

Is Accountability in the Management of Public Finances a Myth? The Case of the West Rand District Municipality

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Abstract: Several South African municipalities, including West Rand District Municipality (WRDM) had deposited funds into VBS Mutual Bank, which they subsequently lost because of the severe illiquidity that the bank experienced. On 11 March 2018, the then Minister of Finance, Mr Nhlanhla Nene placed the VBS mutual Bank under curatorship due the liquidity crisis, as explained above. This liquidity crisis was caused by amongst others what has been reported as grand theft of the bank's funds and fraud by allegedly amongst others, the bank's directors. The VBS theft and fraud case is currently being heard in court, and some of those who are alleged to have benefitted have been charged. Section 7(3)(b) of the Local Government: Municipal Finance Management Act (MFMA) 56 of 2003 requires municipalities to only open bank accounts such as investment accounts with banks registered in terms of the Banks Act 94 of 1990. Investments in mutual banks such as VBS are as such prohibited by the MFMA. As described above, the WRDM is one of the 14 municipalities, which were found to have illegally deposited money into VBS, whereby municipal officials and political office bearers are alleged to have personally benefitted for making such deposits. A forensic report by audit firm Deloitte, published in 2019 indicates that the WRDM may have lost as much as R224.5 million after illegally investing in the now-defunct VBS bank. The paper used the qualitative methodology wherein the materials used consisted of documents in the public domain. Through a careful analysis of both primary and secondary sources of information and statutes on local government finance, the researcher provides an in-depth and objective description of the case. The paper considered the necessary prerequisites that need to be in place to ensure accountability in the management of public finances at the WRDM, and come up with a framework that will highlight these prerequisites. The paper highlights three broad prerequisites in this regard, that is, following an accountability ladder, instituting internal controls and implementing a combined assurance model. The presence of these prerequisites could go a long way in ensuring that there is accountability in the management of public finances.

Keywords: Accountability, Internal control, Internal audit, Combined assurance, West Rand District Municipality

1. Introduction

The West Rand District Municipality (WRDM) is one of the 14 municipalities, which have been found to have illegally deposited money into VBS mutual Bank (hereafter referred to as VBS bank), whereby municipal officials and political office bearers are alleged to have personally benefitted for making such deposits. A forensic report by audit firm Deloitte, published in 2019 indicates that the WRDM may have lost as much as R224.5 million after illegally investing in the now-defunct VBS bank. The above-described state of affairs raises several questions regarding the municipality's management of public finances, internal controls and accountability where such controls are found to be weak or non-existent, such as when the municipality's funds were illegally deposited into a mutual bank. Of concern also is that neither the municipality's internal or external auditors discovered this transgression by the municipality.

The WRDM is a Category C municipality situated in the west of the Gauteng Province. Category C municipalities, are municipalities which have municipal executive and legislative authority in different areas that include more than one municipality (Republic of South Africa [RSA], 1996:75). The WRDM thus comprises three local municipalities: Merafong, Mogale and Rand West Cities. The municipality's main contribution to the economy is manufacturing (22%) followed by mining (19%), community services (19%), finance (16%), trade (10%), transport (6%), construction (4%) (West Rand District Municipality, 2021; Municipalities of South Africa, 2021).

The VBS bank was placed under curatorship due to what was termed a "severe liquidity crisis". This liquidity crisis was caused by amongst others what has been reported as grand theft of the bank's funds and fraud by amongst others, allegedly the bank's directors. The VBS theft and fraud case is currently being heard in court, and some of those who are

alleged to have benefitted have been charged. Several South African municipalities, including WRDM had deposited funds into VBS, which they subsequently lost because of the illiquidity that the bank experienced, as described above. Section 7(3)(b) of the Local Government: Municipal Finance Management Act (MFMA) 56 of 2003 requires municipalities to only open bank accounts such as investment accounts with banks registered in terms of the Banks Act 94 of 1990. Investments in mutual banks such as VBS are as such prohibited by the MFMA.

The aim of the paper is thus to consider the necessary prerequisites that need to be in place to ensure accountability in the management of public finances at the WRDM, and come up with a framework that will highlight these prerequisites. The question that the paper seeks to answer is: *What are the prerequisites that need to be in place to ensure accountability in the management of public finances at the WRDM?*

2. Methods and Materials

The WRDM has been selected as a case of typical accountability failures in South Africa's local government sphere. A single-case design was thus followed. The method deployed for the paper is qualitative, wherein the material for this paper consisted of documents in the public domain. Through a careful analysis of both primary and secondary sources of information and statutes on local government finance, the researcher set out to provide an in-depth and objective description of the case (Wood, Sebar, & Vecchio, 2020:458-459). Subsequently, the accountability implications of this case are analysed through the application of applicable theoretical lenses.

3. Theoretical Perspectives

The subsequent sections provide an exposition of theoretical perspectives relevant to answering the paper's research question.

3.1 Public Financial Management

Public financial management is defined as "the budgeting, accounting, internal control, flow of funds, financial reporting, and auditing arrangements by which governments receive funds, allocate them, and record their use" (World Bank, 2013:1). Good public financial management gives citizens

the assurance that their taxes are being used correctly, assures donors and lenders that the funds they provide are being used for their intended purpose, and demonstrates to the private sector that the government is able to provide an environment conducive for investment and growth.

Public finance is the cornerstone of any government, as it is through public finances that a government is able to provide services to its citizens. Government therefore should ensure that its income and expenses are managed efficiently and effectively through its budget. Public finance relates to the finances of the state in a multi-dimensional way as illustrated by the following factors:

- Public finance is evident in a government's budget, which is mainly financed through taxes, collected from both individuals and companies;
- Tax income enables a government to become a role-player in a country's economy; and
- Tax income collected by a government ultimately goes back into the economy through government spending the money on various items such as salaries and infrastructure development (Sharan, 1967:343; Thys, Wait, Cronje, Mthethwa, Sambo, Nzewi & Draai, 2020:13).

In the South African context, the advent of democracy in 1994 made it necessary for the government to apply sound financial management principles that would result in a public administration that is able to render better public services to all citizens. In this regard, Madue (2009:413) emphasises that accountability in service delivery and financial management is the cornerstone of democracy.

3.2 Accountability

Bananuka, Nkundabanyanga, Nalukenge & Kaawaase (2018:140) refer to accountability as "an obligation to demonstrate and take responsibility for performance in light of agreed expectations". Sambo & Kanyane (2020:7) define accountability as a prospect that one may be requested to explain one's actions or decisions. Eton, Murezi, Mwosi & Ogwel (2018:107) posit that accountability necessitates organisations to comply with all applicable laws, regulations, ethical standards and policies such as that for conflict of interest and whistleblowing. Banuka *et al.* (2018:140-141) further explain accountability as a

relationship between various parties, wherein there is an accountee and one who holds the accountee to account.

Accountability is regarded as holding elected or appointed individuals and institutions that have a public mandate accountable to the public for the actions, activities and decisions that they take or make. Accountability from a financial management perspective, is concerned with "the ability to account for the allocation, use and control of public spending and resources according to legally accepted standards with regard to budgeting, accounting and auditing" (Sambo & Webb, 2017:150). Accountability by public officials has a number of dimensions, which are explained in the form of a ladder which include accountability by standards and accountability by judgement.

The ladder of accountability as explained by Banuka *et al.* has five steps which translate into five dimensions of accountability. In the first three steps, public officials are required to show that they comply with legislations and demonstrate prudence in their conduct. The three steps comprise financial accountability, process accountability and performance accountability. Kanyane & Sambo (2021:203) refer to two types of financial accountability, that is, external and internal financial accountability. "The former refers to the obligation that institutions have to external stakeholders, such as customers and state agencies, while the latter refers to the obligations that internal stakeholders, such as staff, have toward each other" from a financial perspective.

Process accountability focuses on procedural matters and efficiency, whilst performance accountability focuses on the outcomes of activities for which an account has to be given. The last two steps comprise of programme accountability and policy accountability. These former focuses on the achievement of goals and objectives and the latter on the quality of policies (Banuka *et al.*, 2018:140). It is thus important for public officials and political office bearers to understand the various dimensions of accountability to be in a position to adequately account as would be expected in each of the dimensions.

In a similar manner Kuye *et al.* (2002:193) point out other dimensions of accountability, which are normally at play in public administration, which are worth noting. The extent to which the dimensions guide the behaviour of public officials is dependent

on the presence of transparency and the efficiency of democratic institutions, including the media. These dimensions are (Kuye *et al.*, 2002:193):

- a legal dimension, which refers to the rule of law;
- a fiscal dimension, which relates to the use of public funds;
- policy and performance dimensions, which refer to meeting goals, promises and expectations;
- a democratic dimension, which relates to democratic legitimacy and respecting democratic processes; and
- an ethical dimension, which refers to how individuals carry or conduct themselves in terms of codes of conduct or moral standards.

Public officials and political office-bearers would thus be expected to be accountable to the public when carrying out their duties in all of the above dimensions, in order to promote transparency.

3.2.1 Ethics and Accountability in Public Administration

Sambo and Webb (2017:150) refer to that section 195 of the Constitution of 1996 emphasises that there must be a high standard of professional ethics in the public sector and that ethics are the basis for governance as an ethical culture is necessary in ensuring that an institution is run ethically. Section 60 of the MFMA stipulates that the Municipal Manager of a municipality shall be the Accounting Officer of the institution. The accounting officer is accountable for all financial matters pertaining to that institution (RSA, 2003:50). An accounting officer has the responsibility of ensuring that the finances of an institution are managed as stipulated in the MFMA. However, accounting officers are dependent on other managers within the institution, who are accountable to them, in terms of managerial accountability. Managerial accountability is concerned with the delegation of responsibilities by an accounting officer to line managers in terms of legislation such as the MFMA. The aim of managerial accountability is to ensure that public institutions deliver services effectively, efficiently and economically, and that the necessary controls and procedures are adhered to (Kuye *et al.*, 2002:123; Pauw *et al.*, 2002:30; Fölscher & Cole, 2006:21). In

this regard, although the municipal manager of the WRDM, is the accounting officer of the municipality, they would have to rely on others to assist them in achieving institutional objectives.

Political analysis South Africa (2021) reports that on 29 June 2021, suspects on the VBS matter were arrested. These suspects included three former officials at the WRDM, that is, the former municipal manager, former chief financial officer and the former manager responsible for income and expenditure. The accused suspects altogether face 20 counts of corruption and two of contravening the MFMA as explained above. The inclusion of the former municipal manager, in those who have been charged with wrongdoing at WRDM is an unfortunate occurrence as this is the same person who ought to have safeguarded the municipality's financial resources in line with the MFMA as explained above.

3.2.2 Deficient Control and Accountability

Various authors emphasise that in public financial management, 'internal control systems' refer to various management tools that aim to:

- achieve, amongst other things, compliance with rules and regulations;
- ensure that the financial information of an institution can be relied upon; and
- enable an institution's operations to run effectively and efficiently (Sarens & De Beelde, 2006:463; Allen, Hemming & Potter, 2013:374).

A sound internal control framework is thus aimed at assuring the public that government operations have achieved basic fiduciary standards in areas such as:

- averting the misuse and inefficient use of financial and human resources;
- preserving assets;
- achieving budget objectives;
- avoiding fraud; and
- ensuring that financial information is produced on time and is reliable (Sarens & De Beelde, 2006:463; Allen *et al.*, 2013:374).

3.3 Internal Controls

Mukyala, Bananuka, Basuuta, Tumwebaze and Bakalikwira (2017:267) regard internal controls as standards, procedures, policies and rules used by an organisation's leaders to communicate the strategy and vision of the organisation. Sari, Ghozali, Achmad (2017:158) are of the view that an internal control system of government that has adopted the Committee of Sponsoring Organization framework (COSO) consists of five components, i.e. the control environment, risk assessment, control activities and information and communication, as well as monitoring.

Eton *et al.* (2018:107) posit that "the development of proper internal controls helps organizations ensure accountability". Similarly, Tumwebaze, Mukyala, Ssekiziyivu, Tirisa & Tumwebonire (2018:1) are of the view that internal controls coupled with managerial competencies are important predictors of accountability. Internal controls are thus expected to improve amongst others the quality of financial reporting, corporate governance and operating performance by reducing waste, misallocation of resources and corruption. From the above, the importance of internal controls to ensure accountability has been illuminated and this relationship will be considered further below when recommendations are made.

3.4 Internal Audit Function

Sarens and De Beelde (2006:464) suggest that internal auditors should be able to assist management in identifying substantial control failures and formulate recommendations for improvement. In doing this, internal auditors elevate their profiles, and are seen to be contributing to an effective internal control structure that improves the quality of information for decision-making purposes. The existence of an internal audit function is expected to result in a monitoring mechanism that is aimed at ensuring that resources within an organisation have been used economically and effectively (Sari *et al.*, 2017:157). Bananuka *et al.* (2018:141) refer to an internal audit function as a third eye of a board that reviews and evaluates internal controls, risk management and regulatory compliance. Furthermore, an internal audit function, as an internal assurance provider, plays an important role of enhancing accountability in the combined assurance model (Bananuka *et al.*, 2018:140). The objective of an internal audit

function is thus to improve the effectiveness of risk management, control and governance, whereby the function has capacity to protect organisations from internal criminal behaviour (Tumwebaze *et al.*, 2018:5).

3.4.1 Outsourcing the Internal Audit Function

Barac and Motubatse (2009:969) highlight that outsourcing is a management strategy of which public institutions could make use to delegate functions or activities formerly performed inside the public institution to specialised and efficient service providers. The authors further highlight that, although the practice of outsourcing functions is well established in the accounting environment, outsourcing the internal audit function, started to emerge during the 1980s. Similarly, Papageorgiou, Yasseen. Padia (2012:11828) suggest that outsourcing of the internal audit function is not a new phenomenon, and it dates back to the eighteenth century. However, the practice gained momentum in the latter half of the 1980s and 1990s. The practice of outsourcing the internal audit function was found necessary as a result of increased demands placed on the skills and competencies of internal auditors during the 1980s (Barac & Motubatse, 2009:969; Fourie & Erasmus, 2009:937). Barac and Motubatse (2009:970) further found that outsourcing of the internal audit function was a growing phenomenon, even in developed countries such as the United Kingdom.

Co-sourcing, where a partnership is entered into between a public institution's in-house internal audit function and its external provider was found to be a growing phenomenon (Fourie & Erasmus, 2009:937). The practice of co-sourcing enables an in-house internal audit function to retain responsibility for internal audit processes, while relying on the external provider for specialised technical skills and personnel, which it may not have. Fourie and Erasmus (2009:937) posit that the increased demands for internal audit services have placed strain on available resources in the function. These resource constraints have led to the co-sourcing or outsourcing of internal audit activities. In this regard, the WRDM has an internal audit function which it shares with its agencies. Lapses have occurred at the municipality and continue to occur as reported by the AGSA and highlighted below. The effectiveness of the municipality's internal audit function could thus be considered with a consideration for co-sourcing.

3.5 External Audit

External auditors are auditors who are independent of the institution being audited. They play the role of providing confirmatory services to an organisation's reports (IrwanAdimas & Achmad, 2019:2). The Auditor-General South Africa (AGSA) performs the external audit function in most of South Africa's public institutions, as provided by the Public Audit Act 25 of 2004 as amended. The WRDM's external audit function is also performed by the AGSA. The AGSA's findings on the WRDM will be reported on below.

3.6 Combined Assurance

Institute of Directors Southern Africa [IoDSA] (2016:10) avers that a combined assurance model aims to enhance and incorporate all assurance providers to enable an effective control environment, support the integrity of information used by management for decision-making as well as external reports of the organisation. Assurance providers in an organisation *inter alia* are: internal auditors and external auditors, whilst the role of an audit committee in this regard is to ensure that the aforementioned assurance providers are fulfilling their duties satisfactorily (IoDSA, 2016:55; cf. Maroun & Prinsloo, 2020:3702). IrwanAdimas and Achmad (2019:2) raise the importance of external auditors partnering with external auditors in an institution as internal auditors have more knowledge of an institution which would assist external auditors in producing more accurate reports.

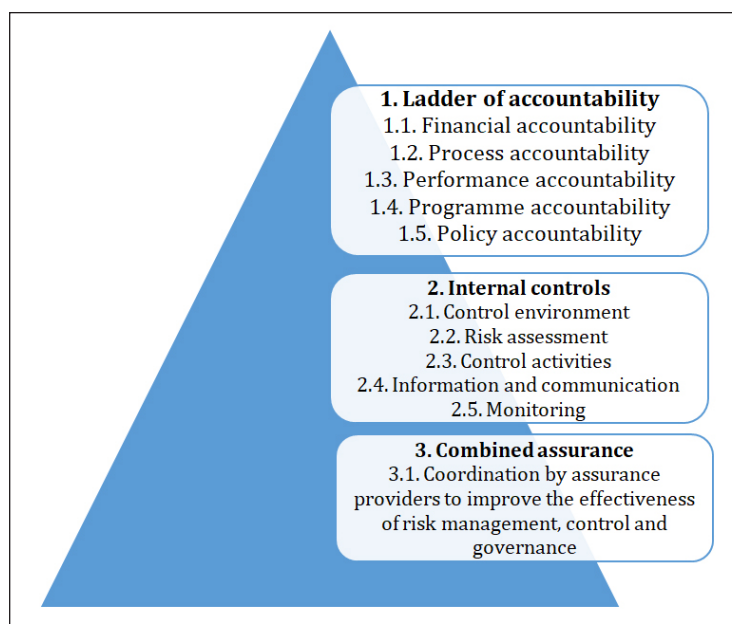
The revelations from the theoretical perspectives highlighted above will inform the recommendations that will be made below.

4. Results and Discussion

The findings of the paper have been summarised in Figure 1 on the following page.

4.1 Auditor-General South Africa Findings on West Rand District Municipality

The WRDM's financial position has reportedly worsened after the municipality invested R76 million in VBS Mutual Bank which was subsequently written off as a financial loss. According to AGSA (2019:56) the gradual weakening of the control environment, weak cash management controls, including a lack

Figure 1: Summary of Theoretical Perspectives


Source: Author's construction

of regular bank reconciliations are the reasons for this financial loss. Accordingly, the amount invested in VBS by WRDM included a R43 million 'neighbourhood development partnership conditional grant' received from the National Treasury. Service delivery was thus negatively affected as money meant to contribute to service delivery in the municipality was diverted from projects that could have benefitted the community. The National Treasury subsequently recovered the lost grant money by reducing unconditional grant funding to WRDM during the 2018/19 financial year (AGSA, 2019:56). AGSA (2019:49) reports on amongst others municipalities whose performance reporting had regressed. The WRDM is one of these municipalities. The reasons furnished by the AGSA for this regression is an absence of necessary controls for performance reporting which were not adequately monitored. "Instead, they focused only on areas raised as findings in prior years which led to similar findings when municipalities added new service delivery performance indicators or when new performance indicators were audited" (AGSA, 2019:49). AGSA (2020:127) alludes to that the implementation of financial improvement strategies at WRDM remains in progress.

4.2 Literature Findings

In providing literature perspectives key to answering the research question: *What are the prerequisites*

that need to be in place to ensure accountability in the management of public finances at the WRDM? relevant literature in public financial management was considered. The importance of accountability and financial management was emphasised. The critical role played by internal controls in reducing the occurrence of unlawful activities such as what occurred at the WRDM was emphasised. When it comes to assurance providers who are supposed to advise management on the said internal controls, it was shown that working together, the internal audit function and external auditors of an institution can improve the accuracy of reports produced. Thus, in answering the paper's research question, from the literature, several prerequisites can be identified, as depicted in Figure 1.

Figure 1 above attempts to answer the paper's research question by highlighting the prerequisites that have emerged from the literature as necessary in ensuring that there is accountability in the management of public finances.

5. Conclusion and Recommendations

The liquidity crisis at VBS bank exposed illegal activities that were taking place in various municipalities, including the WRDM. The AGSA has found that service delivery projects at the WRDM were compromised as a result of money having been redirected from these projects into investments at

VBS bank in contravention with the MFMA, which prohibits investments in mutual banks. The lapses that occurred at the WRDM when the illegal investments were made have raised several questions around the municipality's internal control environment and whether those who transgress are held accountable for the transgressions. The paper set out to answer the following question: *What are the prerequisites that need to be in place to ensure accountability in the management of public finances at the WRDM?*

In answering the above question, various literature was consulted as well as official documents such as those of the AGSA, who is the supreme auditor of public institutions in the Republic of South Africa as provided for in the Public Audit Act 25 of 2004 as amended. The AGSA has reported on the deficient internal control environment at the WRDM, which could be attributed to lapses that have occurred and continue to take place. To address these lapses, the paper has considered various literature on public financial management, which points to various prerequisites which have to be in place to ensure accountability in the management of public finances. These prerequisites can be summarised under the broad topics of following a ladder of accountability, instituting internal controls and having a combined assurance model.

A ladder of accountability has to be understood by public officials and political office bearers to ensure that they adequately account as would be expected in each of the dimensions of the ladder. Instituting internal controls is critical as although internal controls do not eliminate lapses all together, they have a potential to reduce the occurrence of lapses. A combined assurance approach is necessary as when there is cooperation between assurance providers, chances are they will work together in providing quality reports to management and ultimately contribute to an improved internal control environment. The framework provided in this paper contributes to the body of literature on public financial management, with a view of addressing challenges experienced in many of South Africa's public institutions such as the WRDM.

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