OF A CHIEF FINANCIAL OFFICER



▶ INCULCATING A CULTURE OF FINANCIAL DISCIPLINE

▶ WHAT IS THE REAL MEANING OF AN EXTERNAL AUDIT AND
HOW SHOULD WE INTERACT WITH THE REPORT

REWARDS SCHOOL OF BUSINESS



Rewards School Of Business is a training school operating as a subsidiary of Thabani Zulu and Company. The school was set up to respond to the dire shortage of skills in South Africa particularly in Financial Management and Governance. With full accreditation the school offers courses in Corporate Governance, Risk Management, Forensic Auditing and Financial Management. For more information and to make bookings to attend one of Rewards School of Business exciting courses visit www.rsob.co.za



Partnering on financial governance



Thabani Zulu & Co

CHARTERED ACCOUNTANTS (SA)

Thabani Zulu CA(SA)
Managing Partner and Editor
Thabani Zulu and Company Chartered
Accountants SA

Thabani Zulu And Company has realized that there is a need to develop skills in our business community, particularly in the areas of Financial Management, Risk management and Governance. If we continue to deny that there is a serious vacuum in these areas, and if we continue not to do anything about it, we will fail our nation. It is for this reason that we have conceptualized and designed this publication. We intend for it to be FREE to you as the reader and be as informative as you may require.

The publication will be issued every quarter, with this being the very first issue. It will contain stimulating and provocative discussions that are aimed at causing leadership, the business community and administrators to do things a little differently. If we maintain the status quo we will continue to get the results we have always been getting. We need to challenge ourselves for change.

The Accountant is a Thabani Zulu and Company concept and publication. We are THE ACCOUNTANT. With vast experience in the fields that we will be discussing, we believe that, through this publication, we will impart knowledge. We have designed a series of courses that will be driven through our subsidiary company, REWARDS SCHOOL OF BUSINESS. We are proud that we have finally got this off the ground and ready to offer the stimulating and insightful ground-breaking courses to you. Those who have experienced the touch of Thabani Zulu and Company will have a sense of the quality of the accredited material that Rewards School of Business has to offer.

To strengthen our offering, Thabani Zulu has been joined by Thando Radebe as a Partner in the firm and CEO of Rewards School of Business. With her passion for empowerment and education, matched with

her experience, Thando is arguably the best to take Rewards School of Business to greater heights.

About this issue of THE ACCOUNTANT

This issue focuses on the financial administrative and reporting challenges that currently face the public administration. The current legislated framework suggests that for municipalities with a year end of June, financial statements must be finalized and submitted for audit by the end of August and the publication to be made by the end of October, literary four (4) months after the end of the year.

Kumba Iron Ore, with a year end of 31 December and a revenue of some R48 Billion in 2011 had a set of financial statements finalized, audited and signed of by the 7th of February the following year. The JSE has a requirement of 3 months for listed entities to report on their audited financials. With such complexities in their operations, we need to ask ourselves how they manage to achieve this. Many have operations around the globe, yet they manage to conform to the JSE requirements.

If we are to achieve the levels of competency and efficiency, we need to interact with these counterparts and seek answers to how what we believe to be a mammoth task is reasonably achievable.

“Kumba Iron Ore, with a year end of 31 December and a revenue of some R48 Billion had a set of financial statements finalized, audited and signed of by the 7th of February the following year. “

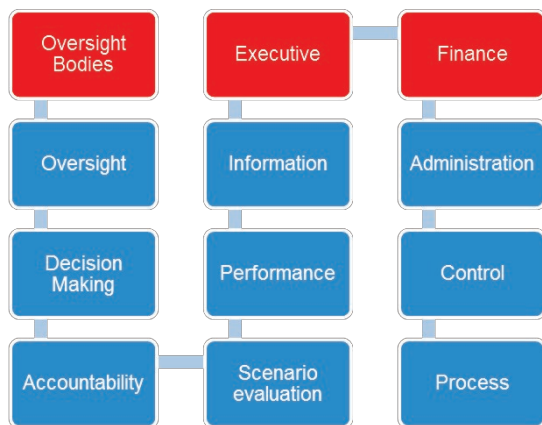
Defining Financial Management

Thinking that management can remove themselves from financial management and leave it to CFO's is a fallacy. It's greater the responsibility of Line Managers than that of Chief Financial Officers

There are numerous myths about what financial management is or is not. Many have resulted in significant collapse of municipalities in South Africa. This document seeks to demystify certain of these myths and put better perspective into what financial management is and how it can be effected in our public administration. We are, in this document, also proposing solutions, directly and indirectly, on how our administration can improve its financial management capabilities.

lies with the management of these finances. If they delegate this to the CFO, they are delegating their critical management responsibility. They are charged with the responsibility for service delivery and they are equipped with the budget to ensure that this responsibility is properly discharged. A fundamental question is, if they are not in control and command of their budget, how are they in control of their service delivery responsibilities.

What is Financial Management



From the diagram above, one can conclude that financial management is the art of the entire organization from:

1. the non executive and governance structures, i.e. council and other council committees to
2. the executive management that are charged with service delivery, to
3. the financial process owners that are responsible for administration and systems of internal control.

If there is a weak-link among these role players, financial management will collapse in a municipality. Each needs to be mindful of their role, must be equipped with tools and knowledge to fulfill their responsibilities and must be available when needed to fulfill such responsibilities.

Myth 1: Financial management is an art of a Chief Financial Officer

This has reduced a mammoth responsibility of oversight bodies and general management into the hands of the CFO's. Whilst they have a responsibility to ensure that financial management is properly advanced in their institutions, through efficient administration, sound systems of financial control and effective reporting, the ultimate role of managing finances

Myth 2: Oversight is limited to administration

One sees this at play when it comes to interrogation of the reports by oversight bodies such as council and audit committees. The questions and the focus moves away from accountability, oversight and decision making into whether the process was followed to engage the services of an external provider; to whether the annual financial statements were qualified by the Office of the Auditor – General; to why there was irregular expenditure and why it was not condoned in terms of the process.

Whilst these questions are relevant, they are administrative in nature. Strictly speaking, with effective financial administration, these questions should not even be asked in the first place. They send municipalities backwards in terms of their maturity in financial management and they reduce the relevance of the oversight bodies.

Questions that one would expect from oversight are service delivery questions. Finance, through reporting, gives impetus to these questions. Questions such as what does it mean to a citizen that the conditional grant is only 10% spent? to why is the municipality spending at this level per housing unit? To how much of the budget of the municipality is consumed by administration and how can administration be streamlined to veer the budget into service delivery?

Famous money quotes:

“Early to bed, early to rise, keeps you healthy, wealthy and wise” - Benjamin Franklin

“A penny saved is a penny earned” - Benjamin Franklin

“If you want to know what God thinks about money, just look at the people He gives it to” - Dorothy Parker

Myth 3: Financial Management equals an unqualified audit report

Without rendering audit as an ineffective tool to financial management, it has unfortunately been used as a panacea to financial management woes of municipalities. A simple test would be to review service delivery measures of municipalities against the reports from external audit. Before even conducting that exercise, one must put an external audit into perspective in so far as financial management is concerned.

Typically, an external audit seeks to answer a question whether the municipality's annual financial statements fairly present the status of performance, position and cash flows of the reporting municipality. An audit would not answer the question whether the same numbers could have been improved or whether delivery on the ground coincides with these numbers and could have improved given the numbers. In its technical configuration, an audit is an effective tool to ensure effective administration and not management.

Myth 4: Financial Management is a complex, technical issue

There is a mystery that has been created in local government about financial management. The reality is that financial administration is complex and is a science. It has been made even more complex by the creation of accounting standards and alignment with international financial administration and reporting. That has made the administration of public funds a complex issue and calls for sound financial administrators or Chief Financial Officers.

The complexities around financial management are fundamentally caused by weaknesses in the Chief Financial Officers themselves. An effective CFO must be able to identify and profile the users of financial information, the decisions that they intend or are tasked to make and their oversight responsibilities over municipalities' administration and service delivery processes and package the financial material against those requirements.

If one studies the financial reporting templates currently used by local authorities and imposes them on the technical skills in financial administration and management of the executive and oversight bodies, one can only conclude that they leave much to be desired. They are hugely effective when consumed by technical people, i.e. National and Provincial Treasuries and auditors but are extremely confusing to other critical bodies that are charged with oversight and accountability in municipalities. If one expected these structures to be relevant and meaningful, one should be able to repackage this technical information to their level of understanding and responsibility. This is a function of a meaningful Chief Financial Officer.

Myth 5: Financial Management equals compliance

Municipalities have been reduced to engines of state that must simply comply and demonstrate that they have complied with the set policies, prescripts and procedures laid out by various structures in government. Financial management has been reduced to presentation of reports in set templates by specific set times.

Again one does not wish to downplay this compliance mindset as it is critical in ensuring proper and procedural administration. However, it has created a culture of compliance and not financial management. Oversight structures are more concerned with whether a report has been sent to national treasury rather than what that report was actually saying. The public administration has moved into a "tick the box" syndrome rather than a management obligation.

The challenge of an effective Chief Financial Officer is to ensure that compliance is achieved and maintained whilst creating a culture and an enabling environment for financial management to take effect. A greater concern should be presenting and allowing for decisions and oversight to

We pride ourselves with practical solutions

Let the waves of Thabani Zulu and Company demystify all challenges that you face in your organization. We have a proven track record with municipalities and other organisations in turning these challenges into opportunities.

Why don't you let your municipality be among the best and be used as a benchmark for excellence.

We have tools, resources and systems to turn your organization around.

Make a call on 031 2661811 or email chairman@tzulu.co.za to see change.



Thabani Zulu & Co

CHARTERED ACCOUNTANTS (SA)

The Role of a Chief Financial Officer

The Chief Financial Officer is an integral part of the organisations financial administration and management. How can be this function be discharged. We explore the dynamics of the CFO's roles and responsibilities in ensuring sound financial governance

Dismissing this upfront; a CFO is *not* a Financial Manager. A CFO is an enabler for financial management to take effect in an organization. The test of his effectiveness is on the capacity of the organization to take meaningful financial decisions. As a matter of course, finances follow strategy and operations, therefore, an effective CFO is one with a capacity to present financial information alongside operational and strategy imperatives of the municipality. If this is not properly done there will be a constant misalignment between councils strategic intentions, management imperatives and the financial resources available to achieve these. A meaningful CFO puts all these into meaningful perspective.

Without venturing into the responsibilities and duties of a Chief Financial Officer, it is necessary to note that when the CFO prepares a budget, creates management accounts and ultimately presents annual financial statements, this is to enable the decision makers, executives and oversight bodies to react on their operations in order to achieve a state of financial soundness. One therefore expects that the CFO's initiatives are:

“The capacitation of the Chief Financial Office, inculcation of a culture of financial discipline throughout the organization and effective and efficient financial reporting that is reliable and adequately timed are key responsibilities of a Chief Financial Officer”

1. Performed speedily to allow for decisions to take effect early enough,
2. Accurate to enable to relevant decisions to be taken,
3. Precise to eliminate clutter in financial reports and achieve meaningful focus,
4. Insightful to enable users to dissect the organisation's financial and operational landscape and identify the effects of the decisions they intend to make, and
5. Coordinated with line management.

It then follows that if the CFO is aiming at creating an environment where proper decision making and oversight is facilitated, then his administration must be sound and efficient. The systems of internal controls and procedures must enhance his capacity to report accurately and reliably. The segregation of duties and authorization controls must be effective to cause for proper accountability and validity of transactions that go through his financial administration systems.

Further, the CFO has to design his environment to facilitate for effective and efficient administration. He should put proper checks and balances to determine that transactions that were processed through his financial administration systems are complete, accurate and valid. There is a myriad of transactions that take place in a municipality on a daily, hourly basis and the risk of error or completeness; or simple abuse; is significant. The results will be inadequate oversight or improper decisions being made. The CFO has to guard the organization against this and perform the checks, balances and reconciliations to satisfy himself that the information he ultimately presents is reliable.

The culture in municipalities, in particular, is that Chief Financial Officers exist for the Office of the Auditor – General. It is probably the only entity that is taken seriously, and so it should. The issue is that CFO's should not perform their functions only to escape a qualification at the end of the year, but rather to enable for effective administration and oversight throughout the year. If this is an adopted approach, which we deal with in the next article, an unqualified audit is a foregone conclusion.

The capacitation of the Chief Financial Office, inculcation of a culture of financial discipline throughout the organization and effective and efficient financial reporting that is reliable and adequately timed are key responsibilities of a Chief Financial Officer. Their presence more in the office interacting with their subordinates and line functionaries, development and monitoring systems of internal controls and entrenching a culture of financial discipline will determine his success in this environment.

Chief Financial Officers should resist the temptations of being politicians or operating in political spaces. As much as it is critical to understand the political direction and, in particular, its financial implications, the tendency is to attempt to please the political principals, often to the detriment of the organization and the negative perceptions leveled on the very CFO. One has to ponder how the billions of irregular expenditure on the 2011 annual results of various municipalities in the country arose!!!

Challenges in Financial Management

The following challenges in financial administration, management and reporting within municipalities have been identified through our involvement in a number of consulting and internal audit engagements with municipalities:

Financial Discipline

- Lack of month end discipline resulting in month end closure not performed, critical month end reconciliations not performed, inability to identify completeness of recording of transactions, and inability to report meaningfully to the municipal structures on financial performance;
- Poor record management resulting in difficulties in tracing financial records supporting the financial affairs of the municipality;
- Lack of processes to identify and manage unauthorised, irregular and wasteful expenditure;
- Disciplinary steps not taken, even when financial mismanagement is identified,
- Issues raised by the Office of the Auditor General not followed up and cleared on time.

Our observations revealed lack of systems of internal controls to manage assets evidenced by:

- Asset registers not updated when acquisitions, impairments or disposals are made;
- Reconciliations of the asset register to the general ledger not performed;
- Regular verifications of assets to ascertain existence and condition not in place.

A lack of these processes contribute to delays in the submission of financial statements due to difficulties encountered in reconciling general ledger / trial balance to corresponding supporting schedules. Further, the existence of assets can not be ascertained due to a lack of on-going process to verify them.

Skills

Inadequate financial management skills, the ability to develop attract and retain talent at the municipality for effective and efficient financial administration and governance. The following indicators of lack of required skills were identified:

- Lack of knowledge of generally recognised accounting practise at transaction level (i.e. inability to account for financial accounts correctly through basic principle of debit and credit),
- Lack of understanding of the importance of month end closure,
- Lack of understanding of reconciliations and their purpose,
- Inadequate supervision of staff activities,
- Inability to present meaningful monthly management reports and provide sound advice to the council,
- Inability to prepare annual financial statements in accordance with applicable generally recognised accounting standards.



Rewards School of Business

OUR MOTTO

Developing people who are risk-smart, workplace-ready and business-wise.

WHO WE ARE

Rewards School of Business is first and foremost a training institution. Our programmes and preparation are aligned to business and workplace needs. Through our offered courses and our practice-oriented tuition model, a competent player in business will be created; combining technical knowledge, leadership and ethics that are fundamentally needed in the working community.

Our emphasis is in ensuring that directors, personnel and business-owners are educated enough to understand their role in the application of relevant laws, regulations and standards. That they are competent in designing integrated risk management tools and taking steps to implement these tools successfully.

HOW WE STAND OUT

“It’s how we train that sets us apart. You will experience it, too”

- Rewards School of Business (RSOB) is accredited by LGSETA.
- RSOB is an offshoot of the Thabani Zulu & Company Training Department, a firm of Chartered Accountants (SA) established in 2007.
- Our select training programmes are aligned with the unit standards of the South African Qualifications Authority (SAQA).
- Our courses are especially tailored for the socio-economic sector, hence the focus on professional skills development in the Public Sector and enrichment of the SMME sector.
- Our courses are offered both off and on site.
- We boast a complement of highly competent facilitators and qualified assessors.

Challenges in Financial Management

GRAP

National Treasury issued a circular requiring all municipalities across the country to be fully compliant with GRAP accounting standards by 2012,

There is a general lack of requisite knowledge by the finance teams on GRAP requirements. This culminates in:

- An inability to account for financial accounts in line with GRAP accounting standards,
- Reliance on consultants in preparing financial statements in line with GRAP requirements by municipalities already converted from IMFO to GRAP,
- Lack of preparedness by those municipalities still to convert to GRAP requirements,
- Financial systems not geared towards GRAP requirements.

A haphazard expectation that the municipalities will suddenly conform to this requirement is, once again, unrealistic. The standards still pose a major threat to even seasoned professionals in the field of Accounting. Private sector professional firms have fully operational technical divisions that interpret these standards for adequate implementation, precisely because they are a challenge. Such infrastructure is, therefore, necessary in order to enable the municipalities to conform.

Document Management

The Office of the Auditor General continues to raise issues on poor management of financial records by municipalities across the country and hence disclaimers of audit opinions are expressed for a large number of municipalities. Eastern Cape is no exception to this challenge.

- Poor record management continues to be a problem in municipalities resulting in difficulties in tracing financial records supporting the financial reports presented. Further, the non-availability of financial records results in inability to fulfil disclosure requirements as per the prescribed financial statement specimen.
- Lack of month end procedures / reconciliations contribute to inability to identify missing financial records and inability to adopt a systematic filing system for ease of tracing.

We have gained experience, collectively as a firm for the past ten (12) years through various capacities, employment and projects ranging from:

1. Regularity audits as employees of Auditor-General
2. Forensic investigations on behalf of the Department of Local Government and Auditor-General;
3. Consulting engagements at the municipalities on behalf of KZN Treasury and Department of Local Government in various forms:
4. Municipal Financial Capability Assessment;
5. Municipal Financial Improvement/Support Programme;
6. Municipal Recovery Programme;
7. Municipal Support on Supply Chain Management;

OUR PLEDGE

Rewards School of Business is managed by a highly competent Management Board that has a reputation to uphold, and is passionate about, skills development in our society. The goal of the Management Board is to become a meaningful player in the education and training sector through on-going market research and staff development.

We do not aspire to be a “Jack of all trades.” The School is exclusively committed to the development of a risk-smart workforce by strengthening the country’s human resource competencies in the areas of corporate governance, risk management, public finance management and SMME management.

OUR APPROACH

We do not subscribe to a “one-size fits all” formula when delivering our services. Group sizes are customized per course, therefore, ensuring that each customer’s needs are especially catered to. We do not want to play a revenue game at the expense of quality and we avoid creating professionals that will not be useful to the business community whilst we pride ourselves with revenue gains.

YOUR REWARD

Given our training model, clients do enjoy a sustainable benefit of an empowered workforce that can organically shape internal systems without the unnecessary duplication of effort and activity from resources. Practicality is the main focus of Rewards School of Business. Our practice-oriented courses enable attendees to proximately transfer learning into the work environment; and become more proactive in their management style, rather than reactive.

TRAINING DIVISIONS

The School hosts six (6) specialised divisions with a specific focus on the public and SMME sectors. Within each division we have targeted courses designed for specific categories of clientele. The divisions are as follows:

Governance and Leadership
Risk Management
Public Finance Management
Supply Chain Management
Forensics and Internal Audit
SMME Growth Management

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What is the real meaning of an external audit and how should we interact with the report

The following challenges in financial administration, management and reporting within municipalities have been identified through our involvement in a number of consulting and internal audit engagements in the municipalities:

The public sector is exposed to an audit by the Office of the Auditor – General annually. Chief Financial officers run around uncontrollably on the due date of the Annual Financial Statements to make sure that they are submitted on time. They interact in anxiety with the external auditors for about two months and then wait in anticipation for the final outcome. “Is it going to be a Disclaimer or an unqualified audit report; or maybe something in between. Well, in this article we would like to explore what these really mean to an organ of state.

Let us start here: An audit is an expression of the defectiveness or otherwise of the Annual Financial Statements. It seeks to answer a question whether the numbers and disclosures fairly present the state of finances of the organization. It looks at disclosure standards and whether they have been complied with, interrogates transactions for validity, accuracy and completeness and concludes on whether what is sitting on the Annual Financials is indeed a reflection of the financial activities of the organization during the year under review. Traditional and conventional audit methodologies are based on selected samples and, therefore, resulting opinions are based on results from the selected samples. Procedures are not designed, and cannot be, to cover the entire population of transactions for the year.

The Annual Financial Statements speak a bigger language than that of mere fair presentation. They point the organization to areas where they need management focus. An audited decline in rates, for instance points to a potential erosion of the municipality’s revenue base which calls for an immediate intervention. Similarly, a decline in cash resources is a pointer to the capacity to discharge immediate financial commitments and needs urgent action. One may argue that this is a matter for management accounts to reflect and resolve, but a case has been made of the impropriety of the management accounting environment in the public sector, particularly municipalities. Annual Financial Statements reflect this information to the users.

The tendency is to treat the Audit Report as a final stage of success, or failure in the annual life of an organization. The fallacy is that an unqualified audit reflects a well - run organization. The truth is it points to proper administration and not necessarily governance, risk management and leadership. For example, unauthorized expenditure escapes a negative audit report if disclosed in the financials, whatever the quantum. Bad management decisions in the year will not receive a qualification if they are properly recorded and the effects properly disclosed in the financials. Therefore the fact that a report is unqualified has little bearing on the running of the organization and merely forms part of a wider set of indicators for proper management.

Another fallacy is to rank audit reports in the order of importance or significance. Somehow we have formulated that reports rank from:

1. Clean audit (whatever this means) to
2. Unqualified audit opinion, to
3. Qualified (except for) audit opinion, to
4. Adverse audit opinion to
5. Disclaimer of an opinion

The mindset is that organizations that obtain disclaimers are the worst in the pack. They are in intensive care and need all resources to be thrown at them. Similarly those that get a qualification, are not in bad shape. They just require attention on the areas where they got qualifications. The reality is, simply put, a disclaimer says that the auditor cannot make an opinion on the set of financial statements. There was some kind of a limitation on the capacity of the auditor to verify the underlying transactions of the organization. It may be a huge fire that burnt down the records during a strike, or a system that got corrupted and corrupted the transaction data. Whatever the reason, it does not necessarily suggest that the municipality is in dire straits and all must panic and institute administration provisions against it. Whilst the disclaimer is not being undermined, we need to take care that we do not downplay other opinions as they may reflect bigger challenges than a disclaimer of opinion.

In the final analysis, an audit opinion is an enabler to the user to perform an analysis of financial statements that have been independently reviewed. It is not a measure of success or failure, neither is it a final step in the process of financial governance. It provides direction and independent review. It is not conclusive.

Thabani Zulu and Company Supports Youth in Action.

A dynamic youth organization operating throughout KwaZulu Natal, with headquarters at KwaMashu enjoys support from Thabani Zulu and Company.

The Organisation, YOUTH IN ACTION, has developed a series of programs for youth empowerment, ranging from programs to address social ills of pregnancy and substance abuse, to programs of you economic emancipation. The organization is comprised of young men and women who have dedicated their time and energy to try and develop a bright future of capable and ethical leadership.



“We cannot sit back and watch our society decay. Neither can we place this challenge only in the hands of our government. This is our future and, ultimately, we will be affected!

We need to be in charge of our destiny and challenge positively ourselves to a realization of a society that we would like to belong to”, says the President of the Youth In Action, Robert Ndlela.



It is for this very reason that Thabani Zulu and Company will, with limited resources, make all efforts to support this organization and many others that cherish a vision of an ethical nation that realizes that it is only through hard innocent work that we will regain the image and values that our forefathers espoused.

We will not only donate money and walk away. We will spend time with our youth. We will play with them, guide them, engage in their discussions and participate in their programs. Ultimately they are the future of our society. As a firm we made that pledge to this dynamic group of young-stars and with help of all concerned elders, we will contribute to the creation of a nation that we can be proud of.





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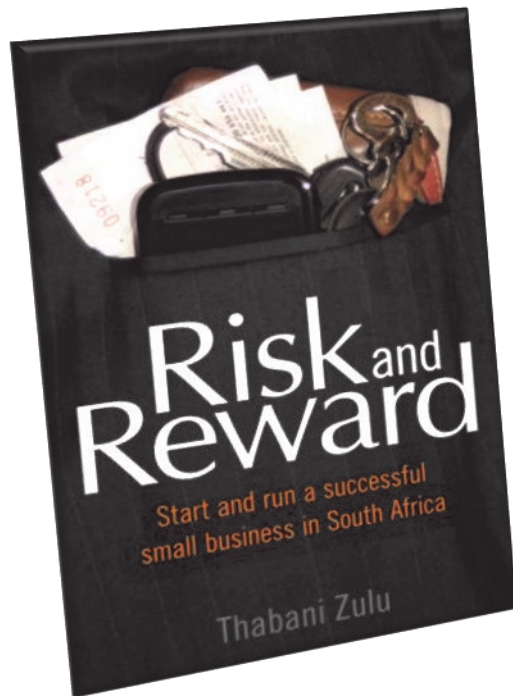
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