



public works

Department:
Public Works
REPUBLIC OF SOUTH AFRICA

RELATED PARTIES: FRAME WORK FOR THE 2012/1013 FINANCIAL YEAR


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Chief Financial Officer

DEPARTMENT OF PUBLIC WORKS

APPROVED DATE: 10/5/2013

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1. Purpose

The purpose of this document is to lay out the process taken by the department in the current financial year with regards to the identification and disclosure of related parties and transactions with the identified related parties.

2. Definition

Related party transaction is a transfer of resources or obligations between related parties regardless of whether a price is charged.

Related party – parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions or if the related party entity and another entity are subject to common control.

3. Steps in process taken

The high level approach taken by the Department on the related party disclosure note is as follows:

STEP 1: Identify all entities as per Schedule 1, 2 and 3 of the PFMA that are related to the Department with reasons


STEP 2: Identify all transactions the Department has entered into with the identified entities for the financial year under review

STEP 3: Determine whether such transactions are at arm's length or not providing rationale thereon.

STEP 4: If the transactions are not at arm's length, determine whether the cost can be *reliably* measured.

- If no, then a qualitative disclosure note should be recommended
- If yes, then a qualitative and quantitative disclosure should be recommended

The above exercise should be reviewed on an annual basis to ensure accuracy and completeness of all related parties identified as well as account for any business changes. The detailed assessment should be as follows:


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Initials

STEP 1: Identification of a related party

For the financial year ended 31 March 2013, related parties to the Department are to be identified as follows:

- A list of all Institutions from Schedule 1, 2 and 3 of the PFMA and the list of Government department from the National Treasury website to be obtained and analysed
- The related party definition should be applied as per the National Treasury Guide to each of these entities.
- For the financial year ending 31 March 2013, six entities identified as being related to the DPW, either as a result of direct control or having significant influence over the entity, they are:
 - a. Agreement South Africa (ASA)
 - b. Construction Industry Development Board (CIDB)
 - c. Council for the Built Environment (CBE)
 - d. Independent Development Trust (IDT)
 - e. Parliamentary Village Management Board (PVMB)
 - f. Property Management Trading Entity (PMTE)

And all National Departments, and their controlled entities, are related parties to the DPW, As a result of common control (operates together to achieve common objectives determined by Cabinet/Provincial Legislature).

STEP 2: Related party transactions

Based on the above identified related parties, further analysis is required to be performed:

- A list of all related party transactions should be identified per each identified related party and documented by management applying their understanding of the business. In addition, to ensure completeness, confirmation letters are to be sent to all identified related parties to provide a list of all transactions that they have entered into with the Department for the year under review. A gap analysis should be performed between the confirmation letter transaction obtained from the related party and those identified by the Department. Variances are to be communicated with the related party and addressed.
- Each transaction identified should be assessed as an inflow/outflow/ transfer or free service between the related party and the Department.
- All transfers between the Department and the related party shall be disclosed under Transfers and Subsidies in the Annual Financial Report and not as a related party as stated per The Guide.

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Initials

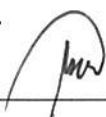


STEP 3: Non arm's length transactions

Non arm's length transactions

The transactions identified can be further categorised as either being an arm's length transaction/non arm's length as follows:

Category	Definition	Disclosure Requirement
Arm's length transaction	<p>"A transaction AT ARMS LENGTH is classified as any transaction at the terms and conditions given to the general public, i.e. a transaction at normal market-related terms and conditions.</p> <ul style="list-style-type: none">For example, the car dealership providing you with a motor vehicle, at a price which any other member of the general public would be required to pay or at a discount which will be given to any other member of the general public."	No disclosure is required as per The Guide
Non arm's length transaction	<p>"A transaction is regarded as NOT AT ARMS LENGTH, if the transaction did NOT occur with normal supplier or client/recipient relationships on terms and conditions no more or less favourable than those which it is reasonable to expect the individual/entity would have adopted if dealing with that individual/entity at arm's length in the same circumstances, i.e. if the individual/entity receives terms and conditions which are different to the general public and ultimately provides a benefit to either of the individuals/entities (at "non-market-related terms and conditions").</p> <ul style="list-style-type: none">For example, the car dealership providing you with a motor vehicle, at a price which is significantly less than that which any other member of the general public would be required to pay."	Disclosure is required as per The Guide



For transactions that are not at arm's length, the Department should address whether these transactions can be reliably measured from accurate and complete records. Where the transaction could not be measured reliably, the recommendation shall be that qualitative disclosure would be applicable in the Annual Financial Statement.

4. Related Party Transactions

4.1 PMTE

- In relation to the other five related parties identified, the Property Management Trading Entity (herewith referred to as 'PMTE') is considered far more complex in nature hence further detailed analysis is required. For the financial year the following was established:
 - a. In 2006, the DPW made a decision to transfer certain functions performed within the DPW to a new trading entity called Property Management Trading Entity. PMTE does not have a functional structure and operates within the departmental structure. The department has been funding PMTE activities either directly or indirectly.
 - b. The two entities are on different accounting frameworks. The Department prepares financial statements on the modified cash basis of accounting whilst the PMTE prepares financial statements using Standards of Generally Accepted Accounting Practices (GRAP). Hence the principles of GRAP 20 were applied when assessing the PMTE transactions.
- Both direct and indirect costs are incurred by the Department which have varying disclosure requirements:

Direct Costs

Where costs have been incurred on behalf of PMTE or services were received from the PMTE and the costs can be measured reliably and the transactions were not at arm's-length (not normal under the circumstances). The Department will disclose the nature of the related party transactions and the related costs. For example; the payment of accommodation on state owned property, salaries to PMTE employees, as well as other transactions with PMTE Finance.

Indirect Cost

Where cost cannot be measured reliably, due to estimation uncertainty, the Department will disclose the nature of all these transactions and the facts relating to these transactions

- Based on the analysis, the apportionment of the corporate services function (Finance and SCM, Ministry, DG, COO, construction property & policy regulations, internal audit, monitoring and evaluations, SMU, legal services, human resource, gender, people with disabilities, marketing and communication, IT, and security management) between the DPW and PMTE was the only identified indirect cost.

Previously the Department allocated such costs using an apportionment basis of 70% (DPW) and 30% (PMTE) for both the head office and the regions. The percentage split was not based on any rationale and during the 2012 audit the Auditor General provided feedback to the DPW to apportion the shared services costs based on a logical rationale.

- After much consideration and analysis, the Department addressed this issue with the National Treasury for guidance as the Department could not measure these costs reliably and the cost/benefit to perform this exercise would not be reasonable
- A ruling was obtained from National Treasury stating that the above indirect costs cannot be measured reliably and therefore the Department need only disclose the relationship and nature of the transaction.

The above exercise should be reviewed on an annual basis to ensure accuracy and completeness of all related parties identified for PMTE

Refer to the working papers for the detailed workings and conclusions reached

4.2 IDT

The primary goal of the Trust is to use its resources, together with strategic partners, in ways which, in the opinion of the Trustees, will best serve to enable poor communities in the Republic of South Africa to access resources and recognize and unlock their potential so as to continuously improve their quality of life.

IDT implement projects on behalf of the Department. The Department funds these projects by transferring amounts to the IDT. The IDT thereafter makes use of those funds and frequently provide reports to the Department indicating the progress of projects including the remaining funds not yet used which should be disclosed as commitments under the related party disclosure

The transfer of funds is however disclosed separately under Transfers and subsidies and does not form part of the related parties disclosure note.

In order to ensure completeness of transactions confirmation letter should be sent to IDT

4.3 Other identified related parties

The only transaction identified for the remaining related parties (ASA, CIDB, CBE, and PVMB) is that of transferring funds from the Department to them. This transaction is disclosed separately under Transfers and subsidies and does not form part of the related parties disclosure note.

To ensure completeness of transactions with these related parties, confirmation letters should be sent out to them regarding the transactions that occurred between them.

5. Conclusion

Transactions are to be disclosed for related parties if it is not at arm's length. Disclosure can either be qualitative or quantitative depending on whether the related party transaction can be measured reliably.

Disclosure of related parties that meets the above criteria shall be disclosed as follows:

- Name of the entity that entered into related party transactions with the department
- The types of the related party relationship
- The types of transactions that have occurred
- The elements of the transactions necessary to clarify the significance of these transactions to its operations and sufficient to enable the Annual Financial Statements to provide relevant and reliable information for decision-making and accountability purposes