Annual Financial Statements 2015/ 2016 Financial Year

Chapter 7

Annual Financial Statements 2015/16 Financial Year

Nketoana Local Municipality
Annual financial statements
for the year ended 30 June 2016

Nketoana Local Municipality
Annual Financial Statements for the year ended 30 June 2016

General Information

Legal form of entity	Local Municipality Demarcation number: FS193
Nature of business and principal activities	Providing municipal services and maintaining the best interests of the local community mainly in the Nketoana area.
Mayoral committee	
Executive Mayor	M Molapisi
Councillors	P Nkomo (Speaker) M Nakedi (Executive Member) M Mphaka (Executive Member) M Blignaut (Executive Member) M Moloedi (Executive Member) G Nhlapo P Mofokeng T Radebe M Malindi M Mosia M Semela K Mokoena N Tshabalala P Sibeko
Grading of local authority	Medium Capacity Grade 3 in terms of the Remuneration of Public Office Bearers' Act
Accounting Officer	LI Mokgatlhe (Municipal Manager)
Chief Finance Officer (CFO)	TG Makgale (acting)
Registered office	Corner Church and Voortrekker St Reitz 9810
Business address	Corner Church and Voortrekker St Reitz 9810
Postal address	P.O. Box 26 Reitz 9810
Capital risk	Nketoana Municipality
Bankers	ABSA (Primary bank)
Auditors	Auditor-General South Africa
Enabling legislation	Municipal Finance Management Act (Act 56 of 2003) Municipal Property Rates Act (Act 6 of 2004) revised 2014 Municipal Structures Act (Act 117 of 1998) Municipal Systems Act (Act 32 of 2000) Division of Revenue Act (Act 2 of 2013)

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The reports and statements set out below comprise the annual financial statements presented to the Council and the provincial legislature:

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Abbreviations

COID	Compensation for Occupational Injuries and Diseases
CRR	Capital Replacement Reserve
DBSA	Development Bank of South Africa
DORA	Division of Revenue Act
GRAP	Generally Recognised Accounting Practice
HDF	Housing Development Fund
IDP	Integrated Development Plan
IAS	International Accounting Standards
IMFO	Institute of Municipal Finance Officers
IPSAS	International Public Sector Accounting Standards
ME's	Municipal Entities
MEC	Member of the Executive Council
MFMA	Municipal Finance Management Act
MIG	Municipal Infrastructure Grant (Previously CMIP)
NERSA	National Energy Regulator of South Africa
PAYE	Pay As You Earn
SCM	Supply Chain Management

Nketoana Local Municipality

Annual Financial Statements for the year ended 30 June 2016

Accounting Officer's Responsibilities and Approval

The municipality is engaged in providing municipal services and maintaining the best interest of the local community, mainly in the Nketoana area and operates principally in South Africa.

The Accounting Officer is required by the Municipal Finance Management Act (Act 56 of 2003), to maintain adequate accounting records and is responsible for the content and integrity of the annual financial statements and related financial information included in this report. It is the responsibility of the accounting officer to ensure that the annual financial statements fairly present the state of affairs of the municipality as at the end of the financial year and the results of its operations and cash flows for the period then ended. The external auditors are engaged to express an independent opinion on the annual financial statements and was given unrestricted access to all financial records and related data.

The annual financial statements have been prepared in accordance with Standards of Generally Recognised Accounting Practice (GRAP) including any interpretations, guidelines and directives issued by the Accounting Standards Board.

The annual financial statements are based upon appropriate accounting policies consistently applied and supported by reasonable and prudent judgements and estimates.

The Accounting Officer acknowledges that he is ultimately responsible for the system of internal financial control established by the municipality and place considerable importance on maintaining a strong control environment. To enable the accounting officer to meet these responsibilities, the Accounting Officer sets standards for internal control aimed at reducing the risk of error or deficit in a cost effective manner. The standards include the proper delegation of responsibilities within a clearly defined framework, effective accounting procedures and adequate segregation of duties to ensure an acceptable level of risk. These controls are monitored throughout the municipality and all employees are required to maintain the highest ethical standards in ensuring the municipality's business is conducted in a manner that in all reasonable circumstances is above reproach. The focus of risk management in the municipality is on identifying, assessing, managing and monitoring all known forms of risk across the municipality. While operating risk cannot be fully eliminated, the municipality endeavours to minimise it by ensuring that appropriate infrastructure, controls, systems and ethical behaviour are applied and managed within predetermined procedures and constraints.

The Accounting Officer is of the opinion, based on the information and explanations given by management, that the system of internal control provides reasonable assurance that the financial records may be relied on for the preparation of the annual financial statements. However, any system of internal financial control can provide only reasonable, and not absolute, assurance against material misstatement or deficit.

The Accounting Officer certifies that the salaries, allowances and benefits of Councillors, loans made to Councillors, if any, and payments made to Councillors for loss of office, if any, as disclosed in note 36of these annual financial statements are within the upper limits of the framework envisaged in Section 219 of the Constitution, read with the Remuneration of Public Office Bearers Act and the Minister of Provincial and Local Government's determination in accordance with this Act.

The external auditors are responsible for independently auditing and reporting on the municipality's annual financial statements. The annual financial statements have been examined by the municipality's external auditors and their report is presented on page 6.

The annual financial statements set out on pages 7 to 89, which have been prepared on the going concern basis, were approved and signed by the Accounting Officer on 30 November 2016:

L.I. Mokgatlhe
Municipal Manager

Nketoana Local Municipality

Annual Financial Statements for the year ended 30 June 2016

Audit Committee Report

We are pleased to present our report for the financial year ended 30 June 2016.

Audit committee members and attendance

The audit committee consists of the members listed hereunder and should meet four times per annum as per its approved terms of reference. During the current year four meetings were held.

Name of member	Number of meetings attended
BTA Matabane (Chairperson)	4
K Motsoane	4
C Mokoena	4

	2015/07/03	2015/10/02	2016/01/26	2016/06/08
BTA Matabane (Chairperson)	Yes	Yes	Yes	Yes
K Motsoane	Yes	Yes	Yes	Yes
C Mokoena	Yes	Yes	Yes	Yes

All members of the Audit Committee are independent, with no interest in the management or conduct of the business of the Municipality.

Audit committee responsibility

The audit committee reports that it has complied with its responsibilities arising from section 166(2)(a) of the MFMA.

The audit committee also reports that it has adopted appropriate formal terms of reference as its audit committee charter, has regulated its affairs in compliance with this charter and has discharged all its responsibilities as contained therein.

The effectiveness of internal control

The system of internal control was not entirely effective for the year under review. During the year under review, several deficiencies in the system of internal control and/or deviations were reported by the internal auditors and the Auditor-General South Africa. In certain instances, the matters reported previously have not been fully and satisfactorily addressed.

The system of controls is designed to provide cost effective assurance that assets are safeguarded and that liabilities and working capital are efficiently managed. In line with the MFMA, Internal Audit provides the Audit Committee and management with assurance that the internal controls are appropriate and effective. This is achieved by means of the risk management process, as well as the identification of corrective actions and suggested enhancements to the controls and processes.

The audit committee is not satisfied with the content and quality of monthly and quarterly reports prepared and issued by the Accounting Officer of the municipality during the year under review.

Evaluation of annual financial statements

The audit committee has:

- reviewed and discussed the unaudited annual financial statements to be included in the annual report, with the Auditor-General and the Accounting Officer;

Internal audit

The audit committee is satisfied that the internal audit function is operating effectively and that it has addressed the risks pertinent to the municipality and its audits, except for issues raised by the committee in their report to Council.

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Chairperson of the Audit Committee

Date: ______________________

PRACTICE LOGO

Report of the Auditor General

To the Provincial Legislature of Nketoana Local Municipality

Report on the financial statements

Responsibility of the Accounting Officer for the annual financial statements

The Accounting Officer is responsible for the preparation and fair presentation of these annual financial statements in accordance with [the applicable reporting framework/basis of accounting] [and in the manner required by the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA). This responsibility includes:

- designing, implementing and maintaining internal control relevant to the preparation and fair presentation of annual financial statements that are free from material misstatement, whether due to fraud or error;
- selecting and applying appropriate accounting policies; and
- making accounting estimates that are reasonable in the circumstances.

Responsibility of the Auditor-General

As required by [section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on these annual financial statements based on my audit.

I conducted my audit in accordance with the International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the annual financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the annual financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the annual financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the annual financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

An audit also includes evaluating the:

- appropriateness of accounting policies used;
- reasonableness of accounting estimates made by management; and
- overall presentation of the financial statements.

Paragraph 11 et seq. of the Statement of Generally Recognised Accounting Practice, GRAP 1 Presentation of Financial Statements requires that financial reporting by entities shall provide information on whether resources were obtained and used in accordance with the legally adopted budget. As the budget reporting standard is still in the process of being developed, I have determined that my audit of any disclosures made by [name of entity] in this respect will be limited to reporting on non-compliance with this disclosure requirement.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Auditor-General South Africa

30 November 2016

Nketoana Local Municipality
Annual Financial Statements for the year ended 30 June 2016

Accounting Officer's Report

The Accounting Officer submits his report for the year ended 30 June 2016.

1. Review of activities

Main business and operations

The operating results and state of affairs of the municipality are fully set out in the attached annual financial statements and do not, in our opinion, require any further comment.

Net deficit of the municipality was R 41 264 760 (2015: deficit R 63 262 126).

2. Going concern

The annual financial statements have been prepared on the basis of accounting policies applicable to a going concern. The municipality's current financial health however indicates that a material uncertainty exists as the municipality may not be able to realise its assets and discharge its liabilities.

The following analysis supports the going concern assumption:
- Total assets (R 1 051 378 120) exceed total liabilities (R 208 711 210)
The municipality has an accumulated surplus and other reserves of R 842 666 910.
Management has reviewed the municipality's cash flow forecast for the year to 30 June 2017 and, in the light of this review and the current financial position, management is satisfied that the municipality has, or has access to, adequate resources to continue in operational existence for the foreseeable future.

The municipality still has the power to levy rates and taxes and it will continue to receive funding from government as evident from the equitable share allocation in terms of the Division of Revenue Act (Act 1 of 2015).

3. Subsequent events

The Accounting Officer is not aware of any matter or circumstance arising since the end of the financial year that would have an impact on the financial statements.

4. Accounting Officer's interest in contracts

In terms of the Supply Chain Management Policy of the municipality, councillors and officials are prohibited from entering into commercial transactions with the municipality.

Councilors and officials are required to disclose any business interest which they may have elsewhere.

The register of declaration of interest is available in the office of the Chief Whip for inspection.

Consistent with the Supply Chain Management Policy of the municipality, none of the councillors or officers entered into any commercial transaction with the municipality during the period under review.The Accounting Officer does not have any interest in contracts.

5. Accounting policies

The annual financial statements have been prepared in accordance with the prescribed Standards of Generally Recognised Accounting Practices (GRAP), including any interpretations and directives issued by the Accounting Standards Board and in accordance with section 122(3) of the Municipal Finance Management Act, (Act No. 56 of 2003).

6. Non-current assets

There were no major changes in the physical nature of non-current assets of the municipality during the year.

7. Accounting Officer

The accounting officer of the municipality during the year and to the date of this report is as follows:

Name	Nationality
L.I. Mokgatlhe	South African

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Accounting Officer's Report

8. Secretary

The municipality had no secretary during the year.

9. Auditors

Auditor-General South Africa will continue in office for the next financial period.

Nketoana Local Municipality

Annual Financial Statements for the year ended 30 June 2016

Statement of Financial Position as at 30 June 2016

Figures in Rand	Note(s)	2016	2015 Restated*
Assets			
Current Assets			
Inventories	4	608 278	586 686
Receivables from exchange transactions	5	-	-
Receivables from non-exchange transactions	6	2 119 152	1 953 845
VAT receivable	7	1 763 881	1 763 881
Consumer debtors	8	17 708 530	15 822 490
Cash and cash equivalents	9	3 104 182	2 908 446
		25 304 023	**23 035 348**
Non-Current Assets			
Biological assets that form part of an agricultural activity	10	24 513	50 476
Investment property	11	13 877 904	13 877 904
Property, plant and equipment	12	1 004 970 006	1 004 475 920
Intangible assets	13	65 598	72 705
Heritage assets	14	529 800	529 800
Other financial assets	15	4 587 776	4 305 805
Long-term deposit	16	2 018 500	2 018 500
		1 026 074 097	**1 025 331 110**
Total Assets		**1 051 378 120**	**1 048 366 458**
Liabilities			
Current Liabilities			
Other financial liabilities	17	1 349 442	1 398 503
Finance lease obligation	18	181 599	-
Payables from exchange transactions	19	163 779 083	113 956 319
VAT payable	20	13 545 356	18 376 667
Consumer deposits	21	1 348 785	1 305 253
Employee benefit obligation	22	422 000	550 000
Unspent conditional grants and receipts	23	92 019	1 091 381
Cash and cash equivalents	9	577 159	1 198 016
		181 295 443	**137 876 139**
Non-Current Liabilities			
Other financial liabilities	17	7 806 024	8 569 848
Finance lease obligation	18	467 740	-
Employee benefit obligation	22	11 033 000	10 619 000
Provisions	24	8 109 003	7 369 811
		27 415 767	**26 558 659**
Total Liabilities		**208 711 210**	**164 434 798**
Net Assets		**842 666 910**	**883 931 660**
Accumulated surplus	25	842 666 910	883 931 660

Nketoana Local Municipality
Annual Financial Statements for the year ended 30 June 2016

Statement of Financial Performance

Figures in Rand	Note(s)	2016	2015 Restated*
Revenue			
Revenue from exchange transactions			
Service charges	26	128 350 794	111 255 685
Rental of facilities and equipment	27	331 864	356 580
Interest received (trading)	28	24 391 914	20 201 160
Other income	29	1 475 690	1 073 811
Interest received - investment	30	1 101 572	583 166
Total revenue from exchange transactions		**155 651 834**	**133 470 402**
Revenue from non-exchange transactions			
Taxation revenue			
Property rates	31	16 612 976	15 835 059
Transfer revenue			
Government grants & subsidies	32	145 433 408	145 035 655
Public contributions and donations	33	8 942 783	4 299 995
Fines	34	216 310	205 404
Total revenue from non-exchange transactions		**171 205 477**	**165 376 113**
Total revenue		**326 857 311**	**298 846 515**
Expenditure			
Employee related costs	35	(80 810 390)	(74 798 709)
Remuneration of councillors	36	(6 891 541)	(6 676 993)
Depreciation and amortisation	37	(58 502 541)	(57 015 081)
Finance costs	38	(10 202 243)	(8 338 647)
Lease rentals on operating lease	39	(5 547 174)	(4 686 484)
Debt Impairment	40	(83 419 298)	(108 567 852)
Repairs and maintenance	41	(18 427 332)	(15 404 523)
Bulk purchases	42	(43 817 910)	(38 934 748)
Contracted services	43	(11 399 862)	(10 758 689)
General Expenses	44	(49 138 817)	(37 729 201)
Total expenditure		**(368 157 108)**	**(362 910 927)**
Operating deficit		**(41 299 797)**	**(64 064 412)**
Gain on disposal of assets and liabilities	45	-	36 425
Fair value adjustments	46	(25 963)	57 861
Actuarial gains/losses	22	61 000	708 000
		35 037	**802 286**
Deficit for the year		**(41 264 760)**	**(63 262 126)**

Nketoana Local Municipality
Annual Financial Statements for the year ended 30 June 2016

Statement of Changes in Net Assets

Figures in Rand	Accumulated surplus	Total net assets
Opening balance as previously reported	533 187 222	533 187 222
Adjustments		
Correction of errors	414 006 564	414 006 564
Balance at 01 July 2014 as restated*	**947 193 786**	**947 193 786**
Changes in net assets		
Deficit for the year	(63 262 126)	(63 262 126)
Total changes	(63 262 126)	(63 262 126)
Opening balance as previously reported	492 774 890	492 774 890
Adjustments		
Correction of errors	391 156 780	391 156 780
Restated* Balance at 01 July 2015 as restated*	**883 931 670**	**883 931 670**
Changes in net assets		
Deficit for the year	(41 264 760)	(41 264 760)
Total changes	(41 264 760)	(41 264 760)
Balance at 30 June 2016	**842 666 910**	**842 666 910**

Nketoana Local Municipality
Annual Financial Statements for the year ended 30 June 2016

Cash Flow Statement

Figures in Rand	Note(s)	2016	2015 Restated*
Cash flows from operating activities			
Receipts			
Taxation		16 673 984	15 835 059
Sale of goods and services		69 183 916	54 705 719
Grants		153 427 832	139 771 682
Interest income		1 101 572	583 166
		240 387 304	210 895 626
Payments			
Employee costs		(87 354 931)	(81 031 940)
Suppliers		(82 578 504)	(72 329 583)
Finance costs		(10 202 243)	(8 338 647)
		(180 135 678)	(161 700 170)
Net cash flows from operating activities	48	**60 251 626**	**49 195 456**
Cash flows from investing activities			
Purchase of property, plant and equipment	12	(59 549 009)	(45 578 295)
Proceeds from sale of property, plant and equipment	12	587 073	36 425
Purchase of other intangible assets	13	(27 582)	(19 666)
Movement in financial assets		(281 971)	306 724
Net cash flows from investing activities		**(59 271 489)**	**(45 254 812)**
Cash flows from financing activities			
Repayment of other financial liabilities		(812 885)	(1 348 909)
Movment in finance lease liability		649 339	-
Net cash flows from financing activities		**(163 546)**	**(1 348 909)**
Net increase/(decrease) in cash and cash equivalents		**816 591**	**2 591 735**
Cash and cash equivalents at the beginning of the year		1 710 430	(881 306)
Cash and cash equivalents at the end of the year	9	**2 527 021**	**1 710 429**

Nketoana Local Municipality

Annual Financial Statements for the year ended 30 June 2016

Statement of Comparison of Budget and Actual Amounts

Budget on Accrual Basis

Figures in Rand	Approved budget	Adjustments	Final Budget	Actual amounts on comparable basis	Difference between final budget and actual	Reference
Statement of Financial Performance						
Revenue						
Revenue from exchange transactions						
Service charges	142 869 000	-	**142 869 000**	128 350 794	**(14 518 206)**	Note 1
Rental of facilities and equipment	409 000	(42 000)	**367 000**	331 864	**(35 136)**	Note 2
Interest received (trading)	12 000 000	10 577 000	**22 577 000**	24 391 914	**1 814 914**	Note 3
Other income - (rollup)	51 867 000	(19 639 000)	**32 228 000**	1 475 690	**(30 752 310)**	Note 4
Interest received - investment	644 000	(44 000)	**600 000**	1 101 572	**501 572**	Note 5
Total revenue from exchange transactions	**207 789 000**	**(9 148 000)**	**198 641 000**	**155 651 834**	**(42 989 166)**	
Revenue from non-exchange transactions						
Taxation revenue						
Property rates	18 796 000	-	**18 796 000**	16 612 976	**(2 183 024)**	Note 6
Transfer revenue						
Government grants & subsidies	84 163 000	-	**84 163 000**	145 433 408	**61 270 408**	Note 7
Public contributions and donations	-	-	**-**	8 942 783	**8 942 783**	
Fines	180 000	-	**180 000**	216 310	**36 310**	Note 8
Total revenue from non-exchange transactions	**103 139 000**	**-**	**103 139 000**	**171 205 477**	**68 066 477**	
Total revenue	**310 928 000**	**(9 148 000)**	**301 780 000**	**326 857 311**	**25 077 311**	
Expenditure						
Personnel	(71 987 000)	1 108 000	**(70 879 000)**	(80 810 390)	**(9 931 390)**	Note 9
Remuneration of councillors	(6 530 000)	(132 000)	**(6 662 000)**	(6 891 541)	**(229 541)**	Note 10
Depreciation and amortisation	(64 000 000)	(3 200 000)	**(67 200 000)**	(58 502 541)	**8 697 459**	Note 11
Finance costs	(1 200 000)	-	**(1 200 000)**	(10 202 243)	**(9 002 243)**	Note 12
Lease rentals on operating lease	-	-	**-**	(5 547 174)	**(5 547 174)**	Note 13
Bad debts written off	(40 316 000)	-	**(40 316 000)**	(83 419 298)	**(43 103 298)**	Note 14
Repairs and maintenance	(10 898 000)	(260 000)	**(11 158 000)**	(18 427 332)	**(7 269 332)**	Note 15
Bulk purchases	(50 434 000)	11 400 000	**(39 034 000)**	(43 817 910)	**(4 783 910)**	Note 16
Contracted Services	(6 930 000)	(963 000)	**(7 893 000)**	(11 399 862)	**(3 506 862)**	Note 17
Transfers and Subsidies	(22 499 000)	5 171 000	**(17 328 000)**	-	**17 328 000**	
General Expenses	(38 978 000)	(4 806 000)	**(43 784 000)**	(49 138 817)	**(5 354 817)**	Note 18
Total expenditure	**(313 772 000)**	**8 318 000**	**(305 454 000)**	**(368 157 108)**	**(62 703 108)**	
Operating deficit	**(2 844 000)**	**(830 000)**	**(3 674 000)**	**(41 299 797)**	**(37 625 797)**	
Fair value adjustments	-	-	**-**	(25 963)	**(25 963)**	
Actuarial gains/losses	-	-	**-**	61 000	**61 000**	
	-	**-**	**-**	**35 037**	**35 037**	
Deficit before taxation	**(2 844 000)**	**(830 000)**	**(3 674 000)**	**(41 264 760)**	**(37 590 760)**	
Actual Amount on Comparable Basis as Presented in the Budget and Actual Comparative Statement	**(2 844 000)**	**(830 000)**	**(3 674 000)**	**(41 264 760)**	**(37 590 760)**	

Nketoana Local Municipality

Annual Financial Statements for the year ended 30 June 2016

Statement of Comparison of Budget and Actual Amounts

Budget on Accrual Basis

Figures in Rand	Approved budget	Adjustments	Final Budget	Actual amounts on comparable basis	Difference between final budget and actual	Reference

Nketoana Local Municipality
Annual Financial Statements for the year ended 30 June 2016

Statement of Comparison of Budget and Actual Amounts

Budget on Accrual Basis						
Figures in Rand	Approved budget	Adjustments	Final Budget	Actual amounts on comparable basis	Difference between final budget and actual	Reference

Basis differences
Both the approved budget and the financial statements are prepared on the accrual basis and differences between the final budget and actual amounts are therefore not due to basis differences.

Timing differences
The budget period does not differ from the financial statements period and differences between the final budget and the actual amounts are therefore not due to timing differences.

Entity differences
The approved budget does not omits programmes or entities that are part of the Municipality for financial statement purposes and differences between the final budget and actual amounts are therefore not due to entity differences.

Explanantions for differences between budget and actual

Note 1
The budgeted amount was not in line with growth expectations. The service charges increased as expected but is still not in line with the budgeted amount.

Note 2
The budgeted amount did not account for the rental contracts that ended during the 2015/2016 financial year.

Note 3
The municipality's interest on overdue accounts is linked to prime and the multiple upward changes to the repo rate was not budgeted for. This was further increased by the rising consumer debtor figure.

Note 4
The budgeted amount included revenue collection strategies which were never implemented.

Note 5
The municipality invest more funds and for longer periods than initially budgeted for.

Note 6
The budgeted amount was not in line with growth expectations. The service charges increased as expected but is still not in line with the budgeted amount.

Note 7
The budgeted amount does not include capital grants such as MIG, RBIG and INEG, whilst the actual amount includes capital and operational grants.

Note 8
Issuing and collection of fines were higher than budgeted for..

Note 9
The municipality did not budget for any expense relating to the vacant positions and the accompanying acting allowances.

Note 10
The actual amount is within 3% of the budgeted amount and the variance is therefore seen as insignificant.

Note 11
The municiplaty's depreciation for 2014/2015 and 2015/2016 was recalculated using the new asset registers and this resulted in the actual figure being significantly lower than the budgeted figure.

Note 12
Interest on overdue payable accounts caused the significant difference between the budgeted and actual amounts.

Nketoana Local Municipality

Annual Financial Statements for the year ended 30 June 2016

Statement of Comparison of Budget and Actual Amounts

Budget on Accrual Basis						
Figures in Rand	Approved budget	Adjustments	Final Budget	Actual amounts on comparable basis	Difference between final budget and actual	Reference

Note 13

Lease rentals were budgeted for under *general expenses*.

Note 14

The 2015/2016 actual write-offs amounted to R23m whilst the increase in the provision for bad debts amounted to R52m. The movement in the Statement of Financial Performance was not adequately budgeted for.

Note 15

Repairs & maintenance on ageing infrastructure was not adequately budgeted for.

Note 16

The budgeted bulk purchases is 12% lower than the actual amount. The significant increase in the cost of electricity was not anticipated and therefore not adequately budgeted for.

Note 17

The vacant positions and lack of yellow fleet resulted in higher contracted service amounts..

Note 18

The significant increase in the electricity expenditure was not adequately budgeted for.

The accounting policies on pages 17 to 46 and the notes on pages 47 to 89 form an integral part of the annual financial statements.

Nketoana Local Municipality
Annual Financial Statements for the year ended 30 June 2016

Accounting Policies

1. Presentation of Annual Financial Statements

The annual financial statements have been prepared in accordance with the Standards of Generally Recognised Accounting Practice (GRAP), issued by the Accounting Standards Board in accordance with Section 122(3) of the Municipal Finance Management Act (Act 56 of 2003).

These annual financial statements have been prepared on an accrual basis of accounting and are in accordance with historical cost convention as the basis of measurement, unless specified otherwise. They are presented in South African Rand.

A summary of the significant accounting policies, which have been consistently applied in the preparation of these annual financial statements, are disclosed below.

1.1 Presentation currency

These annual financial statements are presented in South African Rand, which is the functional currency of the Municipality.

1.2 Going concern assumption

These annual financial statements have been prepared based on the expectation that the municipality will continue to operate as a going concern for at least the next 12 months.

1.3 Biological assets that form part of an agricultural activity

The entity recognises a biological assets that form part of an agricultural activity or agricultural produce when, and only when:
- the entity controls the asset as a result of past events;
- it is probable that future economic benefits or service potential associated with the asset will flow to the municipality; and
- the fair value or cost of the asset can be measured reliably.

Biological assets that form part of an agricultural activity are measured at their fair value less costs to sell.

The fair value of livestock is determined based on market prices of livestock of similar age, breed, and genetic merit.

A gain or loss arising on initial recognition of biological assets that form part of an agricultural activity or agricultural produce at fair value less costs to sell and from a change in fair value less costs to sell of a biological assets that form part of an agricultural activity is included in surplus or deficit for the period in which it arises.

Where market determined prices or values are not available, the present value of the expected net cash inflows from the asset, discounted at a current market-determined pre-tax rate where applicable is used to determine fair value.

Where fair value cannot be measured reliably, biological assets are measured at cost.

1.4 Investment property

Investment property is property (land or a building - or part of a building - or both) held to earn rentals or for capital appreciation or both, rather than for:
- use in the production or supply of goods or services or for
- administrative purposes, or
- sale in the ordinary course of operations.

Owner-occupied property is property held for use in the production or supply of goods or services or for administrative purposes.

Investment property is recognised as an asset when, it is probable that the future economic benefits or service potential that are associated with the investment property will flow to the Municipality, and the cost or fair value of the investment property can be measured reliably.

Investment property is initially recognised at cost. Transaction costs are included in the initial measurement.

Where investment property is acquired through a non-exchange transaction, its cost is its fair value as at the date of acquisition.

Accounting Policies

1.4 Investment property (continued)

Costs include costs incurred initially and costs incurred subsequently to add to, or to replace a part of, or service a property. If a replacement part is recognised in the carrying amount of the investment property, the carrying amount of the replaced part is derecognised.

Fair value

Subsequent to initial measurement investment property is measured at fair value.

The fair value of investment property reflects market conditions at the reporting date.

A gain or loss arising from a change in fair value is included in net surplus or deficit for the period in which it arises.

If the entity determines that the fair value of an investment property under construction is not reliably determinable but expects the fair value of the property to be reliably measurable when construction is complete, it measures that investment property under construction at cost until either its fair value becomes reliably determinable or construction is completed (whichever is earlier). If the entity determines that the fair value of an investment property (other than an investment property under construction) is not reliably determinable on a continuing basis, the entity measures that investment property using the cost model (as per the accounting policy on Property, plant and equipment). The residual value of the investment property is then assumed to be zero. The entity applies the cost model (as per the accounting policy on Property, plant and equipment) until disposal of the investment property.

Once the entity becomes able to measure reliably the fair value of an investment property under construction that has previously been measured at cost, it measures that property at its fair value. Once construction of that property is complete, it is presumed that fair value can be measured reliably. If this is not the case, the property is accounted for using the cost model in accordance with the accounting policy on Property, plant and equipment.

Investment property is derecognised on disposal or when the investment property is permanently withdrawn from use and no future economic benefits or service potential are expected from its disposal.

Gains or losses arising from the retirement or disposal of investment property is the difference between the net disposal proceeds and the carrying amount of the asset and is recognised in surplus or deficit in the period of retirement or disposal.

Compensation from third parties for investment property that was impaired, lost or given up is recognised in surplus or deficit when the compensation becomes receivable.

1.5 Property, plant and equipment

Property, plant and equipment are tangible non-current assets (including infrastructure assets) that are held for use in the production or supply of goods or services, rental to others, or for administrative purposes, and are expected to be used during more than one period.

The cost of an item of property, plant and equipment is recognised as an asset when:

- it is probable that future economic benefits or service potential associated with the item will flow to the municipality; and
- the cost of the item can be measured reliably.

Property, plant and equipment is initially measured at cost.

The cost of an item of property, plant and equipment is the purchase price and other costs attributable to bring the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. Trade discounts and rebates are deducted in arriving at the cost.

Where an asset is acquired through a non-exchange transaction, its cost is its fair value as at date of acquisition.

Where an item of property, plant and equipment is acquired in exchange for a non-monetary asset or monetary assets, or a combination of monetary and non-monetary assets, the asset acquired is initially measured at fair value (the cost). If the acquired item's fair value was not determinable, it's deemed cost is the carrying amount of the asset(s) given up.

When significant components of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

Accounting Policies

1.5 Property, plant and equipment (continued)

Costs include costs incurred initially to acquire or construct an item of property, plant and equipment and costs incurred subsequently to add to, replace part of, or service it. If a replacement cost is recognised in the carrying amount of an item of property, plant and equipment, the carrying amount of the replaced part is derecognised.

The initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located is also included in the cost of property, plant and equipment, where the entity is obligated to incur such expenditure, and where the obligation arises as a result of acquiring the asset or using it for purposes other than the production of inventories.

Recognition of costs in the carrying amount of an item of property, plant and equipment ceases when the item is in the location and condition necessary for it to be capable of operating in the manner intended by management.

Items such as spare parts, standby equipment and servicing equipment are recognised when they meet the definition of property, plant and equipment.

Major inspection costs which are a condition of continuing use of an item of property, plant and equipment and which meet the recognition criteria above are included as a replacement in the cost of the item of property, plant and equipment. Any remaining inspection costs from the previous inspection are derecognised.

Property, plant and equipment are depreciated on the straight line basis over their expected useful lives to their estimated residual value.

Property, plant and equipment is carried at cost less accumulated depreciation and any impairment losses.

The useful lives of items of property, plant and equipment have been assessed as follows:

Item	Depreciation method	Average useful life
Land		Indefinite
Buildings	Straight line	5 - 60 years
Furniture and fixtures	Straight line	5 - 7 years
Motor vehicles	Straight line	5 - 15 years
Office equipment	Straight line	4 - 15 years
Emergency equipment	Straight line	5 years
Leased assets	Straight line	3 years
Electricity network	Straight line	5 - 60 years
Roads and stormwater	Straight line	10 - 60 years
Wastewater network	Straight line	5 - 70 years
Water network	Straight line	5 - 60 years

The residual value, and the useful life and depreciation method of each asset are reviewed at the end of each reporting date. If the expectations differ from previous estimates, the change is accounted for as a change in accounting estimate.

Reviewing the useful life of an asset on an annual basis does not require the entity to amend the previous estimate unless expectations differ from the previous estimate.

Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item is depreciated separately.

The depreciation charge for each period is recognised in surplus or deficit unless it is included in the carrying amount of another asset.

Items of property, plant and equipment are derecognised when the asset is disposed of or when there are no further economic benefits or service potential expected from the use of the asset.

The gain or loss arising from the derecognition of an item of property, plant and equipment is included in surplus or deficit when the item is derecognised. The gain or loss arising from the derecognition of an item of property, plant and equipment is determined as the difference between the net disposal proceeds, if any, and the carrying amount of the item.

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Accounting Policies

1.5 Property, plant and equipment (continued)

Assets which the municipality holds for rentals to others and subsequently routinely sell as part of the ordinary course of activities, are transferred to inventories when the rentals end and the assets are available-for-sale. Proceeds from sales of these assets are recognised as revenue. All cash flows on these assets are included in cash flows from operating activities in the cash flow statement.

1.6 Intangible assets

An asset is identifiable if it either:
- is separable, i.e. is capable of being separated or divided from an entity and sold, transferred, licensed, rented or exchanged, either individually or together with a related contract, identifiable assets or liability, regardless of whether the entity intends to do so; or
- arises from binding arrangements (including rights from contracts), regardless of whether those rights are transferable or separable from the municipality or from other rights and obligations.

A binding arrangement describes an arrangement that confers similar rights and obligations on the parties to it as if it were in the form of a contract.

An intangible asset is recognised when:
- it is probable that the expected future economic benefits or service potential that are attributable to the asset will flow to the municipality; and
- the cost or fair value of the asset can be measured reliably.

The municipality assesses the probability of expected future economic benefits or service potential using reasonable and supportable assumptions that represent management's best estimate of the set of economic conditions that will exist over the useful life of the asset.

Where an intangible asset is acquired through a non-exchange transaction, its initial cost at the date of acquisition is measured at its fair value as at that date.

Expenditure on research (or on the research phase of an internal project) is recognised as an expense when it is incurred.

An intangible asset arising from development (or from the development phase of an internal project) is recognised when:
- it is technically feasible to complete the asset so that it will be available for use or sale.
- there is an intention to complete and use or sell it.
- there is an ability to use or sell it.
- it will generate probable future economic benefits or service potential.
- there are available technical, financial and other resources to complete the development and to use or sell the asset.
- the expenditure attributable to the asset during its development can be measured reliably.

Intangible assets are carried at cost less any accumulated amortisation and any impairment losses.

An intangible asset is regarded as having an indefinite useful life when, based on all relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows or service potential. Amortisation is not provided for these intangible assets, but they are tested for impairment annually and whenever there is an indication that the asset may be impaired. For all other intangible assets amortisation is provided on a straight line basis over their useful life.

The amortisation period and the amortisation method for intangible assets are reviewed at each reporting date.

Reassessing the useful life of an intangible asset with a finite useful life after it was classified as indefinite is an indicator that the asset may be impaired. As a result the asset is tested for impairment and the remaining carrying amount is amortised over its useful life.

Internally generated brands, mastheads, publishing titles, customer lists and items similar in substance are not recognised as intangible assets.

Internally generated goodwill is not recognised as an intangible asset.

Amortisation is provided to write down the intangible assets, on a straight line basis, to their residual values as follows:

Item	**Useful life**

Accounting Policies

1.6 Intangible assets (continued)

Computer software, other	4 years

1.7 Heritage assets

Class of heritage assets means a grouping of heritage assets of a similar nature or function in a municipality's operations that is shown as a single item for the purpose of disclosure in the annual financial statements.

Heritage assets are assets that have a cultural, environmental, historical, natural, scientific, technological or artistic significance and are held indefinitely for the benefit of present and future generations.

Recognition

The municipality recognises a heritage asset as an asset if it is probable that future economic benefits or service potential associated with the asset will flow to the municipality, and the cost or fair value of the asset can be measured reliably.

Initial measurement

Heritage assets are measured at cost.

Where a heritage asset is acquired through a non-exchange transaction, its cost is measured at its fair value as at the date of acquisition.

Subsequent measurement

After recognition as an asset, a class of heritage assets is carried at its cost less any accumulated impairment losses.

Impairment

The municipality assess at each reporting date whether there is an indication that it may be impaired. If any such indication exists, the municipality estimates the recoverable amount or the recoverable service amount of the heritage asset.

Transfers

Transfers from heritage assets are only made when the particular asset no longer meets the definition of a heritage asset.

Transfers to heritage assets are only made when the asset meets the definition of a heritage asset.

Derecognition

The municipality derecognises heritage asset on disposal, or when no future economic benefits or service potential are expected from its use or disposal.

The gain or loss arising from the derecognition of a heritage asset is included in surplus or deficit when the item is derecognised (unless the Standard of GRAP on leases requires otherwise on a sale and leaseback).

1.8 Financial instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or a residual interest of another entity.

The amortised cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount, and minus any reduction (directly or through the use of an allowance account) for impairment or uncollectibility.

A concessionary loan is a loan granted to or received by an entity on terms that are not market related.

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

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Accounting Policies

1.8 Financial instruments (continued)

Derecognition is the removal of a previously recognised financial asset or financial liability from an entity's statement of financial position.

A derivative is a financial instrument or other contract with all three of the following characteristics:
- Its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract (sometimes called the 'underlying').
- It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors.
- It is settled at a future date.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability (or group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, an entity shall estimate cash flows considering all contractual terms of the financial instrument (for example, prepayment, call and similar options) but shall not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate (see the Standard of GRAP on Revenue from Exchange Transactions), transaction costs, and all other premiums or discounts. There is a presumption that the cash flows and the expected life of a group of similar financial instruments can be estimated reliably. However, in those rare cases when it is not possible to reliably estimate the cash flows or the expected life of a financial instrument (or group of financial instruments), the entity shall use the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments).

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable willing parties in an arm's length transaction.

A financial asset is:
- cash;
- a residual interest of another entity; or
- a contractual right to:
  - receive cash or another financial asset from another entity; or
  - exchange financial assets or financial liabilities with another entity under conditions that are potentially favourable to the entity.

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

A financial liability is any liability that is a contractual obligation to:
- deliver cash or another financial asset to another entity; or
- exchange financial assets or financial liabilities under conditions that are potentially unfavourable to the entity.

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

Liquidity risk is the risk encountered by an entity in the event of difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset.

Loan commitment is a firm commitment to provide credit under pre-specified terms and conditions.

Loans payable are financial liabilities, other than short-term payables on normal credit terms.

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: currency risk, interest rate risk and other price risk.

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

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Accounting Policies

1.8 Financial instruments (continued)

A financial asset is past due when a counterparty has failed to make a payment when contractually due.

A residual interest is any contract that manifests an interest in the assets of an entity after deducting all of its liabilities. A residual interest includes contributions from owners, which may be shown as:
- equity instruments or similar forms of unitised capital;
- a formal designation of a transfer of resources (or a class of such transfers) by the parties to the transaction as forming part of an entity's net assets, either before the contribution occurs or at the time of the contribution; or
- a formal agreement, in relation to the contribution, establishing or increasing an existing financial interest in the net assets of an entity.

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability. An incremental cost is one that would not have been incurred if the entity had not acquired, issued or disposed of the financial instrument.

Financial instruments at amortised cost are non-derivative financial assets or non-derivative financial liabilities that have fixed or determinable payments, excluding those instruments that:
- the entity designates at fair value at initial recognition; or
- are held for trading.

Financial instruments at cost are investments in residual interests that do not have a quoted market price in an active market, and whose fair value cannot be reliably measured.

Financial instruments at fair value comprise financial assets or financial liabilities that are:
- derivatives;
- combined instruments that are designated at fair value;
- instruments held for trading. A financial instrument is held for trading if:
  - it is acquired or incurred principally for the purpose of selling or repurchasing it in the near-term; or
  - on initial recognition it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short term profit-taking;
  - non-derivative financial assets or financial liabilities with fixed or determinable payments that are designated at fair value at initial recognition; and
  - financial instruments that do not meet the definition of financial instruments at amortised cost or financial instruments at cost.

Classification

The entity has the following types of financial assets (classes and category) as reflected on the face of the statement of financial position or in the notes thereto:

Class	Category
Consumer receivables	Financial asset measured at amortised cost
Other receivables	Financial asset measured at amortised cost
Other financial asset	Financial asset measured at amortised cost

The entity has the following types of financial liabilities (classes and category) as reflected on the face of the statement of financial position or in the notes thereto:

Class	Category
Trade and other payables	Financial liability measured at amortised cost
Other financial liabilities	Financial liability measured at amortised cost

The entity has the following types of residual interests (classes and category) as reflected on the face of the statement of financial position or in the notes thereto:

Class	Category
Residual interest	Measured at cost

Nketoana Local Municipality

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Accounting Policies

1.8 Financial instruments (continued)

Initial recognition

The entity recognises a financial asset or a financial liability in its statement of financial position when the entity becomes a party to the contractual provisions of the instrument.

The entity recognises financial assets using trade date accounting.

Initial measurement of financial assets and financial liabilities

The entity measures a financial asset and financial liability initially at its fair value plus transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

The entity measures a financial asset and financial liability initially at its fair value [if subsequently measured at fair value].

The entity first assesses whether the substance of a concessionary loan is in fact a loan. On initial recognition, the entity analyses a concessionary loan into its component parts and accounts for each component separately. The entity accounts for that part of a concessionary loan that is:

- a social benefit in accordance with the Framework for the Preparation and Presentation of Financial Statements, where it is the issuer of the loan; or
- non-exchange revenue, in accordance with the Standard of GRAP on Revenue from Non-exchange Transactions (Taxes and Transfers), where it is the recipient of the loan.

Accounting Policies

1.8 Financial instruments (continued)

Subsequent measurement of financial assets and financial liabilities

The entity measures all financial assets and financial liabilities after initial recognition using the following categories:
- Financial instruments at fair value.
- Financial instruments at amortised cost.
- Financial instruments at cost.

All financial assets measured at amortised cost, or cost, are subject to an impairment review.

Fair value measurement considerations

The best evidence of fair value is quoted prices in an active market. If the market for a financial instrument is not active, the entity establishes fair value by using a valuation technique. The objective of using a valuation technique is to establish what the transaction price would have been on the measurement date in an arm's length exchange motivated by normal operating considerations. Valuation techniques include using recent arm's length market transactions between knowledgeable, willing parties, if available, reference to the current fair value of another instrument that is substantially the same, discounted cash flow analysis and option pricing models. If there is a valuation technique commonly used by market participants to price the instrument and that technique has been demonstrated to provide reliable estimates of prices obtained in actual market transactions, the entity uses that technique. The chosen valuation technique makes maximum use of market inputs and relies as little as possible on entity-specific inputs. It incorporates all factors that market participants would consider in setting a price and is consistent with accepted economic methodologies for pricing financial instruments. Periodically, an municipality calibrates the valuation technique and tests it for validity using prices from any observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on any available observable market data.

The fair value of a financial liability with a demand feature (e.g. a demand deposit) is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid.

Reclassification

The entity does not reclassify a financial instrument while it is issued or held unless it is:
- combined instrument that is required to be measured at fair value; or
- an investment in a residual interest that meets the requirements for reclassification.

Where the entity cannot reliably measure the fair value of an embedded derivative that has been separated from a host contract that is a financial instrument at a subsequent reporting date, it measures the combined instrument at fair value. This requires a reclassification of the instrument from amortised cost or cost to fair value.

If fair value can no longer be measured reliably for an investment in a residual interest measured at fair value, the entity reclassifies the investment from fair value to cost. The carrying amount at the date that fair value is no longer available becomes the cost.

If a reliable measure becomes available for an investment in a residual interest for which a measure was previously not available, and the instrument would have been required to be measured at fair value, the entity reclassifies the instrument from cost to fair value.

Gains and losses

A gain or loss arising from a change in the fair value of a financial asset or financial liability measured at fair value is recognised in surplus or deficit.

For financial assets and financial liabilities measured at amortised cost or cost, a gain or loss is recognised in surplus or deficit when the financial asset or financial liability is derecognised or impaired, or through the amortisation process.

Impairment and uncollectibility of financial assets

The entity assess at the end of each reporting period whether there is any objective evidence that a financial asset or group of financial assets is impaired.

Financial assets measured at amortised cost:

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Accounting Policies

1.8 Financial instruments (continued)

If there is objective evidence that an impairment loss on financial assets measured at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced directly OR through the use of an allowance account. The amount of the loss is recognised in surplus or deficit.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed directly OR by adjusting an allowance account. The reversal does not result in a carrying amount of the financial asset that exceeds what the amortised cost would have been had the impairment not been recognised at the date the impairment is reversed. The amount of the reversal is recognised in surplus or deficit.

Financial assets measured at cost:

If there is objective evidence that an impairment loss has been incurred on an investment in a residual interest that is not measured at fair value because its fair value cannot be measured reliably, the amount of the impairment loss is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment losses are not reversed.

Nketoana Local Municipality
Annual Financial Statements for the year ended 30 June 2016

Accounting Policies

1.8 Financial instruments (continued)

Derecognition

Financial assets

The entity derecognises financial assets using trade date accounting.

The entity derecognises a financial asset only when:
- the contractual rights to the cash flows from the financial asset expire, are settled or waived;
- the entity transfers to another party substantially all of the risks and rewards of ownership of the financial asset; or
- the entity, despite having retained some significant risks and rewards of ownership of the financial asset, has transferred control of the asset to another party and the other party has the practical ability to sell the asset in its entirety to an unrelated third party, and is able to exercise that ability unilaterally and without needing to impose additional restrictions on the transfer. In this case, the entity :
  - derecognise the asset; and
  - recognise separately any rights and obligations created or retained in the transfer.

The carrying amounts of the transferred asset are allocated between the rights or obligations retained and those transferred on the basis of their relative fair values at the transfer date. Newly created rights and obligations are measured at their fair values at that date. Any difference between the consideration received and the amounts recognised and derecognised is recognised in surplus or deficit in the period of the transfer.

If the entity transfers a financial asset in a transfer that qualifies for derecognition in its entirety and retains the right to service the financial asset for a fee, it recognise either a servicing asset or a servicing liability for that servicing contract. If the fee to be received is not expected to compensate the entity adequately for performing the servicing, a servicing liability for the servicing obligation is recognised at its fair value. If the fee to be received is expected to be more than adequate compensation for the servicing, a servicing asset is recognised for the servicing right at an amount determined on the basis of an allocation of the carrying amount of the larger financial asset.

If, as a result of a transfer, a financial asset is derecognised in its entirety but the transfer results in the entity obtaining a new financial asset or assuming a new financial liability, or a servicing liability, the entity recognise the new financial asset, financial liability or servicing liability at fair value.

On derecognition of a financial asset in its entirety, the difference between the carrying amount and the sum of the consideration received is recognised in surplus or deficit.

If the transferred asset is part of a larger financial asset and the part transferred qualifies for derecognition in its entirety, the previous carrying amount of the larger financial asset is allocated between the part that continues to be recognised and the part that is derecognised, based on the relative fair values of those parts, on the date of the transfer. For this purpose, a retained servicing asset is treated as a part that continues to be recognised. The difference between the carrying amount allocated to the part derecognised and the sum of the consideration received for the part derecognised is recognised in surplus or deficit.

If a transfer does not result in derecognition because the entity has retained substantially all the risks and rewards of ownership of the transferred asset, the entity continue to recognise the transferred asset in its entirety and recognise a financial liability for the consideration received. In subsequent periods, the entity recognises any revenue on the transferred asset and any expense incurred on the financial liability. Neither the asset, and the associated liability nor the revenue, and the associated expenses are offset.

Financial liabilities

The entity removes a financial liability (or a part of a financial liability) from its statement of financial position when it is extinguished — i.e. when the obligation specified in the contract is discharged, cancelled, expires or waived.

An exchange between an existing borrower and lender of debt instruments with substantially different terms is accounted for as having extinguished the original financial liability and a new financial liability is recognised. Similarly, a substantial modification of the terms of an existing financial liability or a part of it is accounted for as having extinguished the original financial liability and having recognised a new financial liability.

Accounting Policies

1.8 Financial instruments (continued)

The difference between the carrying amount of a financial liability (or part of a financial liability) extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, is recognised in surplus or deficit. Any liabilities that are waived, forgiven or assumed by another entity by way of a non-exchange transaction are accounted for in accordance with the Standard of GRAP on Revenue from Non-exchange Transactions (Taxes and Transfers).

Presentation

Interest relating to a financial instrument or a component that is a financial liability is recognised as revenue or expense in surplus or deficit.

Dividends or similar distributions relating to a financial instrument or a component that is a financial liability is recognised as revenue or expense in surplus or deficit.

Losses and gains relating to a financial instrument or a component that is a financial liability is recognised as revenue or expense in surplus or deficit.

Distributions to holders of residual interests are recognised by the entity directly in net assets. Transaction costs incurred on residual interests are accounted for as a deduction from net assets. Income tax [where applicable] relating to distributions to holders of residual interests and to transaction costs incurred on residual interests are accounted for in accordance with the International Accounting Standard on Income Taxes.

A financial asset and a financial liability are only offset and the net amount presented in the statement of financial position when the entity currently has a legally enforceable right to set off the recognised amounts and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

In accounting for a transfer of a financial asset that does not qualify for derecognition, the entity does not offset the transferred asset and the associated liability.

1.9 Leases

A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership.

When a lease includes both land and buildings elements, the entity assesses the classification of each element separately.

Finance leases - lessee

Finance leases are recognised as assets and liabilities in the statement of financial position at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments. The corresponding liability to the lessor is included in the statement of financial position as a finance lease obligation.

The discount rate used in calculating the present value of the minimum lease payments is the interest rate implicit in the lease.

Minimum lease payments are apportioned between the finance charge and reduction of the outstanding liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of on the remaining balance of the liability.

Any contingent rents are expensed in the period in which they are incurred.

Accounting Policies

1.9 Leases (continued)

Operating leases - lessor

Operating lease revenue is recognised as revenue on a straight-line basis over the lease term.

Initial direct costs incurred in negotiating and arranging operating leases are added to the carrying amount of the leased asset and recognised as an expense over the lease term on the same basis as the lease revenue.

The aggregate cost of incentives is recognised as a reduction of rental revenue over the lease term on a straight-line basis.

The aggregate benefit of incentives is recognised as a reduction of rental expense over the lease term on a straight-line basis.

Income for leases is disclosed under revenue in statement of financial performance.

Operating leases - lessee

Operating lease payments are recognised as an expense on a straight-line basis over the lease term. The difference between the amounts recognised as an expense and the contractual payments are recognised as an operating lease asset or liability.

1.10 Inventories

Inventories are initially measured at cost except where inventories are acquired through a non-exchange transaction, then their costs are their fair value as at the date of acquisition.

Subsequently inventories are measured at the lower of cost and net realisable value.

Inventories are measured at the lower of cost and current replacement cost where they are held for;

- distribution at no charge or for a nominal charge; or
- consumption in the production process of goods to be distributed at no charge or for a nominal charge.

Net realisable value is the estimated selling price in the ordinary course of operations less the estimated costs of completion and the estimated costs necessary to make the sale, exchange or distribution.

Current replacement cost is the cost the municipality incurs to acquire the asset on the reporting date.

The cost of inventories comprises of all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

The cost of inventories of items that are not ordinarily interchangeable and goods or services produced and segregated for specific projects is assigned using specific identification of the individual costs.

The cost of inventories is assigned using the first-in, first-out (FIFO) formula. The same cost formula is used for all inventories having a similar nature and use to the municipality.

When inventories are sold, the carrying amounts of those inventories are recognised as an expense in the period in which the related revenue is recognised. If there is no related revenue, the expenses are recognised when the goods are distributed, or related services are rendered. The amount of any write-down of inventories to net realisable value or current replacement cost and all losses of inventories are recognised as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realisable value or current replacement cost, are recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

1.11 Impairment of cash-generating assets

Cash-generating assets are assets managed with the objective of generating a commercial return. An asset generates a commercial return when it is deployed in a manner consistent with that adopted by a profit-oriented entity.

Impairment is a loss in the future economic benefits or service potential of an asset, over and above the systematic recognition of the loss of the asset's future economic benefits or service potential through depreciation (amortisation).

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1.11 Impairment of cash-generating assets (continued)

Carrying amount is the amount at which an asset is recognised in the statement of financial position after deducting any accumulated depreciation and accumulated impairment losses thereon.

A cash-generating unit is the smallest identifiable group of assets managed with the objective of generating a commercial return that generates cash inflows from continuing use that are largely independent of the cash inflows from other assets or groups of assets.

Costs of disposal are incremental costs directly attributable to the disposal of an asset, excluding finance costs and income tax expense.

Depreciation (Amortisation) is the systematic allocation of the depreciable amount of an asset over its useful life.

Fair value less costs to sell is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal.

Recoverable amount of an asset or a cash-generating unit is the higher its fair value less costs to sell and its value in use.

Useful life is either:
- (a) the period of time over which an asset is expected to be used by the municipality; or
- (b) the number of production or similar units expected to be obtained from the asset by the municipality.

Criteria developed by the municipality to distinguish cash-generating assets from non-cash-generating assets are as follow: