

SECTIONAL TITLE PROPERTY IN SOUTH AFRICA: AN ACCOUNTING AND AUDITING PERSPECTIVE

by

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DECLARATION

I declare that the dissertation hereby handed in for the qualification Magister in Accounting and the University of the Free State is my own independent work and that I have not previously submitted the same work for a qualification at/in another university/faculty.

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SUMMARY

This study was undertaken against the background of the current housing problem in South Africa. Sectional titles play an important role in addressing this challenge, which is a high priority problem in the country. Very little research has so far been done on the South African sectional title industry from an accounting and auditing perspective. Furthermore, legislation in this regard is often contradictory and confusing. In addition, pressure regarding costs such as audit fees and management fees from owners of sectional title units bring about unique challenges and problems for the industry. These aspects do, however, provide ample opportunity for research.

The first main aim of this study was an overview of practical problems experienced from an accounting and auditing perspective regarding risks associated with sectional titles, auditing-specific problems relating to sectional title and accounting-specific problems relating to sectional title. The second, two-fold aim of the study was to find possible solutions to the above-mentioned problems and to make recommendations in this regard. The third aim of the study was to set industry benchmarks by way of analysis and interpretation of a sample of annual financial statements of sectional title schemes over a three year period. These benchmarks can be of assistance as an industry standard for owners, trustees, managing agents, auditors and accountants rendering a professional service within the sectional title industry.

The literature review of this study covered three main aspects in respect of sectional title schemes, namely legal aspects relating to accounting and auditing matters of sectional title schemes, auditing and assurance aspects and accounting and reporting aspects.

The literature review paved the way for a detailed analysis of the auditing and accounting aspects relating to the sample of body corporate financial statements and an empirical study performed on the sectional title industry in South Africa by way of interviewing a sample of role players in the industry.

The results of the empirical study and data analysis revealed a great number of contradictory and confusing legal aspects as well as uncertainties in the industry. Various problems and concerns were addressed and practical recommendations were made of which the industry should take note. The empirical findings can also be used as a valuable basis for further research.

Key words: sectional title, sectional title management, accounting, auditing, sectional titles act, participation quota, financial statements of sectional title schemes, audit reports of sectional title schemes, sectional title budgets, auditing profession, accounting profession.

OPSOMMING

Hierdie studie is onderneem teen die agtergrond van die heersende behuisingsvraagstuk in Suid-Afrika. Deeltitels speel 'n baie belangrike rol om hierdie hoë-prioriteit uitdaging aan te pak. Daar is nog baie min navorsing gedoen oor die Suid-Afrikaanse deeltitel-industrie, spesifiek vanuit 'n rekeningkundige en ouditkundige perspektief. Verder bestaan daar baie teenstrydige en verwarrende wetgewing oor hierdie industrie. Kostedruk deur eienaars van deeltiteleenhede op onder meer oudit- en bestuursfooi bied verder eiesoortige uitdagings en probleme vir die industrie. Hierdie aspekte bied egter baie geleenthede vir navorsing.

Die hoofdoel van hierdie studie was 'n oorsig oor die praktiese probleme wat vanuit 'n rekeningkundige en ouditkundige perspektief ondervind word ten opsigte van die risiko's wat met deeltitels geassosieer word, sowel as rekeningkundige en ouditkundige probleme wat met deeltitels verband hou. Tweedens is oplossings vir bogenoemde probleme en aanbevelings ten doel gestel. Derdens was dit 'n mikpunt om riglyne daar te stel na aanleiding van die ontleding en vertolking van 'n steekproef finansiële jaarstate van deeltiteleiendom wat oor 'n drie-jaar tydperk gedoen is. Hierdie riglyne kan as 'n moontlike industrie-standaard dien vir eienaars, trustees, bestuursagente, en ouditeure en rekenmeesters wat professionele dienste aan die deeltitel-industrie lewer.

Die literatuuroorsig van die studie fokus op drie hoofaspekte aangaande deeltitelskemas, naamlik, regsaspekte rakende rekeningkundige en ouditkundige kwessies, ouditkundige- en gerusstellingsaspekte en rekeningkundige- en verslagdoenings-aspekte.

Die literatuuroorsig baan die weg vir 'n uitvoerige ontleding van die ouditkundige en rekeningkundige aspekte van 'n steekproef finansiële jaarstate asook 'n empiriese studie gedoen oor die deeltitel-industrie in Suid-Afrika deur middel van onderhoude wat gevoer is met 'n steekproef rolspelers in die industrie.

Die resultate van die empiriese studie en data-ontleding onthul verskeie teenstrydige en verwarrende regsaspekte en onsekerhede in die industrie. Verskeie probleme en kommerwekkende aangeleenthede is aangespreek en praktiese aanbevelings is gemaak waarvan die industrie kennis behoort te neem. Die empiriese gevolgtrekkings kan ook gebruik word as 'n waardevolle grondslag vir verdere navorsing.

Sleutelwoorde: deeltitel, deeltitelbestuur, rekeningkunde, ouditkunde, deeltitelwet, deelnemingskwota, finansiële state van deeltitelskemas, ouditverslae van deeltitelskemas, deeltitelbegrotings, ouditprofessie, rekeningkunde professie.

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“To thank others is to recognise that we are not alone and that our path is shared by those who accompany us.” – Montserrat Figueras

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LIST OF ABBREVIATIONS

AG	: Auditor General
AGSA	: Auditor General of South Africa
APB	: Accounting Practices Board
CA(SA)	: Chartered Accountant (South Africa)
CC	: Close Corporation
EAAB	: Estate Agency Affairs Board
FRSC	: Financial Reporting Standards Council
GAAP	: Statements of Generally Accepted Accounting Practice
IASB	: International Accounting Standards Board
IASC	: International Accounting Standards Committee
IASCF	: International Accounting Standards Committee Foundation
IEASA	: Institute of Estate Agents of South Africa
IFRIC	: International Financial Reporting Interpretations Committee
IFRS	: International Financial Reporting Standards
IFRS for SMEs	: IFRS for Small and Medium-sized Entities
IoD	: Institute of Directors in Southern Africa
IRBA	: Independent Regulatory Board for Auditors
ISA	: International Standard on Auditing
ISAs	: International Standards on Auditing

NAMA : National Association of Managing Agents
SA GAAP : South African Generally Accepted Accounting Practice
SAICA : South African Institute of Chartered Accountants
SAIPA : South African Institute of Professional Accountants
SARS : South African Revenue Services
SMEs : Small and Medium-sized Entities
STA : Sectional Titles Act

CHAPTER 1 – INTRODUCTION AND STUDY LAYOUT

“And Jesus said to him ‘Foxes have holes and birds of the air have nests but the Son of man has no place to rest his head.’” - Luke 9:24 - NKJV

1.1. BACKGROUND

Homeownership is one of the building blocks in the development of a stable society (Ed., 2005, p. 22; Conostas & Bleijs, 2009, p. int; Pienaar, 2010, p. 3). The pride in owning one’s own home, however humble it may be, should never be underestimated. (See also Maree (2011, p. 3).) The great 20th century American architect Frank Lloyd Wright once said that one should *“regard it as just as desirable to build a chicken house as to build a cathedral”*. In Luke 9:58, Jesus also told a man that *“Foxes have holes and birds of the air have nests but the Son of man has no place to rest his head.”* (NKJV)

Housing in South Africa is at the forefront of the national agenda for delivery by the government and other non-governmental organisations (Lekota, 2009, p. 13; Timse, 2008, p. 4). Various housing-subsidy instruments are being made available by the government to assist low-income households in gaining access to housing (Department: Human Settlements Republic of South Africa, 2009). It is important to note that while a considerable amount of information is available on the housing situation in South Africa, the data are at times contradictory. There are often differences between data produced by the government and data derived from independent surveys on the same issue (Hemson & O'Donovan, 2005, p. 17). More than 2.6 million houses have been built for the poor since the start of the new democracy in South Africa in 1994 (Lekota, 2009, p. 13; Ed., 2008, p. 6), and the government has made the commitment to eradicate all

squatter camps by 2014 (Hosken & Mbanjwa, 2007, p. 17; Cilliers, 2008, p. 10; Benjamin, 2007, p. 3). The aim of the South African government is further to provide fully-subsidised housing to the poor and creating housing for approximately 7 million households by 2014 (Hemson & O'Donovan, 2005, p. 17; Witepski, 2009, p. 91).

Unfortunately, many of the RDP (Reconstruction and Development Project) houses built since 1994 have been reported to be sub-standard and of poor quality (Ebersohn, 2011, p. 2). The government has already spent more than R500 million in destroying and rebuilding some of these houses, and the total cost of this national project is estimated to be more than R2 billion (Lekota, 2009, p. 13; Ed., 2008, p. 6; SAPA, 2009).

Furthermore, many provincial governments are not reaching the targets set by national government (Ebersohn, 2011, p. 2) and the current backlog in housing therefore continues to grow (Lekota, 2009, p. 13; Van Rooyen, 2008, p. 6; Ed., 2004, p. 6). During 2011 it was reported that the provincial governments of the Western Cape, Eastern Cape, KwaZulu-Natal and the Free State were not reaching monthly targets for the building of low-cost housing. The Free State Province, for example, spent only 19% of their housing budget during the first six months of the 2010-'11 financial year (SAPA, 2011). The national government considered channeling the allocated funds to other provinces that are reaching their targets and are not underspending (Ebersohn, 2011, p. 2). The gravity of the housing issue in South Africa is further evidenced by the fact that the Auditor General of South Africa (AGSA) embarked on performance audits of the approval and allocation of housing subsidies at the Department of Local Government and Housing in four Provincial Administrations throughout South Africa in 2005/2006 (AGSA, 2006). The provinces under audit by the AGSA during the 2005/2006 financial year was the Free State, Northern Cape, Limpopo and Gauteng, and various exceptions were raised in the respective reports by the AGSA. (See also Crous (2012, pp. 225-235) and Khalane (2012, p. 4).)

The above-mentioned situation is also evidenced in academic research. In a recent study undertaken by Coetzee (2010, p. 306) the risk maturity of a sample of private sector as well as national government organisations were investigated. The results of the study showed that none of the national government organisations investigated were risk mature and the study therefore concluded that for public sector organisations, the implementation of a risk management framework is a great concern. A recent study on the audit reports of the Free State Provincial Departments (Crous, 2012, p. 255) further showed that the Free State Department of Local Government and Housing received qualified audit reports from the Auditor General for the years 2007/2008, 2008/2009 and 2009/2010. The Auditor General launched a special investigation into subsidies paid to individuals employed in the national, provincial and local departments in the 2007/2008 and 2008/2009 financial years (Crous, 2012, p. 257). The study also revealed a serious lack of control over actual service delivery by support organisations over several years. The Auditor General identified various projects that were not completed; irregular, fruitless and wasteful expenses amounting to millions of rands; poor quality of materials used in projects and sub-standard workmanship.

It is estimated that South Africa's current population of roughly 48 million will grow to approximately 50 million by 2020 (Cilliers, 2008, p. 10). Statistics show that the number of households in South Africa has increased by 45% or 4 million units from 1995 (Cilliers, 2008, p. 10; Hemson & O'Donovan, 2005, p. 17). The number of households in the country is increasing at a faster rate than the growth in population. As the number of households increase, the number of people per household decreases. It is, therefore, not surprising that the average number of people in one household was 4.7 in 1995, but dropped to 3.7 in 2007 (Cilliers, 2008, p. 10). The rapid increase in households, as well as limited resources and financial shortfalls in local government (Essop, 2008, p. 2; Steenkamp, 2008, p. 8; Peyper, 2008, p. 7) can lead to an even greater backlog in housing than the current estimated 2.8 million (Lekota, 2009, p. 13; Van Rooyen, 2008, p. 6). This is also discussed by Ebersohn (2011, p. 2).

The above situation is further aggravated by the mostly uncontrolled influx of immigrants, especially from Zimbabwe, Tanzania and Mozambique, into South Africa (Ed., 2010, p. 6; Chikanga, 2012, p. 4; Landau, 2012, p. 14). In 2010, researchers estimated that there were around 650 000 Zimbabweans living in Johannesburg (Kuljian, 2010, p. 31). The majority of these immigrants are desperate for housing, and take refuge in precarious and unhygienic circumstances in run-down buildings in cities throughout South Africa (Bega, 2010, p. 2; May, 2010, p. 19). Le Roux (2010, p. 13) reports that in May 2010 it was estimated that nearly 30 000 “survival immigrants” were living in 40 of the 1 000 buildings that were classified as dilapidated by the Johannesburg municipality and that roughly 3 000 illegal immigrants were seeking refuge in the Central Methodist Church in central Johannesburg (Rabkin, 2010, p. 2; Kuljian, 2010, p. 31; Takali, 2010, p. 2; Cilliers, 2010, p. 6). The inflow of immigrants into South Africa has also sparked various incidents of xenophobic violence throughout South Africa between 2008 and 2012 (Ed., 2010, p. 14; Mboya, 2010, p. 20; Chikanga, 2012, p. 4; SAPA, 2011, p. 3). (See also Landau (2012, p. 14) and Hosken (2011 , p. 1).)

Linked to the housing issue in South Africa is the significant rise in incidents of building hijacking during the past few years, where syndicates illegally take over buildings and rent out rooms to desperate tenants (Molosankwe, 2010, p. 2). These rooms are often rented out at extortionate prices, the living conditions are usually unhygienic and the buildings quickly turn into crime-ridden slums (Ed., 2010, p. 14; Ed., 2010, p. 28; Thakali, 2010, p. 5). Many of these buildings do not have running water, electricity or basic sanitation (Damons, 2010, p. 10; Moeng, 2010, p. 7). Sources vary on the exact number of hijacked buildings in South Africa, but during 2010 the Johannesburg municipality reported that there were approximately 1 200 dilapidated buildings in the inner city of Johannesburg alone, of which approximately 400 have been hijacked (Bradlow, 2010, p. 13; Damons, 2010, p. 6). The government and police have launched various initiatives to deal with the issue in recent years (Cokayne, 2010, p. 20; Ndaba, 2010, p. 3; Cox, 2010, p. 2; Cox, 2010, p. 2).

While the government is attempting to take care of mainly the very lower-end households, some private market developers take care of the needs of high-end homeowners. In-between the two extremes there remains a large, ever-growing market sector. At the lower end of this market sector are many low-income households in South Africa earning between R3 500 and R5 000 per month that do not qualify for RDP houses, as these houses are meant for the poor. At the same time, these households do not qualify for housing loans (Nkalane, 2010, p. 6). Their level of income make it impossible to afford even the cheapest house in the “affordable housing” market segment (Kloppers, 2010, p. 16; Ed., 2010, p. 16). At the higher end of the market sector are the potential middle-end homeowners – an estimated 3.7 million households that can afford a house between R130 000 and R500 000 (Witepski, 2009, pp. 89-91). These households also do not qualify for government subsidies, nor can they afford luxury high-end residential property. Seen in the light of the previously mentioned increase in households, as well as changing market dynamics, the number of households in this category is set to keep expanding in future. It is, therefore, clear that in future South Africa will require thousands of affordable housing units near urban employment sites (Witepski, 2009, pp. 89-93; Herman, 2007, p. 6). (See also Muller (2010, p. 37) and Fife (2010, p. 46).)

During the past few years the media has regularly reported on fraud and corruption occurring with the renting of government housing, government housing projects (Mbanjwa, 2011, p. 8; Phakathi, 2011, p. 3; Nkomo, 2011, p. 4; Ngudle, 2011, p. 1) and especially circumvention of waiting lists (also called “indigent lists” or “beneficiary lists”) for low-cost housing (Essop, 2011, p. 2; De Kock, 2011, p. 4; Barnard, 2011, p. 4). (See also Teke (2012, p. 1), Essop (2012, p. 1) and Dorasamy (2011, p. 1).) These incidents contribute to the housing backlog in South Africa.

The housing backlog in South Africa means that all possibilities must be explored, and Sectional title property can address this problem to a great extent, especially in the

middle-income market. Specific mention is made of the major role sectional ownership can play in public housing projects by Van der Merwe (2010, p. 22). He rightly states that the aim of sectional ownership is to provide urgently needed residential accommodation for households of all income levels, within commuting distance of employment centres. (See also Herman (2007, p. 6), Nel (1999, p. V), Benjamin (2007, p. 3), Van Wyk (2005, p. 12) and Pienaar (2010, pp. 9-10)).

At the commencement of the study, in-depth research searches were done by the research specialists at the academic libraries of the Central University of Technology, Free State and the University of the Free State as well as the Archive for Contemporary Affairs at the University of the Free State. The candidate also performed extensive searches at the above libraries and archives as well as on the internet. These searches revealed that very little academic research has so far been done on sectional titles in South Africa. The academic research identified was mostly postgraduate research in the fields of law, cost accounting, taxation and regional planning. All of the dissertations were completed before 1999 and dated back as far as 1988. It was thus determined that no academic research has been done specifically from an accounting and auditing perspective to date on the sectional title industry in South Africa.

In the rest of the first chapter of this study the concept of sectional title property in South Africa, as well as the governance and management thereof will be introduced briefly. The need for a study regarding an accounting and auditing perspective on sectional title property in South Africa will also be addressed. The problem statement, aim of the study, research methodology and the contents of the study will also be discussed and the chapter will be closed with a concluding section.

1.2. SECTIONAL TITLE PROPERTY IN SOUTH AFRICA – BACKGROUND AND OVERVIEW

In this section, a brief overview of sectional title property in South Africa will be given for background purposes. This aspect will be dealt with in detail in Chapter 2 of the study.

Before the early 1970's, the concept of sectional ownership was not recognised in South Africa. It was impossible to obtain full ownership rights to a section of a building such as an apartment. Woudberg (1999) and Van der Merwe (2010) give an overview of the legislative history of sectional title property in South Africa.

In South African law, the maxim *superficies solo cedit* was taken over from Roman Dutch law (an ultimately Roman law), in terms of which a landowner was also considered to be the owner of any building erected on the land, and a building was seen as a single unit (Van der Merwe, 2010, pp. 15-16; Pienaar, 2010, p. 22). Ownership consisted of the entire building, which could not be bought in separate parts. This means that South African law did not recognise separate ownership in a building or parts of that building apart from the ownership of the land on which the building was built (Van der Merwe, 2010, pp. 15-16; Woudberg, 1999, p. 3). (See also Shrand (1972, p. 1)).

The Great Depression of the 1930's and the two World Wars caused a world-wide decline in social and economic conditions. This resulted in a desperate shortage in housing (Van der Merwe, 2010, pp. 5-6). Several factors played a role in the shortage of accommodation close to centres of employment, including an increase in the population, immigration, the flow of people to the cities due to better job opportunities and increased costs of land and building materials. In those years, inflation also became a harsh reality, and the rising cost of residential property made it increasingly difficult for

the average household to afford a freestanding property. Due to the aforementioned reasons, many households could only afford to buy a section of a building, for example an apartment, but it was legally impossible to obtain full ownership of a property such as a flat or apartment (Van der Merwe, 2010, pp. 15-16; Woudberg, 1999, p. 3).

Legal systems around the world were compelled to consider the institution of legislation on sectional ownership, and South Africa was no exception. The Sectional Titles Act came into being in 1971, and this enabled homeowners to purchase a section of a building, such as an apartment, with full ownership rights on that section (Van der Merwe, 2010, pp. 15-16; Woudberg, 1999, p. 3; Shrand, 1972, p. 1; Nel, 1999). (See also Paddock (2008, pp. 1-3).) The Sectional Titles Act No. 66 of 1971 was later replaced with the Sectional Titles Act No. 95 of 1986 (Van der Merwe, 2010, pp. 15-16). The Sectional Titles Act 95 of 1986 has been amended by Act No. 11 of 2010, which was published in the Government Gazette on 7 December 2010. The Sectional Title Schemes Management (STSM) Act 8 of 2011 was gazetted and signed by the President in mid-2011. The STSM Act does not repeal the original Sectional Titles Act 95 of 1986 (as amended), but does repeal and/or amend certain provisions thereof. However, by the end of 2012 the STSM Act was still not operational (Padayachee, 2012, p. 1; Ed., 2012, p. 1).

Apart from the reasons mentioned in the paragraphs above, several other factors also contribute to the charm and appeal of the concept of sectional title. Urbanisation contributes greatly to the shortage in housing in the vicinity of employment hubs in South Africa. People move from rural to urban areas for reasons such as the hope of a higher standard of living and better job opportunities, to name but a few. A report by Statistics South Africa (2006, pp. 21-25) on migration and urbanisation in South Africa shows that the majority of the population (56%) is living in urban areas and that there has been a steady increase in the proportion of urbanisation over time. (See also Maree (2011, p. 3).) It is stated that an increase in the level of urbanisation can be expected in

the foreseeable future. This fact is also substantiated by a report by the United Nations (2004, p. 2). It is stated that in 2003, 39% of the population in Africa lived in urban areas, and that the figure is expected to increase rapidly, so that by 2030, 54% of the African population will live in urban areas. Against this background, an important aim of the Sectional Titles Act is to encourage the rapid provision of urban accommodation.

Another important matter that sectional ownership aims to address is the issue of utilisation of land resources. Residential property in city centres and urban employment hubs is expensive as well as scarce (Ed., 2009, p. 42; Smith, 2009, p. 2; Van der Merwe, 2010, pp. 19-22; Gerber, 2005, p. 6). Sectional title makes it possible to use available land optimally, and spread construction cost between several owners. If a piece of land is, for instance, used for a residential development such as a high-rise building, the population density is potentially much higher and the cost much lower than when using the land for single-family housing (Van der Merwe, 2010, p. 20).

Sectional title has over the years also proved to be very popular from an investment perspective. The provision of housing units in sectional title developments has generally proven to be more affordable than single housing units. The lower cost can be attributed to various factors such as sharing of walls, floor, corridors, and driveways as well as a more efficient utilisation of land, to name but a few. This can result in a reduced cost per unit, making an investment in sectional title very attractive and also bringing homeownership within reach of households who cannot afford a conventional single-housing unit (Woudberg, 1999, p. 5; Van der Merwe, 2010, p. 21). According to Wessels (2011, p. 17) property economists at FNB believe that, due to the rising cost of housing maintenance, flats and townhouses will form the bulk of South Africa's residential property in a few years' time.

A further matter which, from a South African perspective, requires specific mentioning is the aspect of safety. One simply needs to open a newspaper to become aware of the issue of crime in the country and safety becomes an increasingly important consideration when choosing a place to live (Pienaar, 2010, p. 11). In a sectional title complex, residents generally live in close proximity to each other and security is usually tighter than in traditional houses (Van der Merwe, 2010, pp. 19-22; Woudberg, 1999, p. 5). Other advantages of sectional title living include a lower maintenance burden on the owner, sharing of otherwise expensive common amenities, and a closer social life (Pienaar, 2010, p. 11).

It should be noted that the Sectional Titles Act governs not only residential property. The Act places no restriction on the type of building that can be utilised. Units in buildings that are acquired under sectional ownership can include factories, offices, retail space and warehouses. Van der Merwe (2010, p. 25) lists various advantages of industrial or commercial sectional ownership. One of the advantages that are especially relevant to the South African economy is that entrepreneurs and small enterprises that will otherwise have to rent a section of a building will be able to purchase suitable premises under sectional ownership.

As mentioned earlier in this chapter, the concept of sectional title emerged in answer to various socio-economic needs. Before sectional title ownership was introduced in South Africa, the only way in which a person could own a single apartment in a building was by way of share block ownership (Constas & Bleijs, 2009, p. 209). Share block schemes are regulated by the Companies Act of 1973 and the Share Block Control Act of 1980. Buying into a share block scheme actually entails purchasing “shares in a company” and not the actual apartment (Woudberg, 1999, p. 3; Van der Merwe, 2010, p. 19; Pienaar, 2010, pp. 293-301). This share only entitles the owner of the share to occupy and use a particular portion of the property that is owned by the share block company. In short, there is a difference in the nature of the right acquired between

sectional title ownership (a real right) and ownership of a share in a share block company. In the case of a share block company being declared insolvent, the shareholder would only have a concurrent claim against the loan account of the company, and could possibly lose most of his/her investment (Constas & Bleijs, 2009, p. 211; Van der Merwe, 2010, pp. 19-21). Sectional title property is, therefore, a much more secure form of investment than share block ownership (Woudberg, 1999, p. 3; Constas & Bleijs, 2009, p. 211; Pienaar, 2010, p. 336).

Another property concept that has gained popularity in South Africa, especially in the holiday and tourism market over the last 30 years, is time-sharing (Pienaar, 2010, p. 9). Time-sharing can be defined as any right to, or interest in the exclusive use or occupation of property, whereby a number of persons can successively occupy property during specified or determined or determinable recurrent periods in any year (Van der Merwe, 2010, p. 72; Pienaar, 2010, p. 411). The concept is generally applied to the shared use of accommodation for holiday purposes during certain periods per year. For example, a time-share holder can occupy a specific unit in a block of flats by the seaside for the last three weeks of December each year (Van der Merwe, 2010, p. 72). This form of property scheme as well as the concepts of share block schemes and retirement schemes falls outside the scope of this study.

Over the past few years, the property industry in South Africa has been hit by a number of large fraud scandals such as the cases of the Theodosiou brothers in 2008, King Financial Services in 2009, Sharemax in 2010 and Wendy Machanik in 2011 (Wessels, 2011, p. 18). One of the largest and most recent incidents was the case of Constantia Sectional Title Management (CSTM). The cover feature of Finweek magazine of 18 August 2011 stated that the sectional title industry was "in the crossfire" (Wessels, 2011, pp. 14-18). CSTM collected millions of rand in fees from its clients and that was then deposited into a single trust account. The CEO, Quentin Brown, was a signatory of the account and he allegedly misappropriated between R20 million and R40 million from

about 20 000 flats and townhouses around Gauteng. (See also Du Plessis and Mkondo (2011, p. 5), Kloppers (2011, p. 4), SAPA (2011, p. 23) and Kloppers (2011, p. 2).)

1.3. GOVERNANCE AND MANAGEMENT OF SECTIONAL TITLE

This section aims to give a brief introductory overview on corporate governance with the King Report as focus point. In the sections of the study dealing with the literature review regarding, for example, legal aspects as well as the sections dealing with the empirical findings further reference will be made, where applicable, to the relevant aspects of corporate governance.

Good corporate governance is beneficial to all types of enterprises, small as well as large (KPMG, 2012, p. 8). The King III Report on Governance for South Africa (2009) as well as its two preceding publications (King I (1994); King II (2002)) is recognised as arguably the best and most well-known publications on governance in the world (Institute of Directors in Southern Africa, 2009, p. 5). (See also Rossouw, Du Plessis, Prinsloo & Prozesky (2009, p. 156), Rossouw & Van Vuuren (2010, pp. 211-212), Fisher & Lovell (2006, pp. 307-308), Rossouw et al (2012, pp. 168-170) and Ghillyer (2008, pp. 81-82).) The first King Report was published in 1994 by the Institute of Directors in Southern Africa (IoD). The so-called King Committee, under the chairmanship of Professor Mervyn King, successfully formalised the need for companies and other entities to recognise that they no longer act independently from the environment and societies in which they operate (Fisher & Lovell, 2006, p. 307). Eight years later, in 2002, the King II Report was one of the first codes of corporate governance to consider the concept of “triple bottom line” reporting, as opposed to the traditional single bottom line of profitability. King II recognised that stakeholders required forward-looking information, considering the economic, environmental and social reality of an entity’s activities. The Report also placed great emphasis on risk management and the importance of ethics (Rossouw, Du Plessis, Prinsloo, & Prozesky,

2009, p. 156; Ghillyer, 2008, p. 80). In 2009, King III was compiled by the King Committee assisted by the King subcommittees, in response to changes in international governance trends and the new Companies Act no. 71 of 2008, emphasizing the importance of conducting annual business reporting in an integrated manner (Institute of Directors in Southern Africa, 2009, p. 5).

King III focuses on the concept of integrated business reporting and the importance of putting financial results in perspective by also reporting on the positive and negative impact of entities on the economic life of the community in which it operates, as well as intentions to enhance or eradicate such impact. In contrast to the King I and II codes, King III makes recommendations about best practices in corporate governance applicable to **all entities**, regardless of the manner and form of incorporation or establishment and whether in the public, private sectors or non-profit sectors (Institute of Directors in Southern Africa, 2009, p. 17; Rossouw & Van Vuuren, 2010, p. 211). (See also Le Roux (2010, p. 1) and KPMG (2012, pp. 8, 38).) It is therefore evident that the fundamental principles of corporate governance are not only applicable to companies and directors of companies (Ed, 2006, p. 2). Entities such as sectional title schemes, together with its bodies corporate and trustees, should also apply the principles in the Code and consider the best practice recommendations in the Report. The Report states that all entities should, by way of explanation, make a positive statement about how the principles have been applied or have not been applied (Institute of Directors in Southern Africa, 2009, p. 17). (See also Ed (2006, p. 2).) Terms such as “directors” and “management” used in the King III Report can therefore be substituted with “trustees” and “body corporate”.

In smaller entities, it is often found that directors, board members, trustees and partners do not fully understand all the risks associated with occupying the relevant position. The application of principles of good corporate governance should play a significant role in giving these individuals clarity on their powers, duties and responsibilities, as well as

informing them of the risks associated with such a position. The aforementioned is explained as follows by KPMG (2012, p. 8):

“Being a director of a company can be rewarding, worthwhile and fulfilling. At the same time it is a demanding and challenging task, even in the best of circumstances. In accepting the position, a director automatically assumes onerous duties, responsibilities and personal liability under both common law and statutory law.”

Mervyn King (2006, p. 18) also adds to the above statement in his definition of corporate governance where he mentions that:

“A more informed definition would be processes to help directors discharge and be seen to be discharging their responsibilities created by their duties. This definition applies equally to all entities which are governed.”

He (2006, p. 36) goes further by indicating the risks that individuals take upon themselves when assuming the position of director, by stating the following:

“Every director must be aware that his personal estate is on the line arising out of his appointment and following his conduct as a director, whether by way of commission or omission.”

Constas and Bleijs (2009, pp. 34-35) brings the above statements into perspective for bodies corporate. They recognise the fact that trustees and other officers of bodies corporate are indemnified by the Sectional Titles Act against all claims, losses, costs and expenses which they may incur or become liable to because of their actions, except in cases of dishonesty or gross negligence. Despite this indemnity, they specifically emphasize that:

“We perceive the fiduciary duty in a body corporate situation as possibly being even more important than that of a company. A person’s investment in his home

is one of the biggest and most important transactions that he is likely to enter into in his entire life, and this must be borne in mind by trustees at all times!"

It is, however, not possible for small entities to follow King III to the letter. Examples of practices that may be difficult or impossible for a small entity to follow and include, is amongst others, the appointment of an audit committee, the establishment of an internal audit function and the appointment of independent, non-executive directors. However, while smaller entities may find it more difficult to implement some of the practices of good corporate governance, it is in their own best interest to address and implement these practices as far as possible (KPMG, 2012, p. 8). Le Roux (2010, p. 1) explains that each entity should consider the approach that best suits its size as well as complexity. The manner of application will differ for each entity, but all entities should strive to continually improve their governance practices (Institute of Directors in Southern Africa, 2009, p. 17). The philosophy of the King III Report revolves around three key aspects, namely leadership, sustainability and corporate citizenship. The first of these aspects, leadership, entails that leaders should be ethically responsible, accountable, transparent, fair in their actions, and direct an entity in a sustainable manner (Institute of Directors in Southern Africa, 2009, p. 10).

The problem with many sectional title schemes is that bodies corporate are not being run like "businesses" (Constas & Bleijs, 2009, pp. 26, 98; Pincus, 2004, p. 18), and that members are reluctant to be appointed as trustees and become involved in the leadership and management of schemes (Constas & Bleijs, 2009, p. 34). Being a trustee is often seen as a "thankless job" which is usually done for little or no remuneration (Constas & Bleijs, 2009, p. 37; Ozynski, 2007, p. 18). (See also Paddock (2008, pp. 10-4).) In practice, trustees are regularly contacted after hours or over weekends by residents wanting to complain about various matters such as noisy neighbours. Furthermore, in some cases a whole complex is owned by a number of investors, who do not live in the complex, and do not want to get involved in the

“problems” of the residents. There are even cases where sectional title schemes are being run without a board of trustees. Many members and trustees are also not equipped with the necessary skills and knowledge to be able to manage the scheme in a sustainable manner and make informed decisions on important matters (Nel, 1999, pp. IV-VI; Constas & Bleijs, 2009, p. 26; Maree, 2011, p. 3). This results in many trustees acting without having the necessary skills and not being fully aware of their duties and obligations (Nthite, 2005, p. 16; Pienaar, 2010, p. 185). This is in sharp contrast with the responsibilities of the trustees in terms of the principle of responsible leadership (Maree, 2011, p. 3). Owners are also increasingly demanding that trustees better understand their duties and remain up to date with the amendments to the Act (Ed, 2006, p. 2). The trustees should take responsibility for ensuring that the body corporate remains a going concern and be willing to take corrective action to ensure that it thrives in a sustainable manner (KPMG, 2012, p. 48; Institute of Directors in Southern Africa, 2009, p. 20). As stewards of the body corporate, the trustees should also show the moral duty of competence, ensuring that they have the knowledge and skills necessary for governing a sectional title scheme effectively (Institute of Directors in Southern Africa, 2009, p. 22). (See also Rossouw & Van Vuuren (2010, p. 213) and Le Roux (2010, p. 92).)

Rising costs and non-payment of levies is a widespread problem among sectional title schemes (Van Noort, 2007, p. 10; Wilson, 2006, p. 22; Pincus, 2004, p. 18; Maree, 2010). (See also Muller (2009, p. 42), Maree (2009, pp. 19-20) and Nthite (2005, p. 16).) Various sectional title schemes around the country are faced with serious cash flow problems and many are operating under insolvent circumstances (Sectional Title South Africa, 2010; Bauer, 2012; Constas & Bleijs, 2009, p. 113). According to research done in 2010 by Santam, approximately 20% of individual sectional title units are behind on their levy payments at any given time (Maree, 2010). This poses a great risk for trustees, in the light of the fiduciary relationship between the trustees and the members of the body corporate. In this regard, the trustees should display leadership in terms of good corporate governance, and take responsibility for managing these risks.

The above-mentioned risk of cash flow problems are not the only risk trustees are faced with. The responsibilities involved with being a trustee are onerous and the Act is cumbersome. Many trustees have time constraints, and they are faced with difficult decisions for which they do not necessarily have sufficient time available to give it the proper attention required. For this reason there is an ever increasing risk involved in being a trustee. This inevitably leads to situations where trustees appoint managing agents to execute the administration and fulfil certain management functions on behalf of the trustees and body corporate of the sectional title scheme. In terms of the Sectional Titles Act, the members of the body corporate hand over an enormous responsibility to the trustees of a sectional title scheme (Constas & Bleijs, 2009, pp. 34, 42; Woudberg, 1999, p. 45; Pienaar, 2010, pp. 184-185). Managing agents are usually professional persons or firms with the necessary skills and knowledge to perform the management and administration of a scheme.

It is important to note that by appointing a managing agent, the trustees are not absolved of their duties, powers and responsibilities (Constas & Bleijs, 2009, pp. 42-47). In terms of the principles of good corporate governance, trustees can delegate certain functions to managing agents (Pienaar, 2010, p. 180), but cannot avoid their ultimate responsibilities, nor completely delegate them. The King Code states very clearly that the board *“should delegate certain functions to well-structured committees but without abdicating its own responsibilities”* (Institute of Directors in Southern Africa, 2009, p. 46). In terms of sectional titles, the trustees must answer to the members of the body corporate and are therefore under increasing pressure to become more transparent, accountable and responsible (KPMG, 2012, p. 8). It can also happen that some trustees act in a manner that is dishonest or grossly negligent (Constas & Bleijs, 2009, p. 35), resulting in more frequent instances of owners taking trustees to court for fraud or poor performance (Ed, 2006, p. 2).

Another important fact to note is that the body corporate of a sectional title scheme is entrusted with trust money in the form of levy contributions from all owners to establish a fund that is sufficient to pay for all expenses of the scheme (Constas & Bleijs, 2009, pp. 107-108). The fact that trust money is dealt with on a day-to-day basis further emphasises the importance of applying principles of good governance. In practice, many owners fend against increasing levies (Pienaar, 2010, p. 158). Especially in times of economic crisis and rising inflation, the levy income of bodies corporate may be put under a lot of pressure and this can increase cash flow problems in a sectional title scheme (Muller, 2009, p. 42). The trust money involved in sectional title schemes further emphasises the vital importance of the fiduciary responsibilities of the trustees and the managing agents involved (KPMG, 2012, p. 84; Pienaar, 2010, pp. 177-178). Mervyn King (2006, pp. 29-30) also sums this up by stating:

“The director has to be a good steward of the company’s assets. He should ensure that the company utilises its assets as if they were the assets of his own family, of which he is the head.”

As pointed out by PricewaterhouseCoopers (2010, p. 3) and Le Roux (2010, pp. 8-9), the principles of good governance applies to all smaller enterprises, despite a lack of formal “corporate” structures. Small enterprises, including the trustees and bodies corporate of sectional title schemes, do not operate independently from their stakeholders. The fundamentals of good corporate governance are as applicable to the trustees and members of the bodies corporate of sectional title schemes as it is to large corporate entities. These fundamentals include, amongst others, transparent stakeholder engagement, accountability, responsible leadership, sound ethical foundations, the governance of risk, compliance with laws and regulations, good stakeholder relations and sustainable organisational performance (KPMG, 2012, p. 9). (See also PricewaterhouseCoopers (2010, pp. 2-3) and Le Roux (2010, p. 69)). Further reference will be made, where applicable, to the relevant aspects of corporate governance throughout the rest of the study.

1.4. FINANCIAL REPORTING IN SOUTH AFRICA – BACKGROUND AND OVERVIEW

South African financial reporting has undergone considerable changes in recent years. The Accounting Practices Board (APB) was formed in 1973 to consider what should be generally accepted accounting practice, and issue South African Generally Accepted Accounting Practice (SA GAAP) (SAICA, 2012). All companies in South Africa, irrespective of their size or form had to prepare financial statement in accordance with SA GAAP (Stainbank, 2008, p. 1).

As a result of a variety of accounting regulatory frameworks for financial reporting in different parts of the world, financial statements can vary significantly across different accounting regimes. The use of varying standards worldwide may compromise comparability and even result in a loss of the credibility of financial statements (Oberholster, et al., 2011, p. 1). Comparable financial information is vitally important for effective competition among the capital markets of the world. Wahlen, Baginski and Brashaw (2008, p. iv) are of the opinion that international expectations for financial statements of high quality are increasing, especially seen in the light of recent financial crises in worldwide capital markets. The pressure among international role players to harmonise accounting standards has lead to the development of International Financial Reporting Standards (IFRS) by the International Accounting Standards Board (IASB), and during 2003, the APB decided to harmonise SA GAAP with IFRS. IFRSs set out the requirements for recognition, measurement, presentation and disclosure for general purpose financial statements and other reporting of all profit-oriented entities (International Accounting Standards Board, 2009).

IFRSs are directed to the general financial information needs of a very wide range of users, for example, creditors, shareholders, employees and the public at large and are mainly aimed at the reporting needs of large entities. The cumbersome recognition,

measurement and disclosure requirements of “full” IFRS place an enormous burden on small and medium-sized entities (SMEs). Van Wyk and Rossouw (2009, pp. 99-101) mention that applying full IFRS do not result in useful and cost-effective information being provided to the users of the financial statements of SMEs, irrespective of their legal form. They argue that these users do not need all the detailed and complex information provided by general purpose financial statements. (See also Steinbank (2008, pp. 1-3), Riddin (2009, pp. 1-2) and Riddin (2010, p. 1).) The IASB recognised the need for a separate standard applicable to the needs of SMEs that often produce financial statements only for the use of owner-managers or tax authorities, and do not necessarily constitute general purpose financial statements. Consequently, the IASB developed and published International Financial Reporting Standards for Small and Medium-sized Entities (IFRS for SMEs). In 2007, South Africa adopted IFRS for SMEs while still in its exposure draft form, making it the first country in the world to do so (Van Wyk & Rossouw, 2009, p. 100; Steinbank, 2008, p. 2).

The new South African Companies Act, 2008, has brought about changes to the standard-setting process and a subsequent re-evaluation of the continued existence of SA GAAP. A decision was made by the APB that SA GAAP will be withdrawn and cease to apply in respect of financial years commencing on or after 1 December 2012. As a result of these decisions, all companies still applying SA GAAP will have to convert to IFRS or IFRS for SMEs. However, the withdrawal of SA GAAP is not only applicable to companies, but also to entities other than companies. In their announcement, the APB and Financial Reporting Standards Council (FRSC) also indicated that other entities that are required to apply SA GAAP in terms of their governing legislation should follow the process of conversion to either full IFRS or IFRS for SMEs (SAICA, 2012).

This announcement is of particular importance to the governing legislation of the sectional title industry in South Africa. Management rule 35 in Annexure 8 of the Sectional Titles Act, 95 of 1986 states the following:

“The trustees shall cause to be prepared, and shall lay before every annual general meeting, for consideration in terms of rule 56 (b), a financial statement in conformity with generally accepted accounting practice, which statement shall fairly present the state of affairs of the body corporate and its finances and transactions as at the end of the financial year concerned.”

Therefore the term “generally accepted accounting practice” used in the Sectional Titles Act may in future possibly need to be interpreted as either full IFRS or IFRS for SMEs. This inevitably raises a question regarding the applicability of these standards to the sectional titles industry.

Full IFRS is intended for use by large entities and IFRS for SMEs is intended for use by small and medium-sized entities. The IASB (2009, p. 10) defines small and medium-sized entities as entities that do not have public accountability and do not publish general purpose financial statements for external uses. Examples of external users include credit rating agencies, business owners not involved in managing the business and potential creditors. An entity has public accountability if its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market, or if it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. Paddock (2008, pp. 1-4) explains that a body corporate controls, manages and administers a sectional title scheme. It does not trade or issue any debt or equity instruments in a public market. Bodies corporate do, however, hold assets in a fiduciary capacity as one of its primary businesses, but only do so for reasons incidental to a primary business. The IASB clearly states that this incidental fiduciary capacity does not make an entity publically accountable, as is the case for travel agents, schools or real estate agents. It is, therefore, clear that in terms of the descriptions provided by the IASB, the body

corporate of a sectional title scheme is regarded as a small or medium-sized entity, and that it can use IFRS for SMEs for reporting purposes instead of full IFRS.

In research published by Van Wyk and Rossouw (2009, p. 113) they argue that IFRS for SMEs follow a “one-size-fits-all” principle and does not distinguish between micro, small and medium-sized entities. Their research also revealed that despite the good intentions of the IFRS for SMEs, there is scepticism among accounting practitioners about whether the standard actually reduces the burden of financial reporting for SMEs. One of the problems in the sectional title industry is the fact that many users of financial statements of bodies corporate do not have an in-depth knowledge of accounting and finance. This makes even a seemingly “simplified” framework such as IFRS for SMEs too complicated and cumbersome for the industry in general. Chapter 4 of this study provides an elaboration of the applicability of IFRS for SMEs for bodies corporate.

1.5. PROBLEM STATEMENT AND AIM OF THE STUDY

From the above it follows that sectional title property plays an important role in addressing the housing problem in South Africa. There are various risks involved in being a trustee of a body corporate, and the risks are being aggravated by owner apathy with regard to scheme management. Furthermore, managing agents face numerous practical problems in the day-to-day management of sectional title schemes. Accounting and auditing practitioners also encounter various practical challenges when performing accounting and assurance services for sectional title clients. Very few members of bodies corporate have knowledge of IFRS, and this raises the question as to whether IFRS is an appropriate and cost-effective framework to use. This study deals with these issues by way of a literature review and empirical study, which will be further alluded to in 1.6. below.

Against the above-mentioned background, the primary aim of the study is as follows:

- To give an overview of practical problems experienced from an accounting and auditing perspective regarding:
 - Risks associated with sectional title;
 - Auditing-specific problems relating to sectional title; and
 - Accounting-specific problems relating to sectional title.
- To attempt to find possible solutions for the above-mentioned problems and to make recommendations in this regard.
- To set benchmarks from the analysis of the annual financial statements of respondents over a three-year period. These benchmarks can be of assistance as an industry standard for owners, trustees, managing agents, auditors and accountants rendering a professional service.

1.6. RESEARCH METHODOLOGY

The purpose of this section is to provide an understanding of the research methodology applied in the study. The research design was developed to address the research problem stated above.

1.6.1. RESEARCH OVERVIEW

Clough and Nutbrown (2002, p. 5) state that research is *“the investigation of an idea, subject or topic for a purpose. It enables the researcher to extend knowledge or explore theory.”* According to Henning, Van Rensburg and Smit (2004, p. 31) researchers choose methods and a research genre that will optimally address the research problem. Henning, Gravett and Van Rensburg (2005, p. xvi) describe research as *“finding a way to a better understanding and explanation through the text of others (literature study) and a small field of inquiry (empirical study).”* (See also Mouton (2011, p. 179).) This

latter approach was also followed in this study, that is, doing a literature study followed by an empirical study in which certain aspects of the literature study were tested.

1.6.2. LITERATURE STUDY

A comprehensive literature study often emphasizes the importance of the research problem as the foundation on which to build an empirical study. Mouton (2011, p. 86) is of the opinion that every research project should start with a review of existing literature available. Pellissier (2007, p. 55) states that the literature study entails a deep review of the traditional field to which the research belongs, presenting the current state of major ideas in the field right up to, but not including, the researcher's own study. Fink (2005, p. 3) has a similar point of view, stating that a research literature review *"is a systematic, explicit, and reproducible method for identifying, evaluating, and synthesizing the existing body of completed and recorded work produced by researchers, scholars and practitioners."* According to Henning, Van Rensburg and Smit (2004, p. 27) the main purpose of a literature review is to put the study into context, to synthesise the available literature and to engage critically with the literature. This is further supported by scholars such as Von Wielligh (2005, pp. 51-53), Rossouw (2006, pp. 13-14) and Els (2007, pp. 8-9).

The literature study in this text commenced with detailed searches done by research specialists at the academic libraries at the Central University of Technology, Free State and the University of the Free State as well as the Archive for Contemporary Affairs at the University of the Free State. The searches identified various possible literature sources, including books, articles, theses, dissertations, internet sources and professional and institutional publications.

The results of the literature study of chapters 2 to 4 provides the basis for the aspects that were empirically tested in chapter 5, as discussed below.

1.6.3. EMPIRICAL STUDY

Flowing from the literature study, an investigation into current practices and challenges in the sectional title industry was undertaken.

According to Coldwell and Herbst (2003, pp. 9-13) there are three broad types of business research strategies, namely descriptive research, exploratory research and causal research. They describe the major purpose of descriptive research as *“to describe the characteristics of a population or phenomenon.”* Exploratory research, according to them, does not start with a specific problem, and the purpose thereof is to develop a hypothesis or a problem to be tested further. The aim of causal research aims at *“demonstrating that a change in one variable causes some predictable change in another variable.”* For purposes of this study, a descriptive research strategy was chosen.

Coldwell and Herbst (2003, pp. 13-16), Anderson and Poole (2009, p. 27) as well as Pellissier (2007, pp. 22-26) distinguish between two other research strategies, namely qualitative and quantitative research strategies. According to Anderson and Poole (2009, pp. 24-25) qualitative research *“stresses meanings in context, rather than numerically measured data.”* Coldwell and Herbst (2003, p. 13) define qualitative research as research for which *“the research findings are not subjected to a formal quantification or quantitative analysis.”* Pellissier (2007, pp. 20-22) adds that qualitative research attempts to *“go deeper, beyond historical facts”* and typically *“involves face-to-face interviewing, either with individuals or groups of respondents”*. Quantitative research, according to Pellissier (2007, p. 19), is appropriate for examining data from large samples of a target population, and the results thereof can be statistically analysed with great accuracy. Coldwell and Herbst (2003, p. 15) has a similar definition, stating that quantitative research *“generally involves the collection of primary data from large numbers of individual units”* and add that *“emphasis is placed on the*

collection of numerical data, the summary of those data and the drawing of inferences from the data”.

Anderson and Poole (2009, p. 27) argue that it is often advisable to combine qualitative and quantitative research strategies, in order to *“maximise the theoretical implications of research findings”*, and this approach can prove valuable in certain projects. Pellissier (2007, p. 22) is of the opinion that the two strategies should be viewed as mutually supportive, as both approaches have specific benefits for solving research problems. In this study, both a qualitative as well as a quantitative research strategy was followed.

1.6.4. QUALITATIVE RESEARCH

The concept of a standardised interview is discussed by Henning, Van Rensburg and Smit (2004, p. 53) as a mechanism that will provide information representing reality through the response of an interviewee, provided that the principles of neutrality and objectivity are strictly adhered to. In such a process *“the interviewer is a neutral facilitator who elicits the forthcoming information from the interviewee and the interviewee gives these responses with the help of questions and prompts in an atmosphere of trust and accountability”*. Clough and Nutbrown (2002, p. 103) adds that interviewing is *“one of the most common and powerful ways in which we try to understand our fellow human beings”*.

In terms of using a qualitative research strategy, a study was done by way of standardised interviews with role players in the sectional title industry limited to the Bloemfontein area in South Africa. For the purposes of this study, the interviewees were divided into three main groups of stakeholders. The first group being chairmen of bodies corporate of sectional title schemes, the second group managing agents of sectional title schemes, and the third group accounting and auditing professionals involved in the

sectional title industry. The reason for splitting interviewees into three groups is that the groups play different roles in the industry and have varying perspectives on practical issues, problems and challenges in the industry.

Henning, Van Rensburg and Smit (2004, p. 71) state the importance of selecting interviewees who can shed optimal light on the issue being investigated. They emphasise that “desirable participants” are an integral part of the purposive sampling procedure. (See also Pellissier (2007, pp. 24-25).) The above-mentioned three groups of stakeholders comply with this requirement.

The populations of the three groups of participants were difficult to determine, due to various factors. According to the Department of Rural Development and Land Reform there were 3383 sectional title schemes registered in Bloemfontein as on 5 April 2012 (see Annexure I). However, many sectional title schemes in Bloemfontein operate without a functioning body corporate and board of trustees. Furthermore, not all the organisations acting as sectional title managing agents are registered with the National Association of Managing Agents (NAMA) and the Estate Agency Affairs Board (EAAB). Many sectional title schemes operate without using the services of a managing agent, and not all sectional title schemes are using the services of professional accounting and auditing practitioners. There are also various auditing and accounting practitioners who is not involved/do not want to get involved in assurance services for sectional title schemes. The reasons why they prefer not to be involved differ from firm to firm. Some practitioners, for instance, do not want to get involved in this type of work due because they perceive the risk to be too high. Others claim that the audit and/or accounting fees attached to the work are so low that it does not make financial sense to accept sectional title clients. Especially some of the larger firms state that it is firm policy not to get involved in work on such a small scale.

Due to the above-mentioned reasons it was not practically possible to determine the exact populations of the bodies corporate and managing agents. The fact that various auditing and accounting practitioners are not involved in service delivery in the industry makes the mentioned practical challenge also applicable to these firms to a large extent. In order to address these practical problems, extensive consultation was undertaken by the candidate as well as the study leader among the three target groups, namely chairmen of bodies corporate of sectional title schemes, managing agents of sectional title schemes, and accounting and auditing practitioners involved in the sectional title industry. After the consultation process, a joint decision was made to include five respondents from each of the three groups. It was also jointly decided which five respondents were to be chosen from each group. Factors such as knowledge of and experience in the industry as well as the number of clients of the managing agents, accounting and auditing practitioners played a role in the choice of the five respondents that were eventually chosen. In view of clarity, the decision making process for the three groups will be briefly discussed.

The five chairmen of trustees of bodies corporate interviewed were selected after extensive enquiry from role players in the sectional title industry in Bloemfontein. The sample was selected to represent one large sectional title scheme (more than 50 units) in the form of a townhouse complex, one medium-sized scheme (between 10 and 50 units) in the form of a townhouse complex, one small sectional title scheme (less than 10 units) in the form of a townhouse complex, one scheme in the form of a large block of flats (more than 100 units) and one scheme in the form of a small block of flats (less than 20 units). This ensured that in terms of residential schemes, the two main forms of complexes (flats and townhouses) are represented and that inputs were received from chairmen over the entire size spectrum, from small to large schemes.

The five managing agents interviewed were selected after a thorough investigation into the main role players in the sectional title industry in Bloemfontein. The sample was

selected to represent two large managing agents (managing more than 100 schemes), two medium-sized agents (managing between 30 and 100 schemes) and one small agent (managing less than 30 schemes). Two of the five managing agents have been operating in Bloemfontein for more than 80 years, one for more than 20 years and the remaining two have been in operation for less than 10 years. The total number of sectional title schemes managed by these five managing agents amount to more than 450.

The five accounting and auditing professionals interviewed were selected after extensive enquiry from various managing agents and chairmen of trustees of bodies corporate in Bloemfontein. The sample was selected to represent two large accounting and auditing practitioners (having more than 100 schemes as clients), two medium-sized practitioners (having between 30 and 100 schemes as clients) and one small practitioner (having less than 30 schemes as clients). All of the accounting and auditing practitioners are established firms in Bloemfontein specialising in, amongst others, accounting and auditing of sectional title schemes. Four of the five practitioners interviewed are senior partners in their firms, and the remaining interviewee is a senior staff member in the auditing division responsible solely for sectional title work. The total number of sectional title clients for which these five practitioners do accounting and auditing work amount to more than 550.

In order to address the research problem of the study, three different research questionnaires were developed as a measurement instrument in order to structure the interviews, one for each main group of interviewees (see Annexure A, C and E). Some of the respondents are Afrikaans-speaking, and Afrikaans questionnaires were used in these instances (see Annexure B, D and F). The questionnaires were designed to structure the interview process, and ensure consistency of the coverage of questions between the three groups and individual interviewees. A formal cover letter from the supervisor (see Annexure G and H) explaining the purpose of the interviews and

addressing the terms of confidentiality was sent to all interviewees before the interviews.

Various aspects from available literature (including Clough and Nutbrown (2002, p. 122), Coldwell and Herbst (2003, pp. 54-57), Henning, Van Rensburg and Smit (2004, pp. 53-55) and Howard and Sharp (1983, pp. 124-133) and scholar Els (2007, pp. 222-228) were taken into account in developing the questionnaires and conducting the interviews. Especially the following aspects were taken into account:

- Explaining the purpose and format of the interview beforehand and asking the interviewees for permission to document the interview by way of taking notes;
- Ensuring that the contents of the questionnaires fit the research problem;
- Keeping all questions as neutral as possible;
- Ensuring that only one question is asked at a time;
- Paying attention to the clarity, language and formulation of questions, leaving no room for ambiguity;
- Ensuring that the order of the questions allow for a logical flow of thought;
- Including a variety of questions – closed as well as open-ended and using Likert scales where applicable; and
- Leaving enough room for comments and motivations of answers, and encouraging additional responses.

The results of the qualitative research study are discussed in detail in Chapter 5 of this study.

1.6.5. QUANTITATIVE RESEARCH

Flowing from the literature study, a quantitative research strategy was followed, by way of an analysis of the annual financial statements and audit reports thereto of bodies corporate over a period of three years.

When performing quantitative research, the results of the research depend largely on the sample data, and it is therefore important that samples are drawn in a scientific and well-managed manner (Howard & Sharp, 1983, p. 126). Pellissier (2007, pp. 32-34) as well as Coldwell and Herbst (2003, pp. 79-81) differentiate between probability sampling and non-probability sampling. The authors state that with probability sampling techniques, every element in the population stands the same chance of being selected. The elements are selected at random after stratifying the population according to some characteristic. This method of sampling ensures that there is no room for bias or favouritism. (See also Singh and Nath (2010, p. 165).) In terms of non-probability sampling, Coldwell and Herbst (2003, p. 79) state that the investigator uses his expertise or judgement in the selection of non-probability samples. They also state that this technique makes it impossible to assess sampling errors or to determine whether a sample is representative of the population or not (See also Singh and Nath (2010, p. 166) and Pellissier (2007, p. 32).)

As stated above, there were 3383 sectional title schemes registered in Bloemfontein according to the Department of Rural Development and Land Reform on 5 April 2012 (see Annexure I). Due to the difficulty of gathering a sample of annual financial statements and audit reports of bodies corporate stretching over an uninterrupted period of at least three years, a non-probability sampling technique was chosen, and the sample was selected by way of convenience sampling. Convenience sampling is described by Pellissier as a technique whereby *“items are selected for the convenience of the researcher because they are readily available, nearby or willing to participate”*

(2007, p. 32). Coldwell and Herbst (2003, p. 81) add that convenience samples are restricted, non-probability samples and that the more convenient elementary units are chosen from a population. (See also Singh and Nath (2010, p. 172).)

A sample of 60 annual financial statements including audit reports thereto was selected at random, covering a period of three years for bodies corporate in the Bloemfontein area in South Africa. These annual financial statements with the accompanying audit reports were obtained from one of the managing agents who participated in the qualitative study. This firm is known to be the largest managing agent in Bloemfontein. The sample of the annual financial statements selected covers a variety of bodies corporate and includes:

- Residential bodies corporate;
 - Small (fewer than 10 units) townhouse complexes;
 - Medium (between 10 and 50 units) townhouse complexes
 - Large (more than 50 units) townhouse complexes;
 - Small (fewer than 10 units) blocks of flats;
 - Medium (between 10 and 50 units) blocks of flats;
 - Large (more than 50 units) blocks of flats; and
- Combined bodies corporate (residential and commercial units in one scheme).

The financial statements with accompanying audit reports were obtained from a managing agent of bodies corporate for the financial years ending 2009 and 2010. Since the 2009 financial statements also have figures for the comparative financial year (2008), the data of three financial years were available for analysis. Furthermore, the sample was selected so as to include financial statements and audit reports drawn up and audited by various accounting and auditing practitioners.

Various forms of analysis were conducted on the selected annual financial statements and accompanying audit reports, the purpose of which is to identify, amongst others, trends, deficiencies in reporting and possible norms for the sectional title industry. These findings are discussed in detail in chapters 3 and 4 of the study.

1.7. CONTENTS OF THE STUDY

The content of the study consists of the following:

Chapter 1 – In this chapter, the background to the housing problem and the sectional title industry in South Africa was introduced briefly. The chapter then briefly discusses governance of sectional title as well as some background on financial reporting in South Africa. The chapter concluded with the problem statement, research methodology and the design of the study.

Chapter 2 – The second chapter deals with the legal aspects surrounding the sectional title industry in South Africa, with specific consideration given to legal aspects relating to accounting and auditing matters of sectional title schemes.

Chapter 3 – In the third chapter, the auditing and assurance aspects of sectional title schemes are examined. Findings based on an analysis of a sample of body corporate annual financial statements are also discussed in this chapter.

Chapter 4 – The fourth chapter deals with accounting and reporting of sectional title schemes. This chapter examines the legal requirements for financial reporting by bodies corporate and examines reporting frameworks currently available. The chapter attempts to address the question as to whether International Financial Reporting

Standards is not perhaps too cumbersome and expensive for the users of body corporate financial statements. The chapter also investigates the possibility of a sectional title-specific reporting framework. Findings based on an analysis of a sample of body corporate financial statements over a period of three years are also discussed in this chapter.

Chapter 5 – In the fifth chapter, an empirical study of the sectional title industry in South Africa will be undertaken. The study is based on interviews held with stakeholders in the sectional title industry. The chapter is divided into four parts. The first part deals with interviews held with chairmen of boards of trustees of bodies corporate. Part two deals with interviews held with managing agents of sectional title schemes, while part three deals with interviews held with accountants and auditors of sectional title schemes. The fourth part of this chapter summarises the findings from the interviews held with the various stakeholders.

Chapter 6 – The sixth chapter indicates the conclusions of the study and presents possibilities for future research.

1.8. CONCLUSION

This chapter commenced with an introductory overview of the challenges faced by South Africa to provide for the housing needs of the country. Sectional title property plays an important role - especially in providing housing to lower-income households and there are clear indicators that it will continue to play an increasingly important role in future. It is, however, clear that there are various challenges facing the sectional title industry, especially from a governance and management perspective, and accounting and auditing practitioners involved in the industry are confronted with various practical issues. In the next chapter legal aspects surrounding the sectional title industry in

South Africa will be discussed and specific consideration will be given to legal aspects relating to accounting and auditing matters of sectional title schemes.

CHAPTER 2 – LEGAL ASPECTS RELATING TO ACCOUNTING AND AUDITING MATTERS OF SECTIONAL TITLE SCHEMES

“And do as adversaries do in law, strive mightily, but eat and drink as friends.” - William Shakespeare - The Taming of the Shrew

“I have gained this by philosophy: that I do without being commanded what others do only from fear of the law.” - Aristotle

2.1. INTRODUCTION

In the first chapter a brief overview was given of, amongst others, the legal aspects governing sectional title and related matters in South Africa. This chapter deals briefly with the legal aspects surrounding the sectional title industry in South Africa, primarily from an accounting, financial, auditing and management perspective. The purpose of the chapter is not to engage in a legal study, and consideration will only be given to legal aspects relating to management, financial, accounting, and auditing matters of sectional title schemes. The chapter will be structured according to the functions and responsibilities of the various role players in sectional title schemes, being the body corporate, the trustees and managing agents. In this chapter, additional aspects covered by the prescribed management rules will also be discussed.

All regulations, sections and rules mentioned in this chapter refer to regulations, sections and rules as per the Sectional Titles Act, 1986 (Act No. 95 of 1986) (as amended) including its Annexures. Throughout the study, consideration has also been given, as indicated, to new as well as concept legislation. An example is the Sectional

Title Schemes Management (STSM) Act 8 of 2011, which was gazetted and signed by the President in June 2011, as discussed in section 1.2 of Chapter 1.

The above-mentioned aspects aim to set a theoretical legal framework for the study. Furthermore, it will set a legal framework against which the empirical findings in Chapters 3 to 5 will, amongst others, be evaluated. It will also be of assistance in ascertaining whether the sectional title industry complies with the regulations as stipulated in the Act.

It should be noted that the Sectional Titles Act refers solely to the masculine form. The usage of the masculine form throughout this study is for purposes of convenience and consistency, and should be interpreted to refer to men and women alike.

2.2. THE BODY CORPORATE

Section 36 states that as soon as any person other than a developer becomes the registered owner of a unit in the scheme, the body corporate is formed. The body corporate is made up of all the individual owners of the sectional title scheme. This means that each and every owner is automatically a member of the body corporate. It is important to note that the provisions of the Companies Act, No 61 of 1973 and the Close Corporations Act, 69 of 1984 do not apply to the body corporate of a sectional title scheme. The body corporate is a separate legal entity, thus it is capable of suing and being sued in its corporate name. The body corporate also has perpetual succession, and continues to exist despite the fact that buying and selling of units and changes in ownership take place in the scheme.

2.2.1. RESPONSIBILITIES, POWERS AND FUNCTIONS OF THE BODY CORPORATE

All the functions of the body corporate as prescribed by the Act are mandatory, being indicated by the wording “*the body corporate shall...*”. (See also Pienaar (2010, p. 150).) An important responsibility of the body corporate is to ensure that all the rules as referred to in section 35 of the Act is enforced.

2.2.1.1. MAINTENANCE OF COMMON PROPERTY

Section 36 states that the main function of the body corporate is the control, administration and management of the common property of the scheme. This must be done in order to benefit all the owners of units in the scheme. Section 37 states that the body corporate should ensure that sufficient funds are available for repair and upkeep of the common property as well as for the payment of administrative and operating expenses and other services. Reasonable provision should also be made for future repairs and maintenance in the form of a reserve fund.

2.2.1.2. LEVY CONTRIBUTIONS

According to section 37, the body corporate must from time to time determine amounts to be collected in order to fulfil the above-mentioned duty. These contributions must be levied on the owners in proportion to the quotas of their individual sections and the body corporate must ensure that monies are collected. The body corporate should open a bank account with a registered bank or financial institution.

2.2.1.3. INSURANCE

Another responsibility of the body corporate, according to section 37, is to ensure that the building(s) and all improvements to the common property are insured against fire and possible other risks to the replacement value thereof. This specific function is often exercised by the trustees on behalf of the body corporate in terms of section 39. Many managing agents also assist with aspects such as obtaining quotations from insurers, making recommendations regarding insurers where they should be contracted as well as paying over insurance premiums of sectional title schemes to insurers.

2.2.1.4. POWERS OF THE BODY CORPORATE

One of the powers of the body corporate, in terms of section 38, is to appoint agents and employees as it may deem fit. The trustees will exercise this power on behalf of the body corporate. The body corporate can also borrow money to perform its functions, and invest surplus funds.

2.2.2. THE FIRST MEETING OF OWNERS

As mentioned above, the body corporate is made up of all the individuals who own units in the sectional title scheme. Therefore, the owners are in effect the will and mind of the body corporate. Many of the functions of the body corporate can be exercised by the members only in a formal meeting. Section 36 states that the first of such meetings of the owners should be held within sixty days of the establishment of the body corporate, with at least seven days written notice with a prescribed agenda attached.

In terms of section 36, the first meeting has to be convened by the developer and he must provide the members of the body corporate with various documents, including proof of revenue and expenditure regarding the management of the scheme up to the establishment of the body corporate, as well as a certificate from the local authority indicating that all rates have been paid by the developer. Section 36 also states that any balance of the revenue has to be paid over to the body corporate.

According to management rule 40, an auditor has to be appointed at this meeting, and in the case where the scheme consists of less than ten units, an accounting officer can be appointed. The auditor or accounting officer will then hold office until the next general meeting.

2.2.3. THE ANNUAL GENERAL MEETING

Management rule 51 states that the annual general meeting (AGM) must be held within four months after the end of each financial year. According to management rule 39, written notice of at least fourteen days must be given to all the owners. This notice has to be accompanied by copies of all the schedules, statements, estimates and reports to be discussed at the meeting. If the passing of a special or unanimous resolution is envisaged, a notice of at least thirty days must be given.

According to management rule 57, no resolutions may be passed or business be transacted without a quorum being present. For purposes of a general meeting, a quorum is determined as follows:

- for schemes of ten or fewer units, the number of owners holding at least fifty per cent of the votes, present in person or by proxy;

- for schemes consisting of fewer than fifty but more than ten units, the number of owners holding at least thirty-five per cent of the votes, present in person or by proxy; and
- for schemes with fifty or more units, the number of owners holding at least twenty per cent of the votes, present in person or by proxy.

Management rule 58 states that if a quorum is not present within half an hour of the proposed starting time of the meeting, the meeting must be adjourned to the same day the next week, at the same place and time. If at this adjourned meeting a quorum is not present within half an hour of the proposed starting time, the owners present in person or by proxy shall then form a quorum.

Quite often in practice, annual general meetings are adjourned due to a quorum not being present. This was one of the main frustrations identified by managing agents as well as trustee chairpersons. This issue will be discussed in detail in Chapter 5.

The resolutions of the members at a general meeting can be achieved either by show of hands or by poll, based on participation quota. The Act defines three kinds of resolutions, namely an ordinary resolution, a special resolution and a unanimous resolution. For an ordinary resolution to be passed, a majority vote of fifty-one per cent is needed, and there must be a quorum present at such a meeting. There are two ways of passing a special resolution. The first way is if seventy-five per cent of all members agree in writing and the second way is if seventy-five per cent of the quorum at a general meeting agrees. Unanimous resolutions are passed if all owners agree in writing, or if there is an eighty per cent quorum at a general meeting and all members present agree.

No owner can be prohibited from voting, except in the case of a majority vote being required. In such a case an owner who is in arrears with his levy payments or has received a warning for persistently contravening the conduct rules will be prohibited from voting.

Votes may be cast either personally or by proxy. Proxies should only be appointed for a specific general meeting, and cannot be used for just any meeting over a period of years.

2.2.3.1. FINANCIAL STATEMENTS

According to management rule 37, ordinary business for the purposes of the annual general meeting includes the consideration of the financial statements of the preceding year. The preparation of the financial statements is one of the responsibilities of the trustees and will be discussed in further detail below under the section dealing with trustee responsibilities.

2.2.3.2. THE CHAIRMAN AND TRUSTEES' REPORT

The chairman of the trustees should act as chairman at every general meeting, unless the members of the body corporate decide otherwise. Management rule 38 stipulates that the trustees should also prepare a report on the affairs of the body corporate in the past year for every annual general meeting, and this report must be signed by the chairman. The Act is not very clear on what exactly should be contained in the Trustees' Report, and in practice the wording is interpreted in many different ways. Chapter 4 will deal with this matter in further detail.

2.2.3.3. REPLACEMENT VALUES FOR INSURANCE PURPOSES

As mentioned above, the trustees should ensure that all buildings and improvements to the common property are insured at the full replacement value thereof. Management rule 29 states that before every annual general meeting, the trustees should prepare schedules reflecting their estimate of these replacement values and such schedules should serve before the annual general meeting for consideration and approval.

2.2.3.4. APPROVAL OF THE BUDGET

According to management rule 36, the trustees must prepare a budget for the next financial year before every annual general meeting. The body corporate must then approve the budget by way of a majority vote at the annual general meeting.

2.2.3.5. APPOINTMENT OF AUDITOR OR ACCOUNTING OFFICER

As stipulated above in the section dealing with the first general meeting of the owners, management rule 40 states that an auditor has to be appointed at every annual general meeting. In the case where the scheme consists of fewer than ten units, an accounting officer can be appointed. The auditor or accounting officer will then hold office from the conclusion of that meeting until the next annual general meeting.

Management rule 40 also stipulates that *“the auditor or accounting officer, as the case may be, must sign the financial statements”*. The wording of this section of management rule 40 does not seem to be very clear. The possible interpretation of this rule and the responsibilities of the auditors and accounting officers will be further investigated and discussed in detail in Chapter 3 and 4 of this study.

2.2.3.6. APPOINTMENT OF TRUSTEES

Management rule 4 states that from the day on which the body corporate is established (see 2.2. above) until the first general meeting of the owners, all owners are deemed to be trustees. These trustees will hold office in this capacity until new trustees are elected at that meeting, and during this interim period, the developer will act as chairman of the trustees.

Per management rule 6, at the first general meeting and at every subsequent annual general meeting, trustees must be nominated and elected by the members of the body corporate. They shall then hold office until the next general meeting, and will be eligible for re-election.

2.2.4. SPECIAL GENERAL MEETINGS

All other meetings not mentioned above are called special general meetings, according to management rule 52. Special general meetings may be called by the trustees at any time they deem fit, or when requested by owners representing at least twenty-five per cent of the total participation quota. Written notice of at least fourteen days must be given to all the owners.

2.3. TRUSTEES

The trustees are the executive and management organ of the body corporate. Management rule 5 states that it is not required that trustees are owners of sections in the scheme; however, the majority of the trustees elected must be owners or spouses of owners. The managing agent may only be a trustee if he is an owner.

The number of trustees are determined by the members of the body corporate in a general meeting, as stipulated in management rule 4, keeping in mind that there must be a minimum of two trustees. In the empirical study undertaken and discussed in Chapter 5, it was clear that in practice it is difficult to determine an optimal number of trustees. Refer to Chapter 5 for further detail on the respondents' comments.

Sections 37 and 38 of the Act determine the performance of duties and exercising of powers that is expected from the body corporate and which is also the first level of responsibility for the trustees.

2.3.1. ELECTION AND REMOVAL

The appointment of trustees has been discussed in 2.2.3.6 above. A trustee is removed from office according to the stipulations of management rule 13 in the following circumstances: if he resigns, if he is convicted of a crime involving dishonesty, if his estate is sequestrated, if he becomes unsound of mind, by resolution of a general meeting of the body corporate to remove him from office, and if he becomes disqualified to act as a director of a company in terms of the Companies Act.

2.3.2. REMUNERATION

Management rule 10 determines the remuneration of trustees. Trustees who are owners are not entitled to any remuneration, except in the case of a special resolution being passed. In the empirical study that was undertaken as part of this study, many trustees and managing agents were of the opinion that this management rule is unfair, and should be changed so that all trustees can be remunerated without the passing of a special resolution. Chapter 5 deals with this matter in further detail.

The body corporate must, however, reimburse trustees for all expenses that were incurred by them in their capacity as trustees. In practice, trustees do not always keep evidence of expenses incurred, which sometimes creates problems with reimbursements. This issue will be discussed further in Chapter 4.

If a trustee is not an owner, he may be remunerated at an amount determined between him and the body corporate. Additionally, he will still be entitled to reimbursements for actual expenses as mentioned above.

2.3.3. MEETINGS OF TRUSTEES

Management rule 15 gives trustees the authority to convene their meetings as they deem fit, and to carry out their necessary duties by way of resolutions passed at these meetings. Any trustee can convene a meeting at any time, provided that seven days' written notice is given to the trustees. At a trustee meeting a quorum is formed by fifty per cent of the number of the trustees, but not fewer than two members. If a quorum is not present within thirty minutes of the proposed starting time, the trustees meeting will be adjourned to the same time on the next business day, and those then present will form a quorum. Owners may attend trustee meetings, but they are not allowed to vote at trustee meetings.

According to management rule 18, the chairman of the trustees will be elected at the first meeting of trustees after an annual general meeting. He will hold office until the end of the next annual general meeting. He has the casting and deliberative vote in all cases where there are more than two trustees.

From the empirical study undertaken, it seems as though, in practice, many boards of trustees hardly ever hold meetings, if at all. This issue will be investigated in further detail in Chapter 5.

2.3.4. FUNCTIONS, POWERS AND DUTIES OF TRUSTEES

Section 40 of the Act explains the fiduciary position of the trustees. Trustees must always act in the best interest of the body corporate, with honesty and in good faith and avoid any material conflict of interest between him and the body corporate. If he has any material interest in any contract of the body corporate, he must notify the other trustees of the nature and extent thereof. If a trustee acts in a manner that is grossly negligent he will be held liable to the body corporate for any loss suffered as a result thereof.

2.3.4.1. APPOINTMENT OF AGENTS

In many cases the trustees lack the time, skill and expertise to fulfil all the functions and duties they are responsible for. Therefore, management rules 26 and 46 state that the trustees may appoint a managing agent to be entrusted with various management and administrative duties of the body corporate. Managing agents are appointed for a period of one year, renewable from year to year. It is important to note that the trustees still remain ultimately responsible for their duties and functions in terms of the Act.

2.3.4.2. FINANCIAL RECORDS AND BOOKS OF ACCOUNT

Contributions collected from the owners do not belong to the trustees or the managing agent, and should always be treated as “trust money” (also refer to section 1.3. in

Chapter 1). Management rules 35 to 45 addresses this extremely important concept by dealing with the responsibilities of trustees regarding all matters relating to financial records. All financial records should be retained for a minimum period of 6 years and all minute books for as long as the scheme remains registered.

According to management rule 35, it is the responsibility of the trustees to ensure that proper accounting records are kept. These records must fairly explain the transactions and financial position of the body corporate. Among the records that must be kept are:

- records of the body corporate's assets and liabilities;
- records of the detail of all amounts received and expended by the body corporate;
- the addresses of all owners and registered mortgagees of units; and
- an individual ledger account for every owner.

The trustees must make all of the above-mentioned records available for inspection to the owner, registered mortgagee or managing agent if requested to do so.

Management rule 35 is not very specific regarding the exact details required in the accounting records, and not all of the wording used in the Act is acknowledged accounting terminology, therefore it is open to interpretation. This matter will be dealt with in detail in Chapter 4.

2.3.4.3. THE BUDGET

The annual financial estimate or budget, as it is widely known, has to be prepared by the trustees before every annual general meeting. Management rule 36 states that the

budget should be in the form of an itemized estimate of the income and expenditure that the body corporate foresees for the next financial year. It must also contain a provision for maintenance and possible contingencies.

2.3.4.4. ANNUAL FINANCIAL STATEMENTS

Management rule 37 stipulates that another duty of the trustees is to ensure that financial statements are prepared according to “*generally accepted accounting practice*”, which has to be a fair representation of the affairs of the body corporate and its finances and transactions for every financial year. The financial statements must include an age analysis of levies, special levies and contributions, an age analysis of accounts payable and the expiry date of all insurance policies.

Once again, the management rule contains wording that is not in accordance with accepted accounting terminology. There are also parts that are unclear and contradictory. This matter will be addressed in detail in Chapters 3 and 4.

2.3.4.5. LEVY COLLECTION

Management rule 30 bestows the duty upon the trustees to levy and collect contributions from the owners, as determined by the budget. The trustees should let each and every owner know in writing within 14 days after each annual general meeting, regarding the amount payable by him. Amounts payable by owners in terms of the budget is usually paid in equal monthly instalments over the course of a financial year.

From time to time the trustees may find it necessary to levy special contributions, for circumstances which were not considered in the annual budget. These special levies may also be payable in instalments or as the trustees deem fit.

2.3.4.6. BANK ACCOUNTS

According to management rules 41 to 44 the trustees must ensure that a bank account is opened in the name of the body corporate at a bank or financial institution. All money received must be deposited in this bank account. The money in the bank account may only be used for expenses of the body corporate or for investment of surplus funds.

The trustees may instruct the managing agent to open and operate this account. Management rule 42 stipulates that if the managing agent is an estate agent, the trustees may instruct the managing agent to deposit money in a trust account as stipulated by section 32(3) of the Estate Agents Act of 1976. If the managing agent handles the bank account on behalf of the body corporate, the money received may only be used for expenses of the body corporate or for investment of surplus funds.

Regarding the investment of surplus funds, management rule 43 states that such funds not immediately needed for expenses or other disbursements may be invested in a savings account or similar type of account with any registered bank or building society. The latter institutions have long since ceased existing in South Africa, and have been fully incorporated into the banking institutions as it is known today. The management rule further stipulates that the chosen financial institution must be approved by the trustees. If the body corporate earns interest, it may be used for any lawful purpose as seems fit.

As per the findings of the empirical study in Chapter 5, the interpretation of management rules 41 to 44 seems to create various practical challenges for managing agents as well as trustees, auditors and accounting practitioners. This issue will be dealt with in detail in Chapter 5 of the study.

2.4. MANAGING AGENTS

As mentioned in 2.3.4.1 above, the trustees may appoint a managing agent to be entrusted with various management and administrative duties of the body corporate. It is important to note that the appointment of a managing agent does not absolve the trustees from their functions, duties and powers in terms of the Act.

The Act does not specify that the managing agent must have any qualifications, but due to the nature of the functions and duties to be performed a sound knowledge of the Act and rules seem to be imperative. In practice, the role of managing agent is usually performed by an estate agent or firm of estate agents (Pienaar, 2010, p. 189).

2.4.1. APPOINTMENT AND TERMINATION

Management rule 46 stipulates that managing agents are appointed for a period of one year, renewable automatically from year to year, unless the managing agent is notified otherwise by the body corporate. The trustees may give notice of termination in the case of such a resolution having been passed at a trustee meeting.

2.4.2. ETHICS AND CODES OF CONDUCT

The Estate Agency Affairs Board (EAAB) is the official regulating authority for the estate agency profession in South Africa, and every estate agent must, by law, be registered with it. The Institute of Estate Agents of South Africa (IEASA) is a voluntary membership organisation for estate agents only. Managing agents can also voluntarily become a member of the National Association of Managing Agents (NAMA).

The EAAB has a Code of Conduct in place and the IEASA has separate ethical standards in place, called the Code of Ethical Obligations in addition to the industry Code of Conduct. Therefore, if an estate agent (or firm of estate agents) acts as managing agent he has to comply, by law, with the Code of Conduct of the EAAB. If he is a member of the IEASA, he has to comply, in addition, with their Code of Ethical Obligations. Furthermore, NAMA also has a Code of Conduct in place for their members.

As was already mentioned in 2.4 above, managing agents do not have to be registered estate agents. This raises the question as to whether trustees should perhaps consider if the managing agent has a code of conduct or code of ethics in place, before appointment of a managing agent. Nothing prohibits a managing agent from drafting and implementing its own code of ethics.

Even though the above-mentioned aspects do not form an integral part of this study, the principles of good corporate governance are of utmost importance. This fact was highlighted in section 1.3 of Chapter 1 as well.

2.4.3. FUNCTIONS AND POWERS

According to management rule 46, the functions, powers and duties of the managing agent have to be agreed upon in the terms of the contract between the parties. It may range from limited functions to extensive management and may include duties such as levy collection, creditor payments, common property management, general repairs and maintenance, completion of tax returns, bookkeeping functions, attending of meetings, and rule enforcement. The functions and powers of managing agents will be further investigated in Chapters 3 and 4 of the study.

2.5. CONCLUSION

In this chapter, an overview was given of the legal aspects and related matters that govern the sectional title industry in South Africa, as far as it is applicable to the aims of this study. Consideration was therefore only given to those legal aspects that deal with the accounting, auditing, finances and management of sectional title schemes.

As mentioned, the matters addressed in this chapter will set a theoretical legal framework with which bodies corporate, managing agents and other role players in the sectional title industry have to comply. Furthermore, it sets the framework against which the empirical findings in Chapters 3 to 5 can be measured.

In this chapter several shortcomings, weaknesses and unclear aspects in the legislation were identified (see for example points 2.2.3.5., 2.3.4.4. and 2.3.4.6.), that will be discussed in more detail in the ensuing chapters.

In the next chapter, auditing and assurance aspects relating to sectional title schemes will be dealt with. The chapter will also include an investigation of findings based on an analysis of a sample of body corporate annual financial statements.

CHAPTER 3 – AUDITING AND ASSURANCE ASPECTS RELATING TO SECTIONAL TITLE SCHEMES: AN OVERVIEW

“Plato is dear to me, but dearer still is truth” - Aristotle

3.1. INTRODUCTION

Chapter 2 gave an overview of the legal matters relating to the sectional title industry in South Africa as far as it concerns accounting, auditing, finances and the management of sectional title schemes. In this chapter, the auditing- and assurance-related aspects concerning sectional title schemes will be dealt with in greater detail. As already mentioned in Chapter 1, there are various aspects regarding auditing and assurance in the Sectional Titles Act which are unclear, or has some form of ambiguity, weakness or shortcoming. In this chapter, these aspects will be further alluded to against the background of the study, as set out in Chapter 1. The chapter will start with a brief history and background of auditing. Definitions of aspects relating to assurance engagements will be evaluated. Furthermore, an analysis will also be made of assurance-related aspects of a sample of audit reports of body corporate annual financial statements.

The 60 financial statements with accompanying audit reports were obtained from a managing agent of bodies corporate for the financial years ending 2009 and 2010. Since the 2009 financial statements also have financial figures for the comparative financial year (2008), the financial data of three financial years are available for analysis. However, the audit reports are only available for the 2009 and 2010 financial years.

3.2. THE HISTORY AND BACKGROUND OF AUDITING: A BRIEF OVERVIEW

The concept of auditing has been around for thousands of years, and can be traced as far back as 5000 B.C. (Dickinson, 1978, p. 1). There is evidence available of audits being performed in the ancient civilisations of Greece, China, Egypt, England and Scotland (Lee & Ali, 2008, p. 2; Brown, 1905, p. 21 & 74; Langhout, 1961, p. 1; Ricchuite, 1982, p. 15). Records of financial transactions of an ancient Mesopotamian civilisation dating back to 3 500 B.C. indicate dots, checks and tick marks as a system of verification. Similar systems were in use during the Zhao Dynasty in China (Ramamoorti, 2003). In ancient Greece, checking clerks were used to check the accounts of public officials at the end of their terms in office, and the ancient Egyptians used a system whereby two separate officials recorded government receipts on separate scrolls, which was later compared and checked for correctness (Chatfield, 1974, p. 111; Brown, 1905, p. 22 & 74). The main purpose of these audits was to ensure the proper recording of government revenue and expenses (Gordon, 1992, pp. 18-19).

In later years, the industrial revolution brought about the concept of companies and outside shareholding. The owner of resources (also often referred to as the principal) appoints managers (agents) to take the responsibility of managing the resources on behalf of the principal (Watts & Zimmerman, 1986, pp. 180-186). This is also referred to as the agency theory. Since the agents are charged with certain responsibilities, they are held accountable to the principal regarding their activities and how resources are spent (Flint, 1988, pp. 12-14). This is also known as the accountability theory. This split between ownership and management of companies brought about the need for an outside party with an objective point of view to give an independent overview of the management of resources of companies on behalf of the owners (Gordon, 1992, p. 19). The cornerstone of modern auditing was an independent, reliable process to verify that funds were used in an efficient manner, and that financial records reflect the actual

financial performance and position of an organisation (Mautz & Sharaf, 1961, pp. 158-161).

Auditing as subject field and the practical application thereof in practice developed for many decades without proper scientific foundations. The development of auditing came about largely against the background of practical needs of the users of annual financial statements as well as the responsibilities that the audit profession was willing to accept with regards to the expressing of an audit opinion. The monumental work by Mautz and Sharaf made probably the first and the greatest contribution in pointing out the aforementioned. The following is a brief excerpt of their viewpoint (1961, p. 40):

"Various efforts have been made to state the basic assumptions or postulates of accounting, although to this date there has been no general acceptance of any single such statement, but little effort has been made to list the basic assumptions of auditing".

The above-mentioned work set the idea into motion that the foundations of auditing were not properly worded. In a study issued by The American Institute of Certified Public Accountants, Moonitz (1961, p. 1) states the following:

"Terms such as axiom, postulate, principle, standard, procedure, canon, and rule, among others, are widely used, but with no general agreement as to their precise meaning".

Schandl (1978, p. xiii) joined them almost twenty years after the work by Mautz and Sharaf when he alleges:

"... auditing ... seems to be caught in a frustrating and stationary situation. Auditing was 'done' but was never analyzed as a scientific activity. The 'art of auditing' was supposed to be acquired by imitation ... there was no theory of auditing; there was not even a proper definition of auditing".

The writings by the above-mentioned authors were probably the most important stimulus for professional bodies and academics to develop auditing as a discipline, which has in turn lead to the development and issuing of auditing standards.

In South Africa, the first formal accounting body was formed in Johannesburg in 1894 and was called the Institute of Accountants and Auditors in the South African Republic. The four provinces in South Africa at the time, namely Natal, Transvaal, Cape and Free State each incorporated their own accounting institute. According to Lubbe (1984, p. 4) and Dickinson (1978, p. 4) the four provincial institutes were combined in 1945, to form the Joint Council of the Societies of Chartered Accountants of South Africa. In 1951 the Public Accountants and Auditors Act (Act 51 of 1951) (PAA Act) was issued, providing for the registration and regulation of South African accountants and auditors (Puttick & Van Esch, 1998, p. 5). In 1966, the name of the Joint Council of the Societies of Chartered Accountants of South Africa changed to the National Council of Chartered Accountants (SA).

The issuing of the Companies Act in 1973 in South Africa brought about significant changes in the profession. The Companies Act then required all companies to undergo a statutory annual audit. Furthermore, the National Council of Chartered Accountants (SA) had to issue statements of generally accepted accounting practice (gaap), due to the fact that the Companies Act required auditors to express an opinion on the compliance of companies with gaap (Dickinson, 1978, p. 4). According to Lubbe (1984, p. 4) the National Council of Chartered Accountants (SA) was dissolved in 1980, and the South African Institute of Chartered Accounts (SAICA) was incorporated. SAICA assisted South African auditors in their duties and issued auditing standards.

As from 1994, South Africa started to harmonise the South African auditing standards with International Standards on Auditing (ISAs). These standards were called the South

African Auditing Standards (SAASs). On 1 January 2005, South Africa fully adopted the entire suite of auditing pronouncements as issued by the International Auditing and Assurance Standards Board (IAASB) of the International Federation of Accountants (IFAC). All previously issued SAASs were withdrawn from use as from that date (IRBA.co.za, p. 1; PAAB, 2002, pp. 2-3).

3.3. DEFINITIONS, ANALYSIS OF THE ACT AND EMPIRICAL FINDINGS APPLICABLE TO ASSURANCE ENGAGEMENTS

3.3.1. INTRODUCTION

In 3.2. above it was mentioned that when owners, investors and others are not directly involved in the “management” of an entity in which they are stakeholders, some form of external assurance is needed. In the case of sectional title schemes, external assurance is also necessary - not only as a result of the legal requirements of the Sectional Titles Act, but also due to the following reasons:

- In many cases the owners stand apathetic towards the management of the scheme (refer to section 1.5. in Chapter 1 and section 5.2.2. in Chapter 5);
- The body corporate of a sectional title scheme is entrusted with trust money in the form of levy contributions (see also 1.3., 5.4.1. and 5.4.3);
- Trustees do not necessarily have the skills and experience required to manage a sectional title scheme and its finances on a day-to-day basis (also refer to section 1.3. in Chapter 1 and section 5.4.6. in Chapter 5); and
- The sheer volume of accounting standards and difficulty of accounting standards as per IFRS or IFRS for SMEs (Van Wyk & Rossouw, 2009, p. 99; Stainbank, 2008, p. 3).

In Chapter 2, mention was made of various aspects in the Sectional Titles Act which refers to the concept of auditing and assurance. Reference was also made to the fact that there are various shortcomings, weaknesses and unclear aspects in the wording of the Act. These will be discussed in more detail in this section.

This section will firstly give the definitions of various terms used throughout this chapter as it appears in the SAICA Handbook on Auditing for 2011/2012. Secondly, the sections and rules in the Sectional Titles act which deals with assurance and auditing will be analysed, and the details of the results of the empirical findings will be discussed.

The sample selection for the quantitative empirical study was discussed in detail as part of the section on research methodology in 1.6.5. of Chapter 1.

3.3.2. ASSURANCE ENGAGEMENTS

An **assurance engagement** refers to “*an engagement in which a chartered accountant in public practice expresses a conclusion designed to enhance the degree of confidence of the intended users other than the responsible party about the outcome of the evaluation or measurement of a subject matter against criteria* (SAICA, 2011, pp. ET-2; SAICA, 2011, pp. GLOSS-2-3). (Own emphasis.)

The International Framework for Assurance Engagements identifies two types of assurance engagements that practitioners may perform, namely **reasonable assurance engagements** and **limited assurance engagements** (SAICA, 2011, pp. GLOSS-3). (Own emphasis.)

The objective of a **reasonable assurance engagement** is defined as “a reduction in assurance engagement risk to an acceptably low level in the circumstances of the engagement as the basis for a positive form of expression of the practitioner’s conclusion (SAICA, 2011, pp. GLOSS-3). (Own emphasis.)

The objective of a **limited assurance engagement** is defined as “a reduction in assurance engagement risk to a level that is acceptable in the circumstances of the engagement, but where that risk is greater than for a reasonable assurance engagement, as the basis for a negative form of expression of the practitioner’s conclusion (SAICA, 2011, pp. GLOSS-3). (Own emphasis.)

3.3.3. CHARTERED ACCOUNTANT

A **chartered accountant** is defined as “a chartered accountant registered as such with the Institute and therefore entitled to use the designation “Chartered Accountant”, “Geoktrooieerde Rekenmeester”, “Chartered Accountant (South Africa)”, “Geoktrooieerde Rekenmeester (Suid-Afrika)”, “Chartered Accountant (SA)” OR “Geoktrooieerde Rekenmeeseter (SA)”, or the initials “CA”, “GR”, “CA(SA)”, or “GR(SA)” (SAICA, 2011, pp. ET-3). (Own emphasis.)

3.3.4. AUDITOR

The term **auditor** refers to “the person or persons conducting the audit, usually the engagement partner or other members of the engagement team, or, as applicable, the firm (SAICA, 2011, pp. GLOSS-3). (Own emphasis.)

3.3.5. AUDIT

ISA 200 states that the purpose of an **audit** is to “*enhance the degree of confidence of intended users in the financial statements. This is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. In the case of most general purpose frameworks, that opinion is on whether the financial statements are presented fairly, in all material respects, or give a true and fair view in accordance with the framework* (SAICA, 2011, pp. 200-2). (Own emphasis.)

3.3.6. AUDITOR AS PER THE SECTIONAL TITLES ACT

The first aspect regarding auditing and assurance that is mentioned in the Sectional Titles Act is Prescribed Management Rule (PMR) 2 which deals with “Interpretation”. PMR 2(c) states the following:

*“**auditor**’ means an auditor qualified to act as such under the Public Accountants’ and Auditors’ Act, 1951 (Act 51 of 1951)”* (Own emphasis.)

This interpretation of an “auditor” by the Sectional Titles Act is outdated, as the auditing profession in South Africa is no longer governed by the Public Accountants’ and Auditors’ Act (PAAA). Currently, the profession is governed by the Auditing Profession Act, 2005 (Act 26 of 2005) (APA) and as from January 2006 this Act provides for the establishment of the Independent Regulatory Board for Auditors to do the following:

“provide for the education, training and professional development of registered auditors, to provide for the accreditation of professional bodies; to provide for the registration of auditors, to regulate the conduct of registered auditors; to repeal an Act and to provide for matters connected therewith.” (Own emphasis.)

Statutory interpretation is the process by which courts interpret and apply legislation, especially in cases where vagueness or ambiguity is present (Botha, 2005, pp. 1-2). Regarding repeal of legislation Botha (2005, pp. 39-44) specifically refers to Section 12 of the Interpretation Act. Section 12 of the Interpretation Act 33 of 1957 states that:

“(1) Where a law repeals and re-enacts with or without modifications, any provision of a former law, references in any other law to the provision so repealed shall, unless the contrary intention appears, be construed as references to the provision so re-enacted.”

In his book on statutory interpretation, Botha (2005, p. 67) explains that the legislator consists of a great number of people taking part in the legislative process, and it cannot always be expected of them to be fully up to date with highly specialised technical legislation. Therefore, the concept of “intention of the legislator” is regularly used when interpreting the law (Botha, 2005, p. 49), but it is ultimately dependent on how clear the language used in the legislation may be to the particular court. According to the principles of legal interpretation, unless later legislation rules clearly otherwise, the wording of an act should be interpreted according to the meaning it had on the day that the legislation was approved. The court will also consider the wider context of the stipulations in the act to determine the goal and reasoning of the legislator, in cases where the wording in the act is contradictory (Botha, 2005, pp. 49-51).

Therefore, even though the reference to “*auditor*” and “*Public Accountants’ and Auditors’ Act, 1951*” in the Sectional Titles Act is obsolete, and has after seven years not been amended, the assumption can most probably be made that the principles of legal interpretation will be applicable to IRBA. The reference to “*Public Accountants’ and Auditors’ Act, 1951 (Act 51 of 1951)*” should be interpreted as meaning the “*Auditing Profession Act, 2005 (Act 26 of 2005)*”.

This interpretation of the wording of the Sectional Titles Act was tested for the 60 sets of financial statements selected for testing over a period of two years. The sections containing “General Information” about the bodies corporate were analysed. Out of the sample of 60 financial statements for the financial year ending 2009, all of the sectional title schemes appointed a firm of chartered accountants. Out of the sample of 60 financial statements for the financial year ending 2010, 59 of the 60 schemes appointed a firm of chartered accountants. For the 2010 financial year, only one scheme appointed a registered professional accountant. It therefore seems that, even though the wording of the act is outdated, in practice the term “auditor” is interpreted as being a chartered accountant or a firm of chartered accountants as intended by the Auditing Profession Act, 2005 (Act 26 of 2005).

An internet-based search on the websites of various professional bodies governing accounting and auditing professionals in South Africa revealed that the South African Institute of Professional Accountants also had some difficulty in interpreting the definition of an auditor. In an answer to a technical query on their website (SAIPA, 2012) regarding whether a SAIPA member may sign off financial statements of a body corporate, SAIPA incorrectly quotes the following:

“Annexure 8 defines... “Auditor” is defined as an auditor registered with the Independent Regulatory Board for Auditors as established in terms of section 3 of the Auditing Profession Act 26 of 2005.”

Annexure 8 does not define an auditor according to SAIPA’s “quote”.

3.3.7. APPOINTMENT OF AN AUDITOR

The second aspect regarding auditing and assurance is prescribed in Prescribed Management Rule (PMR) 40 of the Act, the wording of which is as follows:

40. Audit

*At the first general meeting and thereafter at every ensuing annual general meeting, the body corporate shall **appoint an auditor to hold office** from the conclusion of that meeting until the conclusion of the next annual general meeting: Provided that where a scheme comprises **less than 10 units**, an **accounting officer** may be appointed for that purpose and the auditor or accounting officer, as the case may be, **must sign the financial statements**.*

(Own emphasis.)

As per the emphasis above, there are four aspects in this Rule that require clarification. The first aspect is the fact that the heading of PMR 40 in Annexure 8 refers to the concept of “Audit”. The second aspect requiring further clarification is the “appointment of an auditor to hold office”; the third is the concept of the “accounting officer”; and the fourth aspect involves the required “signing of the financial statements.” These four aspects will be dealt with individually below.

3.3.7.1. THE USE OF THE WORD “AUDIT” IN THE HEADING OF PRESCRIBED MANAGEMENT RULE 40

The heading Prescribed Management Rule 40 of Annexure A to the Sectional Titles Act is “*Audit*”. The use of the word “audit” as the heading to this rule is especially important

in the light of the various interpretational challenges of PMR 40, which will be further alluded to in the sections to follow.

In PMR 2 which deals with interpretation no mention is made of the interpretation of the word “audit”. The only close reference is to the interpretation of “auditor” which was discussed in the previous section of this chapter.

According to Botha (2005, p. 79) there are a number of intra-textual aids available for purposes of statutory interpretation. One of these aids is the headings of chapters or sections in an act. He explains that these headings can be seen as “pre-reasons” to such sections, and can be used by the court to determine the “intention of the legislator”. He, however, adds that the value attached to such a heading will depend on the individual circumstances and in the light of the contextual approach, all factors, including headings, should be investigated in order to determine the intention of the legislator (Botha, 2005, p. 80).

One can therefore argue that the “pre-reasoning” to PMR 40 was to have the rule deal with “auditing” and audit-related aspects, even though the term is not clearly defined under the interpretations provided by PMR 2.

3.3.7.2. APPOINT AN AUDITOR TO HOLD OFFICE

PMR 40 only mentions that the body corporate shall “*appoint an auditor to hold office*”, but nowhere in the Act is it stated what exactly is expected from the auditor, other than the last part of Section 40 which says that he “*must sign the financial statements*”. The wording of this section is unclear and is not in line with the standards of the professional bodies governing the audit profession in South Africa.

Botha (2005, p. 69) makes a very important comment in his book on statutory interpretation, namely that where one encounters technical legislation, applicable to specific trades, industries or professions, the wording of that legislation should be interpreted in its specialised, technical context. He refers specifically to the court case of *Kommissaris van Doeane en Aksyns v Mincer Motors* 1959 (1) SA 114 (A).

As discussed in 3.2. of this chapter, the auditing profession has very specific guidelines and standards which is issued by the South African Institute of Chartered Accountants (SAICA) and the Independent Regulatory Board for Auditors (IRBA).

Seen in the light of the above, an auditor cannot simply be “*appointed to hold office*” as indicated by the Sectional Titles Act. As mentioned in 3.3.2. above, there are two different types of assurance engagements which can be performed by an auditor, namely limited assurance engagements and reasonable assurance engagements. According to ISA 210 (SAICA, 2011, pp. ISA 201-3) the auditor has to specifically “*agree the terms of the audit engagement with management or those charged with governance, as appropriate*”. The Sectional Titles Act neither specifies the type of assurance engagement required (if any), nor does it give clear guidance on the terms of the engagement.

Furthermore, the standard (SAICA, 2011, pp. ISA 210-2) prescribes that one of the preconditions for an audit is the following:

“Obtain the agreement of management that it acknowledges and understands its responsibility:

(i) For the preparation of the financial statements in accordance with the applicable financial reporting framework, including where relevant their fair presentation...” (Own emphasis.)

As mentioned in section 1.3. of Chapter 1, the terms “management” and “those charged with governance” can be read as “body corporate” in the case of sectional title schemes. Therefore, according to the ISA 210 quoted above, the auditor of a body corporate should ensure that the body corporate understands that they should prepare the financial statements and that this is not the responsibility of the auditor.

In practice, however, it often happens that the auditor of a sectional title scheme is responsible for both the preparation of the financial statements as well as for the audit thereof. This was evidenced by the results of the empirical study in Chapter 5.

For the sample of 60 sets of financial statements of bodies corporate over a period of two years, the audit reports/accounting officer reports were analysed. For the 2009 financial year 53 of the 60 bodies corporate had a “Report of the Independent Auditor”, 3 had a “Report of the Accounting Officer” and 4 bodies corporate did not have any form of report. For the 2010 financial year 55 of the 60 bodies corporate had a “Report of the Independent Auditor”, 2 had a “Report of the Accounting Officer” and 3 bodies corporate did not have any form of report. The reason why some of the schemes appointed an accounting officer will be discussed in 3.3.7.2. below.

According to the results of the empirical findings it therefore seems that the wording of PMR 40 which states that the body corporate shall “*appoint an auditor to hold office*”, has in practice mostly been interpreted to mean that a full audit should be performed.

Internet-based searches done on the websites of various South African professional bodies governing accounting and auditing practitioners also revealed that there seems to be disagreement and confusion regarding the interpretation of PMR40.

On the SAIPA Technical website (SAIPA, 2012) the question is raised as to whether a SAIPA member may sign off the financial statements of a body corporate consisting of 12 units. SAIPA answers as follows:

“The rules require that the trustees must ... appoint an auditor to hold office ... However, where a scheme comprises less than 10 units, an accounting officer, rather than an auditor may be appointed for that purpose and the auditor or accounting officer, as the case may be, must sign the financial statements.”

SAIPA gives no indication of what is meant by “appoint an auditor to hold office”.

On the website of SAICA (SAICA, 2011) the following very specific technical question is posed:

“What type of assurance / audit report / review is required for Body Corporates under the Sectional Titles Act 95 of 1986? The Act just says that the auditor / accounting officer must “sign the financial statements”. What does this mean? Is an audit of this type of entity required by law? What type of audit / assurance report / review is required?”

The following answer is given:

“If there are 10 or more units, an audit is required. As this is clearly spelt out, it seems that no audit is required if there are less than 10 units – only the accounting officer need sign the financial statements. ... The guidance from the Act is as follows: “Sectional Titles Act, 1986 (Act No. 95 of 1986) Sectional Titles Regulations Annexure 8 Management Rules Duties of trustees Audit 40. At the first general meeting and thereafter at every ensuing annual general meeting, the body corporate shall appoint an auditor to hold office from the conclusion of that meeting until the conclusion of the next annual general meeting: Provided that where a scheme comprises less than 10 units, an accounting officer may be appointed for that purpose and the auditor or accounting officer, as the case may be, must sign the financial statements.”

Once again the professional body does not give clear guidance on the interpretation and it seems as though the specifics of the technical question posed remain largely unanswered.

A further cause for concern is the apparent ignorance of many sectional unit owners as well as so-called “sectional title experts” when it comes to matters relating to accounting and auditing and interpretation of the Act. On the website of Sectional Titles Online (STO), members can have discussions on a website forum. On the STO forum (Sectional Titles Online, 2007) one of the members were concerned about the scheme in which he owned a unit. He saw that an accounting officer performed the duties, and not a “CA”. The answer he received on the forum was: *“rule 40 requires the auditor or accounting officer to perform an audit and sign the financials”*. A further reply stated that *“The auditors should be a company or partnership that is independant [sic] from the MA. If they are, then give them a call and let them know what is [sic] happened.”* This is but one example among many alarming pieces of advice floating around in cyberspace.

Currently available publications on sectional titles also do not give any guidance on auditing other than what is stated in the Act. Paddock’s Sectional Title Survival Manual (2008, pp. 10-1) as well as Pienaar’s publication on Sectional Titles (2010, pp. 163, 169) simply gives the prescriptions of the Act word for word. Conostas and Bleijs (2009, p. 100) state that:

“a body corporate must be managed like a business and every business should be audited every year. The audit, which must be undertaken by an independent auditor, gives members of the body corporate an opportunity to review the financial affairs at yearly intervals, and is an important “checks and balances” mechanism, which ensures that the body corporate is accountable to its members for everything it does from a financial point of view.” (Own emphasis.)

Van der Merwe (2010, p. 14.2.5.3) has a much stronger viewpoint on this, interpreting the Act as follows:

“Since the substitution of rule 40 in 2005,166 the auditor or accounting officer must also sign the financial statements... (Own emphasis.)

He further states (2010, p. 14.4.6.) the following:

“From 2005 the financial statements of the trustees must be audited and signed by the auditor or the accounting officer, as the case may be...” (Own emphasis.)

From the above it is clear that there are varying opinions among experts in the field of sectional titles, academics and professional bodies regarding the interpretation of PMR 40.

3.3.7.3. ACCOUNTING OFFICER

PMR 40 further states that if there are fewer than 10 units, an “*accounting officer*” can be appointed and that he must “*sign the financial statements*”. In PMR 2(b) the Act defines an “*accounting officer*” as follows:

*“**‘accounting officer’** means a person who in terms of section 60 (2) of the **Close Corporation Act, 1984 (Act 69 of 1984)**, is qualified to perform the duties of an accounting officer.” (Own emphasis.)*

3.3.7.3.1. THE DEFINITION OF ACCOUNTING OFFICER

Prescribed Management Rule 50 of the Sectional Titles Act refers to the Close Corporation Act for purposes of defining an “*accounting officer*”. The Close

Corporations Act, No. 69 of 1984, was enacted by Parliament in South Africa in June 1984. A close corporation, or CC, enables smaller businesses to operate with a legal personality separate from its individual members, providing less complexity and easier legal administration than a company. Close corporations are also less expensive to operate and provide limited liability and perpetual succession. The Companies Act, 2008 has significantly changed the regulatory framework applicable to close corporations and furthermore prohibits the registration of any new close corporation after 1 May 2011. Existing close corporations would, however, be administered indefinitely under the Close Corporations Act, 1984. (SAICA, 2011). It is once again important to note that, as mentioned in section 2.2. of Chapter 2, the provisions of the Close Corporations Act do not apply to sectional title schemes in South Africa.

Section 60 of the Close Corporations Act, No. 69 of 1984 defines an “accounting officer” as follows:

“Qualifications of accounting officers

60.(1) No person shall be appointed as or hold the office of an accounting officer of a corporation, unless he is a member of a recognized profession which-

(a) as a condition for membership, requires its members to have passed examinations in accounting and related fields of study which in the opinion of the Minister would qualify such members to perform the duties of an accounting officer under this Act;

(b) has the power to exclude from membership those persons found guilty of negligence in the performance of their duties or of conduct which is discreditable to their profession; and

(c) has been named in a notice referred to in subsection (2).

[Sub-s. (1) amended by s. 9 (a) of Act 81 of 1992.]

(2) The Minister may from time to time publish by notice in the Gazette the names of those professions whose members are qualified to perform the duties of an accounting officer in terms of this Act.

(3) A member or employee of a corporation, and a firm whose partner or employee is a member or employee of a corporation, shall not qualify for appointment as an accounting officer of such corporation unless all the members consent in writing to such appointment.

(4) A firm as defined in section 1 of the Public Accountants' and Auditors' Act, 1991 (Act 80 of 1991), and any other firm may be appointed as an accounting officer of a corporation, provided each partner in the latter firm is qualified.”
(SAICA, 2010, p. 305) (Own emphasis.)

The SAICA Technical website (SAICA, 2011, p. FAQ) gives guidance on the interpretation of this section of the Close Corporation Act by listing specific individuals who fall within the scope of the definition. According to SAICA, the members of the following professional bodies are qualified to act as accounting officer:

“1. The South African Institute of Chartered Accountants A Chartered Accountant (SA) CA(SA) or An Associate General Accountant (SA) AGA(SA)

2. Auditors registered in accordance with the provisions of the Auditing Profession Act No. 26 of 2005 - A Registered Auditor (RA)

3. The Southern African Institute of Chartered Secretaries and Administrators ACIS/FCIS

4. The Chartered Institute of Management Accountants CIMA

5. The South African Institute of Professional Accountants Professional Accountant (SA)

6. The Chartered Association of Certified Accountants ACCA

7. The Institute of Administration and Commerce of Southern Africa IAC

8. The South African Institute of Business Accountants SAIBA

9. The Members of the Chartered Institute for Business Management only certain members”.

As mentioned in 3.3.7.1. above, for the 2009 financial year 3 of the 60 bodies corporate analysed had a “Report of the Accounting Officer” and for the 2010 financial year 2 of the bodies corporate had a “Report of the Accounting Officer” as part of the financial statements. All three of the “Accounting Officer Reports” issued for the 2009 financial year were issued by firms of Chartered Accountants. Of the two “Accounting Officer Reports” issued in 2010, one was issued by a firm of Chartered Accountants and one was issued by a SAIPA Certified Professional Accountant. According to these findings, the Sectional Titles Act and resultant reference to the Close Corporations Act defining the concept of “accounting officer” was correctly interpreted.

3.3.7.3.2. THE NUMBER OF UNITS

PMR 40 states that if there are less than 10 units, an “*accounting officer*” can be appointed and that he must “*sign the financial statements*”.

For the sample of 60 sets of financial statements of bodies corporate over a period of two years, the audit reports/accounting officer reports were analysed. In the sample of 60 bodies corporate, 11 were classified as small (consisting of fewer than 10 units), 46 were classified as medium (between 10 and 50 units) and three schemes were classified as large (more than 50 units). Also refer to 1.6.5. in Chapter 1 for more detail on the background to the quantitative research methodology.

For the 2009 financial year, 3 of the 11 small schemes had a “Report of the Accounting Officer”. For that year, 8 of the 11 small schemes had a “Report of the Independent

Auditor”. For the 2010 financial year, 2 of the 11 small schemes had a “Report of the Accounting Officer” and 8 of the 11 small schemes had a “Report of the Independent Auditor”. The remaining small scheme had no assurance report of any kind for the 2010 financial year. According to these results of the empirical data, only 27.27% of the small schemes identified opted for an accounting officer report in 2009, and 18.18% opted for an accounting officer report in 2010. The remaining schemes were audited.

3.3.7.3.3. AUDIT FEES

The question inevitably arises as to whether audit fees are a large expense for bodies corporate and if there is a difference in the fees charged for small, medium and large schemes.

For the total sample, audit fees amounted to 1.50% of average total expenses in 2008, 1.03% in 2009 and 1.09% in 2010. For the small entities, average audit fees amounted to 2.41% of average total expenses in 2008, 3.07% in 2009 and 2.79% in 2010. For the medium entities, average audit fees amounted to 1.94% of average total expenses in 2008, 1.32% in 2009 and 1.27% in 2010. For the large entities the figures were 0.48%, 0.19% and 0.47% for 2008, 2009 and 2010 respectively.

Of all the expenses which were analysed as a percentage of average total expenses, audit fees was one of the lowest when expressed as a percentage of average total expenses. Section 4.4. in Chapter 4 contains a detailed analysis of these figures. The conclusion that can be drawn from these figures is that, when expressed as a percentage of average total expenses, audit fees are relatively low compared to other expenses of the bodies corporate analysed.

One can also analyse the audit fees for bodies corporate in terms of actual rand amounts. Expressed in rand terms, average audit fees per unit for the total sample were R82.74 in 2008, R61.98 in 2009 and R71.51 in 2010. Expressed in rand terms, average audit fees per unit for the small entities in the sample were R109.84 in 2008, R147.54 in 2009 and R169.73 in 2010. For the medium entities identified average audit fees per unit amounted to R100.50 in 2008, R72.63 in 2009 and R79.30. For the 3 large entities the average audit fees per unit amounted to R25.58, R11.82 and R26.87 for 2008, 2009 and 2010 respectively. That means that, based on average audit fee per unit expressed in rand terms, a small entity spent 9.3% more than a medium entity and 329.41% more than a large entity in 2008. In 2009, a small entity spent 103.17% more than a medium entity and 1147.99% more than a large entity. A small entity spent 114.06% more than a medium entity and 531.80% more than a large entity in 2010.

Therefore, at first glance audit fees seem relatively low as a percentage of average total expenses for small, medium as well as large entities. However, as seen in the above paragraph, audit fees are significantly higher for small and medium entities than it is for large entities when expressed in rand terms.

A further question which arises in this regard is whether it is less costly to appoint an accounting officer to review the financial statements than to appoint an auditor to perform an audit.

In 2009 the 3 small entities that made use of an accounting officer paid on average R907.96 per scheme for the services of the accounting officer. This amounted to R164.30 per unit. In 2010, the 2 small entities that made use of an accounting officer paid R1 265.00 on average per scheme for the services of an accounting officer. This amounted to R149.44 per unit. In 2009, the 8 small entities that made use of an auditor paid R1 329.25 on average per scheme for the services of the auditor. This amounted

to R200.64 per unit. In 2010, the 2 entities that made use of an auditor paid R1 144.44 on average per scheme for the services of the auditor. This amounted to R177.58 per unit.

Therefore, based on rand amounts, in 2009 it was 46.40% less expensive for a small scheme to use the services of an accounting officer, whereas in 2010 it was 9.53% more expensive. Based on rand per unit, in 2009 it was 22.12% less expensive for a small scheme to use the services of an accounting officer and in 2010 it was 18.83% less expensive. It should, however, be noted that the sample used in this case was very small and is by no means representative of the entire population of schemes. Various other factors also play a role when an auditor or accounting officer determines his fees for professional work. This will be discussed in detail as part of the empirical findings in Chapter 5.

3.3.7.4. SIGNING OF FINANCIAL STATEMENTS

In 3.3.7.2. above, the concept of “appointment of an auditor to hold office” was discussed. From the above it is clear that there are varying opinions among experts in the field of sectional titles, academics and professional bodies regarding the interpretation of that section of PMR 40.

PMR 40, however, includes another section that is unclear. It states:

*“...and the auditor or accounting officer, as the case may be, **must sign the financial statements...**”* (Own emphasis.)

As was the case in 3.3.7.2., Botha's viewpoint (2005, p. 69) should again be taken into consideration here. His viewpoint regarding statutory interpretation is that where one encounters technical legislation, applicable to specific industries or professions, the wording of that legislation should be interpreted in its specialised, technical context.

ISA 700 (SAICA, 2011, pp. ISA700-1) deals with the auditor's responsibility to form an opinion on and report on financial statements. It also deals with the form and content of the auditor's report issued as a result of an audit of financial statements.

The difference in the wording between the Sectional Titles Act and the International Standard on Auditing is important. The International Standard on Auditing (SAICA, 2011, pp. ISA700-1) states that the auditor should "form an opinion on and report on financial statements", not to "sign the financial statements", as stated in PMR 40. Furthermore, at the conclusion of an audit, "the auditor's report shall be signed" (SAICA, 2011, pp. ISA700-7), and not the financial statements as prescribed by PMR 40. (Own emphasis.)

In relation to this ISA 200 (SAICA, 2011, pp. ISA200-3) states the following:

"The auditor may also have certain other communication and reporting responsibilities to users, management, those charged with governance, or parties outside the entity, in relation to matters arising from the audit. These may be established by the ISAs or by applicable law or regulation." (Own emphasis.)

The wording of PMR40 stating "must sign the financial statements" does not, however, imply any communicating or reporting responsibilities in relation to matters arising from the audit, therefore ISA 200 cannot be used to interpret PMR40.

In paragraph 21 of ISA 210 (SAICA, 2011, pp. ISA210-5), the following guidance is given for under the heading “Auditor’s Report Prescribed by Law or Regulation”:

“In some cases, law or regulation of the relevant jurisdiction prescribes the layout or wording of the auditor’s report in a form or in terms that are significantly different from the requirements of ISAs. In these circumstances, the auditor shall evaluate:

- (a) Whether users might misunderstand the assurance obtained from the audit of the financial statements and, if so,*
- (b) Whether additional explanation in the auditor’s report can mitigate possible misunderstanding...” (Own emphasis.)*

The interpretation of the signing of financial statements as prescribed in PMR 40 by Van der Merwe (2010, p. 14.2.5.3) in his book on Sectional Titles is as follows:

“Since the substitution of rule 40 in 2005,166 the auditor or accounting officer must also sign the financial statements of the trustees which increase his or her responsibility. (Own emphasis.)

“The annual financial statement of receipts and expenditure presented to the annual general meeting by the trustees must be audited by the auditor or accounting officer, as the case may be.” (Own emphasis.)

“The contract of appointment should cover key matters such as the scope of the audit, a review of internal control mechanisms, the date of delivery of the auditor’s report, and the amount of the auditor’s fee. Well-maintained records, competent management personnel, a strong budget committee and a co-operative relationship between client and auditor simplify the auditor’s task and help reduce the cost of the audit.” (Own emphasis.)

Van der Merwe's first statement is incorrect on three different levels. The first reason for it being incorrect is that, as mentioned earlier, an auditor forms an opinion on and reports on financial statements, instead of signing the financial statements. The audit report is signed, not the financial statements. The second reason for his statement being incorrect is the phrase that states "*must sign the financial statements of the trustees.*" As already mentioned in Chapter 2, the actual financial statements are those of the body corporate, not of the trustees. The trustees are only responsible for the preparation thereof. The third aspect that discredits his statement is that it is unclear what the author means by stating that it "*will increase his or her responsibility*". An auditor has various responsibilities such as, for example, the responsibilities relating to fraud in an audit (SAICA, 2011, p. ISA240), amongst others, but all of the responsibilities arise from performing an actual audit, not simply from the signing of financial statements. Furthermore, there are various aspects that can be increased in an audit, for instance, the assessed risk of material misstatement (SAICA, 2011, p. ISA330) or the level of materiality (SAICA, 2011, p. ISA320), but the responsibility of an auditor cannot be increased just because of the "signing" of the "financial statements". From an auditor's perspective Van der Merwe's statement is therefore perhaps misleading.

Van der Merwe's second statement that the "*annual financial statement of receipts and expenditure*" must be audited is also not correct in terms of International Financial Reporting Standards. There is no such thing as an "*annual financial statement of receipts and expenditure*". Financial statements consist of, amongst others, a statement of profit or loss and other comprehensive income (formerly referred to as an income statement), a statement of financial position (formerly referred to as a balance sheet), a statement of changes in equity, a cash flow statement as well as notes to the financial statements. Also refer to section 4.3.5. in Chapter 4 for further detail on the requirements regarding the presentation of financial statements.

Van der Merwe's third statement is once again only partially accurate. The author is correct in his statement that there should be a "*contract of appointment*", despite the evidently erroneous wording. ISA 210 deals with agreeing on the terms of audit engagements (SAICA, 2011, pp. ISA210-1) and provides an example of an Audit Engagement Letter (SAICA, 2011, pp. ISA210-14-15). Van der Merwe is under the incorrect impression regarding internal control, as an audit does not necessarily entail a "*review of internal control mechanisms*", as he puts it. In making his risk assessment, an auditor will consider the internal control relevant to an entity's preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not necessarily for the purpose of expressing an opinion on the effectiveness of the entity's internal control (SAICA, 2011, pp. ISA265-1). Another obvious blunder in the author's statement is that he is of opinion that measures such as a budget committee and a good co-operative relationship "*help reduce the cost of the audit*". This observation is very far from the truth.

In his book on Sectional Titles, Van der Merwe further states (2010, p. 14.4.6.) the following:

*"From 2005 the financial statements of the trustees must be audited and signed by the auditor or the accounting officer, as the case may be. It has been suggested that these officials should not only provide an analysis of the body corporate's debts but should also **certify** that adequate provision has been made in the budget for payment of the arrear debts of the body corporate."* (Own emphasis.)

Once again, he mentions the statements should be "*audited and signed*". He also adds two additional responsibilities, being provision of an analysis of the debts of the body corporate, and certification that provision has been adequately made for the payment of arrear debts.

To say that the auditor or accounting officer should provide an “analysis of the debts of the body corporate” is a very broad and unclear statement. It is true that PMR 37 states the following:

“(2) The financial statement shall include information and notes pertaining to the proper financial management by the body corporate, including:

(a) the age analysis of debts in respect of levies, special levies and other contributions;

(b) the age analysis of amounts owing by the body corporate to the creditors...” (Own emphasis.)

The specific wording of the Act is, however, different from how Van der Merwe interprets it. The Act states that the financial statements (as prepared by the trustees) should include an age analysis of debts and amounts owing, but nowhere does the Act state that the auditor should provide an analysis of the body corporate’s debts. The term “analysis” is also an extremely wide concept and one can but wonder what the author had in mind when he interpreted the Act.

Van der Merwe bestowed a further, perhaps even more daunting, task on the auditors and accountants stating that they should “certify that adequate provision has been made in the budget for payment of the arrear debts of the body corporate.” (Own emphasis.) Maree (2006, pp. 1-3) has an even stronger viewpoint in his article in the *Property Law Digest*. Maree contends the following:

“It should be a statutory requirement (as opposed to a mere management rule), that auditors should certify in respect of all budgets that adequate provision has been made therein for payment of body corporate debts.” (Own emphasis.)

He goes even further to add:

“Once the trustees have determined the individual levies in terms of section 37(2), a final budget schedule must be certified by the auditor to the effect that

the levies reflected therein are in accordance with the budget and the participation quotas.” (Own emphasis.)

It should be noted that the term “certify” is not a formally acknowledged term in auditing literature and should not be thrown around at random as a synonym for “audit” when interpreting the Act. See also Lubbe (1987, pp. 25-27).

The confusing interpretations above regarding the signing of financial statements may very well be a classic example of the audit expectation gap. Therefore it would, at this point in the study, be appropriate to consider the audit expectation gap in greater detail.

3.3.7.4.1. THE EXPECTATION GAP

The concept of the audit expectation gap has been around for a long time and is considered to be one of the foremost issues confronting the auditing profession worldwide (Sikka, Puxty, Willmott, & Cooper, 1998, p. 299; Koh & E-Sah, 1998, pp. 147-150). There is a distinct difference between what the audit profession perceives their objectives to be, and what the public expects from an audit, or “thinks” that the auditor does (Sikka, Puxty, Willmott, & Cooper, 1998, p. 302; Koh & E-Sah, 1998, pp. 148-149; Wolf, Tackett, & Claypool, 1999, pp. 468-469). Research by Gloeck and de Jager (1993, p. 27) revealed that even financially knowledgeable persons have certain expectations regarding audits which falls outside the scope of normal audits and cannot be met by auditors.

The audit report is one of the primary aspects in the expectation gap. The two parties each have their own perception of what it entails; for instance, certify or guarantee. The users of financial statements are often not satisfied with how audit findings are

communicated (Gaston, 1987, p. 38). Lubbe (1990, p. 8) explains that the core of the expectation gap between the profession and the client ('client' specifically referring to outside stakeholders) lies between the risk that the auditing profession is prepared to accept in respect of annual financial statements and the confidence which clients search for in the statements.

One possible logical conclusion for the confusion evident from the above sections of this chapter is that the legislator who wrote the Sectional Titles Act, as well as the interpreters of the Act, all fell into the trap of the expectation gap.

3.3.7.4.2. COMPARISON TO THE CLOSE CORPORATIONS ACT

To further illustrate the point of the inappropriate wording regarding the signing of financial statements in the Sectional Titles Act, reference can be made to the Close Corporations Act No. 69 of 1984. Section 58 of the CC Act states the following:

“(2) The annual financial statements of a corporation – ...

(e) shall contain the report of the accounting officer referred to in section 62 (1) (c).” (Own emphasis.)

The detail of Section 62 being as follows:

“(1) The accounting officer of a corporation shall, not later than three months after completion of the annual financial statements-

(a) subject to the provisions of section 58 (2) (d), determine whether the annual financial statements are in agreement with the accounting records of the corporation;

(b) review the appropriateness of the accounting policies represented to the accounting officer as having been applied in the preparation of the annual financial statements; and

(c) report in respect of paragraphs (a) and (b) to the corporation.” (Own emphasis.)

From the above extracts it is clear that nowhere in the Close Corporations Act is it stated that the accounting officer should sign the financial statements. The accounting officer performs certain procedures, after which a report is issued. There is also a distinct difference between the duties that have to be performed by the accounting officer, and the scope of a full audit.

For the sample of 60 sets of financial statements of bodies corporate over a period of two years, the financial statements as well as the audit reports/accounting officer reports were analysed. None of the financial statements were signed by the auditors or accounting officers for the years 2009 and 2010. As discussed above, auditors and accounting officers do not sign financial statements. For the 2009 financial year 53 of the 60 bodies corporate had a “Report of the Independent Auditor”, 3 had a “Report of the Accounting Officer” and 4 bodies corporate did not have any form of report. For the 2010 financial year 55 of the 60 bodies corporate had a “Report of the Independent Auditor”, 2 had a “Report of the Accounting Officer” and 3 bodies corporate did not have any form of report.

The conclusion can therefore be made that for the 2009 and 2010 financial years, the auditors and accounting officers did not follow the prescriptions of “signing the financial statements” as per the Sectional Titles Act. The practitioners rather opted for the issuing and signing of the relevant audit and accounting officer reports.

3.3.8. CONFIRMATION

A further aspect regarding auditing assurance mentioned in the Act is stipulated in Prescribed Management Rule (PMR) 56(i), which states the following regarding compulsory items on the AGM agenda:

*“the **confirmation** by the **auditor or accounting officer** that any amendment, substitution, addition or repeal of the rules (as contemplated in section 35(5) of the Act) have been submitted to the Registrar of Deeds for filing as contemplated in section 35(5)(c) of the Act.”* (Own emphasis.)

For the sample of 60 sets of financial statements of bodies corporate over a period of two years, the financial statements as well as the audit reports/accounting officer reports were analysed. None of the audit reports or accounting officer reports made any specific mention of PMR 56. In some cases the information was simply stated in the supplementary information to the financial statements. For the financial year ended 2009, 45 (75%) of the financial statements had a sentence in the supplementary information to the financial statements stating that no changes were made to the rules of the complex, or that changes have been submitted to the Registrar, whatever the case may be. However, in 37 of the 45 instances (82.22%) where the information was contained in the supplementary information to the financial statements, the supplementary information was not audited. For the financial year ended 2010, 54 (90%) of the financial statements had a sentence in the supplementary information to the financial statements stating that no changes were made to the rules of the complex, or that changes have been submitted to the Registrar, whatever the case may be. However, in 37 of the 54 instances (68.52%) where the information was contained in the supplementary information to the financial statements, the supplementary information was not audited.

The conclusion can be made that most of the supplements to the financial statements mentioned the fact that there were no changes to the rules or that rules were submitted

to the Registrar. However, in the majority of these cases, the supplementary information was not audited. Therefore, there was no “*confirmation by the auditor or accounting officer*” as prescribed by PMR 56 of the Sectional Titles Act.

3.3.9. AMENDMENT OF RULES

In terms of rules of a body corporate, the following is stipulated in Section 35 of the Act:

*“(1) A scheme shall as from the date of the establishment of the body corporate be controlled and managed, subject to the provisions of this Act, by means of **rules***

(2) The rules shall provide for the control, management, administration, use and enjoyment of the sections and the common property, and shall comprise

*(a) management rules, prescribed by regulation, which rules may be substituted, added to, amended or repealed by the developer when submitting an application for the opening of a sectional title register, to the extent prescribed by regulation, **and which rules may be substituted, added to, amended or repealed from time to time by unanimous resolution of the body corporate as prescribed by regulation...**” (Own emphasis.)*

In her article, Jennifer Paddock (2010, p. 8) explains that the Sectional Titles Act makes provision for rules to be altered, but that the necessary procedures should be followed. Since the auditing of a scheme is governed by Prescribed Management Rules (PMR) 2, 40 and 56, one can interpret Section 35 in such a way that a unanimous resolution may be passed, removing those PMRs from the rules of the scheme. This can be especially helpful in cases such as, for example, a self-managed scheme with one owner who does not want to incur the extra expense and administration involved in having the financial statements of the complex audited.

It is, however, not advisable in general, due to many banks requiring audited financial statements of a body corporate as one of the prerequisites in granting a home loan to a prospective buyer of a sectional title unit.

For the sample of 60 sets of financial statements of bodies corporate over a period of two years, the financial statements as well as the audit reports/accounting officer reports were analysed. None of the entities changed their rules in such a way that the compulsory auditing of the schemes was no longer required.

3.4. GENERAL EMPIRICAL FINDINGS

3.4.1. AUDITING OR INSPECTION OF BUDGET

None of the audit reports or accounting officers reports analysed gave any indication that the budget of the body corporate for the ensuing financial year was inspected or audited. In section 3.3.7.4 above it was mentioned that Van der Merwe (2010, p. 14.4.6.) wants the auditors to “***certify that adequate provision has been made in the budget for payment of the arrear debts of the body corporate.***” (Own emphasis.) As mentioned in that section, his erroneous interpretation of the Act is probably due to the expectation gap. It is furthermore clear that no inspection or auditing of body corporate budgets occurred for the selected sample.

3.4.2. AUDITING OF SUPPLEMENTARY INFORMATION

For the sample of 60 sets of financial statements of bodies corporate over a period of two years, the audit reports were analysed. The audit reports contained the following wording (with a few variations on the specific formulation):

“We have audited the accompanying financial statements of the Body Corporate of, which comprises of the trustee’s report, the balance sheet as at, the income statement for the year then ended, a summary of significant accounting policies and other explanatory notes, as set out on pages xx to xx.” (Own emphasis.)

Some of the financial statements analysed contained supplementary information in the form of an explanation of audit fee provision, a debtors age analysis, information regarding changes to the rules of the complex, or a statement regarding the solvency of the body corporate.

For the 2009 financial year, 10 of the 60 sets of financial statements contained no supplementary information whatsoever. For the 2009 financial year, 53 of the 60 bodies corporate had a “Report of the Independent Auditor”. Of these reports, only 7 indicated that the supplementary information was audited. In these cases, the line “*as set out on pages xx to xx*” in the audit report included the page numbers containing the supplementary information.

For the 2010 financial year, 2 of the 60 sets of financial statements contained no supplementary information whatsoever.

For the 2010 financial year 55 of the 60 bodies corporate had a “Report of the Independent Auditor”. Of these reports, only 10 indicated that the supplementary information was audited. In these cases, the line “*as set out on pages xx to xx*” in the audit report included the page numbers containing the supplementary information.

An interesting observation was made regarding the auditing of supplementary information. In 2010, 10 reports indicated that supplementary information was audited, compared to 7 reports in 2009. From these reports there was only one body corporate for which both the 2009 and 2010 supplementary information was audited according to the wording of the audit report. Further inspection into this inconsistency indicated that in many instances the audit reports used seemed to be a template that was copied and pasted from one year to the next. This sometimes resulted in the line “*as set out on pages xx to xx*” in the audit report to be exactly the same from year to year, even though the page numbers did not stay the same.

The problem with this is that it may lead to an assumption by the reader of the audit report that the supplementary information was audited, when it was not the case, or vice versa. Practitioners should exercise caution when using audit report templates to ensure that only the information that was indeed audited is included in the pages indicated by the audit report.

3.4.3. QUALIFIED AUDIT REPORTS

For the sample of 60 sets of financial statements of bodies corporate over a period of two years, the audit reports were analysed. For the 2009 financial year, 53 of the 60 bodies corporate had a “Report of the Independent Auditor” and for the 2010 financial year 55 of the 60 bodies corporate had a “Report of the Independent Auditor”.

From all the audit reports analysed, only one body corporate received a qualified audit report. The specific body corporate received a qualified audit report for both the 2009 and 2010 financial year, stating that the body corporate is not a going concern.

3.4.4. FINANCIAL STATEMENTS NOT COMPLYING WITH SOUTH AFRICAN STATEMENTS OF GENERALLY ACCEPTED ACCOUNTING PRACTICE

For the sample of 60 sets of financial statements of bodies corporate over a period of two years, the audit reports were analysed. For the 2009 financial year, 53 of the 60 bodies corporate had a “Report of the Independent Auditor”, and all of these audit reports contained an emphasis of matter paragraph stating that the financial statements do not comply with South African Statements of Generally Accepted Accounting Practice (SA GAAP). For the 2010 financial year 55 of the 60 bodies corporate had a “Report of the Independent Auditor”. Once again, all of these audit reports contained an emphasis of matter paragraph stating that the financial statements do not comply with SA GAAP.

3.4.5. SECTIONAL TITLES ACT TAKEN INTO ACCOUNT

For the sample of 60 sets of financial statements of bodies corporate over a period of two years, the audit reports were analysed. For the 2009 financial year 53 of the 60 bodies corporate had a “Report of the Independent Auditor”, and for the 2010 financial year, 55 of the 60 bodies corporate had a “Report of the Independent Auditor”. None of these audit reports mentioned that any aspects of the Sectional Titles Act were taken into account when performing the audit.

3.5. CONCLUSION

The chapter started with a brief history and background of auditing. Definitions and sundry aspects relating to assurance engagements were evaluated. Various sources were used, including the Sectional Titles Act, The SAICA Handbook on Auditing, the

Close Corporations Act, and literature on the aforementioned. It is clear that there is much uncertainty, ambiguity and confusion on what is expected regarding the audit of bodies corporate. Most of these issues probably stem from the expectation gap, as explained. An analysis was made of assurance-related aspects of a sample of audit reports of body corporate annual financial statements. From this analysis it is evident that auditing and accounting practitioners are not always acting consistently and that they are also not consistent in their application of the Sectional Titles Act.

Chapter 4 will investigate aspects relating to the accounting and reporting of sectional title schemes. The legal requirements for financial reporting by bodies corporate and currently available reporting frameworks will specifically be addressed. The possibility of a sectional title-specific reporting framework as well as the findings based on an analysis of a sample of body corporate financial statements over a period of three years will also be discussed.

CHAPTER 4 – ACCOUNTING AND REPORTING ASPECTS RELATING TO SECTIONAL TITLE SCHEMES

“Therefore, the Kingdom of Heaven can be compared to a king who decided to bring his accounts up to date with servants who had borrowed money from him”. - Matthew 18:23
NLT

“(The bookkeeper) is clean, immaculately clean, physically, mentally and morally, and the only creature who can handle red ink, a bad pen and a rough edged ruler without blotting the page. His cleanliness borders on the supernatural... The next feature of the bookkeeper for consideration is his system. This often borders on the marvellous... It always paralyses the easygoing businessman with wonder. System, system, the regulator of the universe, what a wonder it is! The competent bookkeeper usually knows more about a firm’s business than the entire board of directors together”. - Brown 1909, p.77-81

4.1. INTRODUCTION

Chapter 2 gave an overview of the legal matters relating to the sectional title industry in South Africa as far as it concerns accounting, auditing, finances and management of sectional title schemes. As already mentioned in Chapter 1, there are various aspects regarding accounting in the Sectional Titles Act which are unclear, or has some form of ambiguity, weakness or shortcoming. In this chapter, these aspects will be further alluded to against the background of the study, as set out in Chapter 1. This chapter will start with a brief history and background of accounting and deal in greater detail with accounting-related aspects relating to sectional title schemes. In the chapter an attempt will also be made to address the question as to whether International Financial Reporting Standards is not perhaps too cumbersome and expensive for the users of

body corporate financial statements. The possibility of another alternative framework for use by bodies corporate will be looked into. An analysis will also be made of accounting-related aspects of a sample of body corporate annual financial statements. The financial statements with accompanying audit reports were obtained from a managing agent of bodies corporate for the financial years ending 2009 and 2010. Since the 2009 financial statements also have figures for the comparative financial year (2008), the data of three financial years is available for analysis. The audit reports for the selected bodies corporate drawn up by the appointed accounting and auditing practitioners also formed part of the data that have been analysed.

4.2. THE HISTORY AND BACKGROUND OF ACCOUNTING: A BRIEF OVERVIEW

The concept of accounting has been around for thousands of years. Governments and individuals with large wealth needed to keep accurate and detailed records. Archaeologists have found evidence of ancient Egyptian civilisations keeping records of transactions and taxes on clay tablets dating as far back as 4000 B.C (Gordon, 1992, pp. 18-19; Kew & Watson, 2012, p. 8; Berry, De Klerk, & Doussy, 2011, p. 5). For hundreds of years, records of commerce were produced in Mesopotamia, with scribes writing up transactions for farmers, merchants and government and ensuring that these transactions complied with commercial requirements (Kew & Watson, 2012, p. 8; Carnegie & Napier, 1996, pp. 9-10).

Although evidence exist that business transactions have been recorded for many thousands of years, there was no organised system recording events until the Middle Ages. This was mainly due to the fact that the numbering systems of the time, being Roman numerals, were too cumbersome to use. During the Renaissance, the Italians actively sought more efficient ways of keeping financial records (Kew & Watson, 2012, pp. 8-9). Benedetto Cotrugli wrote the first chapter on accounting in his 1458

manuscript *Della mercatura e del mercante perfetto* (Yamey, 1994, pp. 43-50; Berry, De Klerk, & Doussy, 2011, p. 5). Thirty-six years later, in 1494, an Italian by the name of Luca Pacioli completed the first published work fully describing the double entry system (Carnegie & Napier, 1996, pp. 11-25). His book *Summa de arithmetica, geometria, proportioni et proportionalità* applied mathematical principles to trade and industry in the Renaissance society. The Venetian double-entry method of bookkeeping described in his monumental work laid the foundation for the universal standard for accounting which is still used today (Kew & Watson, 2012, p. 9; Berry, De Klerk, & Doussy, 2011, p. 5). The early literature works up until the nineteenth century focused on the technique of bookkeeping, explaining how recording of transactions should take place using the double-entry system. The development of the theory of accounting began only in the nineteenth century (Carnegie & Napier, 1996, pp. 9-10; Berry, De Klerk, & Doussy, 2011, p. 5).

During the late 1800's and early 1900's, the accounting profession saw the rise of organised societies of accountants around the globe. As mentioned in Chapter 3, the first formal accounting body in South Africa was formed in Johannesburg in 1894 and was called the Institute of Accountants and Auditors in the South African Republic (Berry, De Klerk, & Doussy, 2011, p. 5; Lubbe, Modack, & Watson, 2011, p. 8). The four provinces in South Africa at the time, namely Natal, Transvaal, Cape and Free State each incorporated their own accounting institute. According to Lubbe (1984, p. 4) and Dickinson (1978, p. 4) the four provincial institutes were combined in 1945 to form the Joint Council of the Societies of Chartered Accountants of South Africa. In 1951, the Public Accountants and Auditors Act (Act 51 of 1951) (PAA Act) was issued, providing for the registration and regulation of South African accountants and auditors (Puttick & Van Esch, 1998, p. 5). In 1966, the name of the Joint Council of the Societies of Chartered Accountants of South Africa changed to the National Council of Chartered Accountants (SA). Today, there are many regional and national accounting societies and institutes, the most prominent being the South African Institute of Professional Accountants (SAIPA) and the South African Institute of Chartered Accountants (SAICA).

Many international accounting institutes and societies are also recognised by the profession in South Africa. Some examples of these are the Chartered Institute of Management Accountants (CIMA), the Association of Chartered Certified Accountants (ACCA) and the Association of Accounting Technicians (AAT).

Over the years, accounting standard-setting bodies worldwide have tried to resolve accounting problems by developing accounting standards (Wingard, Von Well, Pretorius, Ferreira, Badenhorst, & Van der Merwe, 2011, p. 3). The accounting profession in the United States of America recognised the importance of establishing formal accounting standards as early as the 1930's (Gordon, 1992, p. 11) with the first serious attempt at developing a formalised structure for accounting theory in the 1960's with the establishment of the Accounting Principles Board (Oberholster, et al., 2011, p. 10). In 1973, the Financial Accounting Standards Board (FASB) succeeded the APB with the mandate of setting accounting standards. The accounting profession in South Africa developed South African GAAP since the early 1970s and enjoyed high international recognition over the years for the quality and strength of its reporting standards (Verhoef, 2012, pp. 1-5). Financial reporting standards require a more consistent treatment of transactions, thereby establishing comparability and continuity in financial statements (Lubbe, Modack, & Watson, 2011, p. 6).

The problem was that the first accounting standards were developed without a proper theoretical framework as foundation and often key issues were addressed across more than one standard (Wingard, Von Well, Pretorius, Ferreira, Badenhorst, & Van der Merwe, 2011, p. 3). As a result of varying accounting regulatory frameworks for financial reporting throughout the world, financial statements differed across various accounting regimes. This often resulted in compromised comparability, a loss of credibility of financial statements and impaired competition among global capital markets (Oberholster, et al., 2011, pp. 1-12). At the 10th World Congress of Accountants in Sydney, Australia in 1972, a proposal was put forward for the establishment of an International Accounting Standards Committee (IASC). The next

year the IASC was formed and the committee was sponsored by nine countries including, amongst others, the United States, Canada, Germany and Japan. Until 1998, the committee completed a core set of financial accounting standards (Alfredson, Leo, Picker, Loftus, Clark, & Wise, 2009, pp. 3-4) and issued the *Framework for Preparation and Presentation of Financial Statements* (Wingard, Von Well, Pretorius, Ferreira, Badenhorst, & Van der Merwe, 2011, p. 1).

In 2001, the International Accounting Standards Board (IASB) was established as part of the IASC Foundation, with the following objectives:

- (a) *to develop, in the public interest, a single set of high quality, understandable and enforceable global accounting standards that require high quality, transparent and comparable information in financial statements and other financial reporting to help participants in the world's capital markets and other users make economic decisions;*
- (b) *to promote the use and rigorous application of those standards;*
- (c) *in fulfilling the objectives associated with (a) and (b), to take account of, as appropriate, the special needs of small and medium-sized entities and emerging economies; and*
- (d) *to bring about convergence of national accounting standards and International Accounting Standards and International Financial Reporting Standards to high quality solutions. (Own emphasis.) (IASB, 2011, p. A8)*

The collapse of American energy giant, Enron, in 2001 and the resulting demise of one of the big five accounting firms in the world, Arthur Andersen, brought about a mind-shift in international role players in the accounting profession. The ripple-effects of the downfall of what was once one of the world's ten most valuable companies, started the push for international accounting and auditing standards to replace the patchwork of country-by-country guidelines that existed until then (Pfanner, 2002, p. 1; Buckstein, 2008, p. 1). Due to the reality of globalisation (Lubbe, Modack, & Watson, 2011, p. 6)

and the pressure among international role players to harmonise accounting standards, the International Accounting Standards Board (IASB) has been tasked with the development and issuing of International Financial Reporting Standards (IFRSs, with Interpretations) as well as related documents such as the *Framework for Preparation and Presentation of Financial Statements*, exposure drafts and discussion documents.

During 2003, the APB decided to harmonise SA GAAP with IFRS. IFRSs set out the requirements for recognition, measurement, presentation and disclosure for general purpose financial statements and other reporting of all profit-oriented entities (International Accounting Standards Board, 2009; Lubbe, Modack, & Watson, 2011, pp. 7-8).

International Financial Reporting Standards are mainly aimed at the reporting needs of large entities and have cumbersome recognition, measurement and disclosure requirements. IFRSs are directed to the general financial information needs of a very wide range of users, for example, creditors, shareholders, employees and the public at large (IASB, 2009, p. 7). As a result, complying with the requirements of “full” IFRS places an enormous burden on small and medium-sized entities (SMEs). In a 2011 CIMA technical update, Fernando (2011) argues that implementing full IFRS requires lots of management time, staff training, and specialist consultations to ensure full compliance. This burden is too heavy for most SMEs to bear. (See also SAICA (2010, p. i).) Van Wyk and Rossouw (2009, pp. 99-101) share the opinion. They mention that applying full IFRS do not result in useful and cost-effective information being provided to the users of the financial statements of SMEs, irrespective of their legal form. They argue that these users do not need all the detailed and complex information provided by general purpose financial statements. (See also Steinbank (2008, pp. 1-3).)

Paul Pactor, Director of Standards for SMEs of the IASB, states that in many countries, this complexity has been pushed down to SMEs due to harmonisation of local accounting standards with IFRS and South Africa was no exception to the rule. After South African GAAP became fully convergent with IFRS, many SMEs were struggling to comply with those standards (SAICA, 2010, p. i). The IASB recognised the need for a separate standard applicable to the needs of SMEs that often produce financial statements only for the use of owner-managers or tax authorities, and do not necessarily constitute general purpose financial statements. Consequently, the IASB developed and published International Financial Reporting Standards for Small and Medium-sized Entities (IFRS for SMEs). In 2007, South Africa became the first country to adopt IFRS for SMEs while it was still in its exposure draft form (Van Wyk & Rossouw, 2009, p. 100; Stainbank, 2008, p. 2).

The IFRS for SMEs, as issued by the IASB in July 2009, consists of 230 pages and is less than 10% in volume of full IFRS. It is also less complex than full IFRS in a number of ways. For instance, it requires roughly 300 disclosures, compared to the 3000 disclosures required by IFRS, and where full IFRS allows accounting policy choices, IFRS for SMEs allow only the easier option (IASB, 2012, p. 4).

Despite the fact that the APB issued IFRS for SMEs, which was simpler than full IFRS, there still existed a demand for a simpler framework for micro entities, as it was believed by some that IFRS for SMEs was too complex for micro entities (SAICA, 2012). In 2009, Van Wyk and Rossouw published an article (p. 113) in which they argue that IFRS for SMEs follow a “one-size-fits-all” principle and does not distinguish between micro, small and medium-sized entities. Their research also revealed that despite the good intentions of the IFRS for SMEs, there is scepticism among accounting practitioners about whether the standard actually reduces the burden of financial reporting for SMEs.

Since 2008, SAICA has investigated the development of a Framework for Non-Public Entities (FfNPE) or a so-called Micro GAAP or third tier financial reporting framework as a consequence of member requests to do so. The Micro GAAP working group was formed in 2008 and embarked on a project to develop the FfNPE. The Micro GAAP working group has since its formation issued three exposure drafts, namely ED 257, ED 275 and ED 285, for public comment. After extensive deliberations by the Accounting Practices Committee, the Accounting Practices Board and the Financial Reporting Standards Council, a decision has been made by SAICA not to proceed with the issuing of the proposed FfNPE, either as a standard or a SAICA guide.

As a result, SA GAAP will be withdrawn and cease to apply in respect of financial years commencing on or after 1 December 2012. Because of these decisions, all companies still applying SA GAAP will have to convert to IFRS or IFRS for SMEs. However, the withdrawal of SA GAAP is not only applicable to companies, but also to entities other than companies. In their announcement, the APB and Financial Reporting Standards Council (FRSC) also indicated that other entities that are required to apply SA GAAP in terms of their governing legislation should follow the process of conversion to either full IFRS or IFRS for SMEs (SAICA, 2012).

The research done among accounting practitioners by Van Wyk and Rossouw mentioned above, indicated that IFRS for SMEs is not deemed to be relevant to smaller and micro-entities in South Africa (2009, p. 113). After the subsequent withdrawal of SA GAAP and Micro GAAP efforts, this problem will still persist.

The South African Institute of Chartered Accountants (SAICA), in response to the requests from the accounting profession servicing the SME market and micro entities across South Africa for guidance that will simplify and reduce the cost to prepare financial statements for micro entities, has developed a guide for applying the

International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs) to a micro entity (SAICA, 2012, p. 1). On their website SAICA stated the following:

“This guide is in the form of an easy-to-use electronic toolkit that comprises a user checklist, an application guide with practical examples, illustrative financial statements, and a disclosure checklist. The guide is aimed primarily at assisting micro entities such as close corporations and companies with a public interest score (as determined by the Companies Act) below 100 points, partnerships and sole-proprietorships, with the practical application of the IFRS for SMEs standard. The guide may also be useful for entities with a public interest score between 100 and 350 points.” (Own emphasis.)

At the time of completion of the study, this guide was still very new and untested in practice. Furthermore, as announced by SAICA, the aim of the guide is to assist small companies, CCs, partnerships and sole-proprietors in applying IFRS for SMEs to their particular environments. They did not mention that it is specifically applicable to the sectional title industry. Closer inspection revealed that the guide included chapters on topics such as business combinations and goodwill, investments in associates and joint ventures, consolidated financial statements and intangible assets - which is not applicable to sectional titles. Therefore, a more in-depth discussion on the applicability of the SAICA guide to sectional title financial reporting fell outside the scope of this study.

The problem of the recent change in wording in the accounting standards internationally is also of particular importance to the governing legislation of the sectional title industry in South Africa. The term “generally accepted accounting practice”, used in the Sectional Titles Act, may possibly in future have to be interpreted as either full IFRS or IFRS for SMEs. A big problem in the sectional title industry is the fact that many users of financial statements of bodies corporate have little to no knowledge of accounting

and finance. This makes even a seemingly “simplified” framework such as IFRS for SMEs too complicated and cumbersome for the industry in general. Riddin (2010, p. 1; 2009, pp. 1-2) further states that there are various aspects in IFRS for SMEs that is not applicable to the sectional title industry and may require deviation from the framework. These challenges will be addressed in the sections below.

4.3. DEFINITIONS, ANALYSIS OF THE ACT AND EMPIRICAL FINDINGS APPLICABLE TO ACCOUNTING

4.3.1. INTRODUCTION

In 4.2. above it was mentioned that the concept of accounting was developed over hundreds of years and that financial reporting standards help to ensure the consistent application and treatment of financial transactions and assists in comparability and continuity in financial statements.

In Chapter 2, mention was made of various aspects in the Sectional Titles Act which refers to the concept of accounting. Reference was also made to the fact that there are various shortcomings, weaknesses and unclear aspects in the wording of the Act. These will be discusses in more detail in this section.

This section will firstly give the definitions of various terms used throughout this chapter as it appears in the IASB’s *A Guide through IFRS 2011*. Secondly, the sections and rules in the Sectional Titles Act which deals with accounting will be analysed, and the details of the results of the empirical findings will be discussed.

The sample selection for the quantitative empirical study was discussed in detail as part of the section on research methodology in 1.6.5. of Chapter 1 and briefly in 4.1 of this chapter.

In various discussions of the legal requirements in the Chapter, it is mentioned that there is vagueness or ambiguity in a specific piece of legislation; the legislation contains wording that is not true to the acknowledged subject terminology of, for example, IFRS, and parts of the legislation make use of outdated terminology. As background to this section it is stated that the aforementioned are probably classic examples of situations where, firstly, the legislator is not acquainted with the subject-specific and technical terminology and secondly, the wording of the legislation is not amended on a regular basis and therefore, does not keep up with developments and new generally accepted subject-specific terminology. In such cases the reader of the specific sections will probably have to resort to the principles of the discipline of statutory interpretation – which may be too much to ask of a person with no legal background.

4.3.1.1. GENERAL DEFINITIONS

Gordon (1992, p. 12) defines **Generally Accepted Accounting Principles (GAAP)** as those principles that have substantial authoritative support, supported by pronouncements by recognised accounting bodies and commonly followed by business practices. As mentioned in 4.2. above, however, SA GAAP has effectively been withdrawn by the APB and the FRSC and will cease to apply in respect of financial years commencing on or after 1 December 2012.

International Financial Reporting Standards (IFRSs) set out recognition, measurement, presentation and disclosure requirements dealing with transactions and events that are important in general purpose financial statements. They may also set

out such requirements for transactions and events that arise mainly in specific industries (IASB, 2011, p. A9).

General purpose financial statements (IASB, 2009, pp. 6-7) are directed towards the common information needs of a wide range of users, for example, shareholders, creditors, employees and the public at large. The objective thereof is to provide information about the financial position, performance and cash flow of an entity that is useful to those users when they make economic decisions.

General purpose financial statements (IASB, 2011, p. A556), referred to as **financial statements**, are those intended to meet the needs of users who are not in a position to require an entity to prepare reports tailor to the particular information needs.

The term **financial reporting** encompasses general purpose financial statements plus other financial reporting (IASB, 2009, p. 6).

The IASB also develops and publishes (IASB, 2009, p. 7) a separate standard intended to apply to the general purpose financial statements of, and other financial reporting by entities referred to as small and medium-sized entities (SMEs). These standards are called **International Financial Reporting Standards for Small and Medium-sized Entities (IFRS for SMEs)**.

The IASB (2009, p. 10) defines **small and medium-sized entities (SMEs)** as entities that do not have public accountability and publish general financial statements for external users.

4.3.2. PUBLIC ACCOUNTABILITY

As mentioned above as well as in section 1.4. of Chapter 1, an entity can be classified as an SME if it does not have public accountability and publishes general financial statements for external users. The IASB states (2009, p. 10) that an entity has **public accountability** if:

- a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in the public market, or
- b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. This is typically the case for banks, credit unions, insurance companies, securities brokers, etc.

This immediately brings to mind the question as to whether a body corporate does not perhaps have public accountability, and therefore cannot be classified as an SME. After all, a body corporate collects money in the form of levies on behalf of a group of members.

The IASB, however, gives clear guidance with regards to this. They state that some entities hold and manage financial resources entrusted to them by clients, customers or members not involved in the management of the entity, but if they do so for reasons incidental to a primary business, that does not make them publicly accountable. Here the IASB refers to entities such as schools, real estate agents, travel agents and charitable organisations to name but a few.

In section 2.2.1. of Chapter 2 the functions and powers of bodies corporate was discussed. As mentioned in that section, the main functions of a body corporate include, amongst others, maintenance of the common property, insurance of the

property, holding of meetings, etc. (See also Paddock (2008, pp. 1-4).) Therefore, even though a body corporate hold and manage financial resources (in the form of levies) entrusted to them by the members of the body corporate (who are not involved in the management thereof), it does so for reasons incidental to its “primary business”. It can be concluded that a body corporate does not have public accountability and can be classified as an SME for financial reporting purposes.

In section 1.4. of Chapter 1 and 4.2. above, the question was posed as to whether IFRS for SMEs is really an appropriate framework to use for the sectional title industry. This issue will be addressed in the sections that follow.

4.3.3. ACCOUNTING OFFICER

The first aspect regarding accounting that is mentioned in the Sectional Titles Act is section 2 which deals with “Interpretation”. Section 2(c) states the following:

*“**accounting officer**’ means a person who in terms of section 60 (2) of the Close Corporation Act, 1984 (Act 69 of 1984), is qualified to perform the duties of an accounting officer” (Own emphasis.)*

The concept of “accounting officer” was extensively dealt with in sections 3.3.7.3.1. and 3.3.7.3.2. of Chapter 3. For the sample of body corporate annual financial statements selected and analysed, the findings was that the Sectional Titles Act and resultant reference to the Close Corporations Act defining the concept of “accounting officer” was correctly interpreted.

4.3.4. BOOKS OF ACCOUNT AND RECORDS

Section 35 of the Sectional Titles Act deals with “books of account and records”. The wording in the Act is as follows:

*“(1) The trustees shall cause **proper books of account and records** to be kept so as **fairly to explain** the **transactions and financial position** of the body corporate, including-*

*(a) a **record of the assets and liabilities** of the body corporate;*

*(b) a record of all **sums of money received and expended** by the body corporate and the matters in respect of which such receipt and expenditure occur;*

*(c) a **register of owners and of registered mortgagees** of units and of all other persons having real rights in such units (insofar as written notice shall have been given to the trustee by such owners, mortgagees or other persons) showing in each case their **addresses**; and*

*(d) **individual ledger accounts** in respect of each **owner**.” (Own emphasis.)*

Each of the emphasised terms will be dealt with below.

4.3.4.1. PROPER BOOKS OF ACCOUNT AND RECORDS

The Act requires trustees to cause proper books of account and records to be kept. The Act does not state that the trustees should do this themselves; they should, however, ensure that it is properly kept. The reality is that, in practice, very few trustees have the skills, knowledge and/or time to keep proper books of accounts and records.

In order to gain an understanding as to who is responsible for keeping books of accounts and records, a sample of 60 sets of financial statements of bodies corporate over a period of two years were analysed, firstly, amongst others, to determine who prepared the financial statements.

For the 2009 financial year 57 of the 60 bodies corporate used the services of a firm of Chartered Accountants to prepare the financial statements, while 3 made use of the services of an Accounting Officer. For the 2010 financial year 58 of the 60 bodies corporate used the services of a firm of Chartered Accountants to prepare the financial statements, and 2 made use of the services of an Accounting Officer. Therefore, none of the trustees of the bodies corporate from the sample opted to prepare the financial statements themselves.

For the above-mentioned sample of 60 sets of financial statements of bodies corporate over a period of two years, a formal enquiry was made to the managing agent as to who is responsible for keeping accounting records. According to the managing agent, the keeping of books of account and records were a joint effort between the managing agent and the accountants chosen by the trustees, but the greatest part of the work was done by the managing agent. The managing agent used the PropAcc accounting system and the Pastel accounting system for managing their trust accounts, preparing levy rolls, doing billing and invoicing, processing creditor payments, preparing general ledger reports, etc. The accounting firms in the sample used Pastel accounting to do additional processing of journal entries and in some cases month-end procedures. In none of the cases did the trustees keep accounting books or records.

It is important to note that this observation may not be representative of the entire population of bodies corporate, as the sample was obtained directly from a managing

agent. Therefore it is possible that there may be instances where trustees keep their own books of account and records.

4.3.4.2. FAIRLY TO EXPLAIN THE TRANSACTIONS AND FINANCIAL POSITION

The second section regarding bookkeeping that requires further investigation is the wording which states the following:

*“(1) The trustees shall cause proper books of account and records to be kept so as **fairly to explain the transactions and financial position** of the body corporate...”* (Own emphasis.)

The Oxford online dictionary describes the word “fairly” as “*to a moderate or high degree*” and “fair” as “*considerable though not outstanding in size or amount*”. It is interesting to note that the Act does not require the explanation to be accurate, complete or precise, only fair.

The terms “*transactions*” and “*financial position*” as used in the Sectional Titles Act are not defined as such in either IFRS or IFRS for SMEs. The term “transactions” is used in IFRS in the following instances: referring to share-based payment transactions in IFRS 2, related party transactions in IAS 24, transaction costs related to acquisition or issue of a financial asset in IFRS 9, significant events and transactions in interim financial reporting as per IAS 34 and non-monetary transactions in IAS 16, 38 and 40. The most applicable description of the term “*transactions*” is probably contained in the current Conceptual Framework (IASB, 2011, pp. A32-A33) which states the following:

“In order to meet their objectives, financial statements are prepared on the accrual basis of accounting. Accrual accounting depicts the effects of

transactions and other events and circumstances on a reporting entity's economic resources and claims in the periods in which those effects occur, even if the resulting cash receipts and payments occur in a different period. This is important because information about a reporting entity's economic resources and claims and changes in its economic resources and claims during a period provides a better basis for assessing the entity's past and future performance than information solely about cash receipts and payments during that period." (Own emphasis.) (See also Lubbe, Modack and Watson (2011, p. 31).)

In IFRS the term "*financial position*" is usually used in the context of the financial statements, more specifically the statement of financial position. The Conceptual Framework (IASB, 2011, p. A32) states the following under the heading "*The elements of financial statements*":

"Financial statements portray the effects of transactions and other events by grouping them into broad classes according to their economic characteristics. These broad classes are termed the elements of financial statements. The elements directly related to the measurement of financial position are assets, liabilities and equity..." (Own emphasis.)

From the above the conclusion can be drawn that, according to the Conceptual Framework, the transactions are part of the "building blocks" which will eventually be taken up in the financial statements and that the financial position of an entity as portrayed by the financial statements is only a piece of the final puzzle which is the annual financial statements.

From an accounting perspective the question then arises as to whether the "*books of account and records*" can "*fairly explain*" the "*transactions and financial position*" of the body corporate. To answer this question one should perhaps investigate the accounting

cycle. The normal accounting cycle in a business consists of a few basic steps which occur in the information environment of the entity (Hall, 2013, pp. 4-13). It usually starts with transactions and source documents which are then entered into journals. The journals are posted to the ledger control accounts from which a trial balance can be produced. After doing adjusting period-end entries, the trial balance is then used to prepare financial statements in the form of a statement of profit or loss and other comprehensive income (income statement), statement of financial position (balance sheet), cash flow statement and notes. The final part of the cycle is the analysis and interpretation of the financial statements (Simkin, Rose, & Norman, 2013, p. 12; Kew & Watson, 2012, pp. 82-87).

From the above it is evident that there are quite a few steps that have to be completed between the *“transactions”*, source documents and journals (*“books of account and records”*) and the actual financial statements (*“financial position”*). The *“books of account and records”* can perhaps *“explain”* the transactions of a body corporate to a certain extent. However, only after various additional processing steps and then through analysing and interpreting the annual financial statements can the financial position of the entity be explained.

The wording of the Act in this instance is unclear and can lead to some confusion. Perhaps a more appropriate wording would simply be to state: *“The trustees shall cause proper books of account and records to be kept”* without adding the additional detail. The requirements of the Act regarding what should be included in the books of account and records will be discussed in the sections below.

4.3.4.3. RECORD OF THE ASSETS AND LIABILITIES

Section 35(1)(a) of the Act states that the books of account and records should include “*a record of the assets and liabilities of the body corporate*”. (Own emphasis.) The term “*record of assets and liabilities*” is not a formally acknowledged term in accounting literature. The Act does not give any further clarification as to what exactly is meant by a record of assets and liabilities. A number of questions can be asked regarding this requirement, for instance: are journals or ledger accounts considered to be sufficient record of assets and liabilities; does it perhaps imply something like a fixed asset register; what level of detail is required, etc.

Taking all of these questions as well as the detail of a normal accounting cycle into account it can perhaps be argued that this sentence in the requirement is superfluous. The reason for this is because the books of account and records of a business, being the journals and ledgers, contain all the detail of all transactions and then by default also the detail (“*record*”) of the assets and liabilities (Kew & Watson, 2012, pp. 82-83). This means that if the accounting is done and the books are properly kept according to the accounting cycle, a record of all assets and liabilities will in any event be contained in the financial records of the entity. Furthermore, most modern accounting packages, including PropAcc and Pastel Accounting, which is widely used by role players in the sectional title industry, have add-on modules and built-in functionality to produce management information from the database in the form of reports.

Regarding the sample of 60 sets of annual financial statements of bodies corporate over a period of two years, a formal enquiry was made to the managing agent as to who is responsible for keeping accounting records, more specifically, a record of assets and liabilities. According to the managing agent, the keeping of these records are done by them and it is an integrated part of the Pastel Accounting software used. In none of the cases did the trustees keep accounting books or records. It is important to note that this

observation may not be representative of the entire population of bodies corporate, as the sample was obtained directly from a managing agent. It is, therefore, possible that there may be instances where trustees keep their own records of assets and liabilities.

The same argument, therefore, holds true as in the previous section. Maybe the Act should just state: *“The trustees shall cause proper books of account and records to be kept”* without alluding to detail such as records of assets and liabilities.

4.3.4.4. SUMS OF MONEY RECEIVED AND EXPENDED

Section 35(1)(b) of the Act states that the books of account and records should include *“a record of all sums of money received and expended by the body corporate and the matters in respect of which such receipt and expenditure occur.”* (Own emphasis.) As in the previous section there is once again an argument for the wording to be superfluous. Records of sums of money received and expended is evidenced and summarised in various forms in the business in the form of source documents, which is the first step in the accounting cycle. Examples of these include, amongst others, deposit slips, receipts issued and received, debtors’ statements, creditors’ statements and bank statements. These source documents are then recorded in the accounting system in the form of journals (or cash book(s)) and ledger accounts. If proper accounting is done, there will usually also be regular bank reconciliations performed (Kew & Watson, 2012, pp. 258-274). All of these add up to provide proper records of the money received and expended, and includes detail such as who the money was paid to, when it was paid, amounts paid, etc.

Regarding the sample of 60 sets of annual financial statements of bodies corporate over a period of two years, a formal enquiry was made to the managing agent as to who is responsible for keeping accounting records, more specifically, sums of money received

and expended. According to the managing agent the keeping of these records are done by them and it is integrated in the PropAcc and Pastel accounting software in use. In none of the cases did the trustees keep accounting books or records. It is important to note that this observation may not be representative of the entire population of bodies corporate, as the sample was obtained directly from a managing agent. Therefore it is possible that there may be instances where trustees keep their own record of sums of money received and expended.

One can reason that perhaps the Act should just state: *“The trustees shall cause proper books of account and records to be kept”* without alluding to detail such as sums of money received and expended.

4.3.4.5. REGISTER OF OWNERS AND OF REGISTERED MORTGAGEES SHOWING THEIR ADDRESSES

A third requirement of Section 35(1) is subsection (c) which states that, as part of the books of account and records the following should be kept:

*“a **register of owners and of registered mortgagees** of units and of all other persons having real rights in such units (insofar as written notice shall have been given to the trustee by such owners, mortgagees or other persons) showing in each case their **addresses**”* (Own emphasis.)

Regarding the sample of 60 sets of annual financial statements of bodies corporate over a period of two years, a formal enquiry was made to the managing agent as to who is responsible for keeping accounting records, more specifically, a register of owners and registered mortgagees. According to the managing agent, the keeping of these records are done by them and it is part of the accounting software packages that they use. In

none of the cases did the trustees keep these registers. It is important to note that this observation may not be representative of the entire population of bodies corporate, as the sample was obtained directly from a managing agent. Therefore it is possible that there may be instances where trustees keep their own register of owners and of registered mortgagees.

4.3.4.6. INDIVIDUAL LEDGER ACCOUNTS REQUIRED IN RESPECT OF EACH OWNER

The final requirement regarding the books of account and records is stated in Section 35(1)(d) which requires the trustees to keep “*individual ledger accounts in respect of each owner.*” (Own emphasis.)

Again, as in the previous sections one can argue that the wording might be superfluous. If proper accounting is done, a trade receivables subsidiary ledger will usually be created to keep an independent account of all transactions with each debtor in an individual account (Kew & Watson, 2012, pp. 327-328). One of the features of accounting software packages such as PropAcc and Pastel accounting is also that individual ledger accounts are kept for all debtors.

With regards to the sample of 60 sets of annual financial statements of bodies corporate over a period of two years, a formal enquiry was made to the managing agent as to whether individual ledger accounts are kept in respect of each owner. According to the managing agent the keeping of these records are done by them, and it is integrated into the PropAcc and Pastel Accounting software in use. They also keep individual ledger accounts for all tenants. In none of the cases did the trustees keep individual ledger accounts for owners. It is important to note that this observation may not be representative of the entire population of bodies corporate, as the sample was obtained

directly from a managing agent. Therefore it is possible that there may be instances where trustees keep their own individual ledger accounts in respect of each owner.

One can therefore reason that perhaps the Act should just state: *“The trustees shall cause proper books of account and records to be kept”* without alluding to detail such as individual ledger accounts.

4.3.5. FINANCIAL STATEMENTS

In Section 37(1) of the Act the concept of the “Annual Financial Statement” is discussed in the following wording:

“The trustees shall cause to be prepared, and shall lay before every annual general meeting, for consideration in terms of rule 56(a), a financial statement in conformity with generally accepted accounting practice, which statement shall fairly present the state of affairs of the body corporate and its finances and transactions as at the end of the financial year concerned”. (Own emphasis.)

Subsection 2 of Section 37 prescribes the detail of further information to be contained in the annual financial statements of a sectional title scheme:

“(2) The financial statement shall include information and notes pertaining to the proper financial management by the body corporate, including:

(a) the age analysis of debts in respect of levies, special levies and other contributions;

(b) the age analysis of amounts owing by the body corporate to the creditors and in particular to any public or local authority in respect of rates

and taxes and charges for consumption or services, including but not limited to, water, electricity, gas, sewerage and refuse removal;

*(c) the **expiry dates of all insurance policies.***” (Own emphasis.)

According to Riddin (2011, p. 1) the aspects mentioned in subsection (2) are often overlooked by auditors or accounting practitioners when drafting the financial statements. The sections mentioned above will be further discussed below.

4.3.5.1. RESPONSIBILITY OF TRUSTEES

The Act requires the trustees to cause financial statements to be prepared. The Act does not state that the trustees should prepare these themselves; they should, however, ensure that it is prepared. The reality is that, in practice, very few trustees have the skills and knowledge to prepare financial statements. Riddin (2011, p. 1) says that, because the trustees are ultimately responsible for the preparation of the financial statements, they cannot hold the managing agent or even the auditor or accounting officer responsible for any failure or defect with the financial statements.

For the sample of 60 sets of financial statements of bodies corporate over a period of two years, the actual financial statements were analysed. For the 2009 financial year 57 of the 60 bodies corporate used the services of a firm of Chartered Accountants to prepare the financial statements, while 3 made use of the services of an Accounting Officer. For the 2010 financial year 58 of the 60 bodies corporate used the services of a firm of Chartered Accountants to prepare the financial statements, and 2 made use of the services of an Accounting Officer. Therefore, none of the trustees of the bodies corporate opted to prepare the financial statements themselves.

4.3.5.2. LAY BEFORE EVERY ANNUAL GENERAL MEETING FOR CONSIDERATION IN TERMS OF RULE 56(A)

As mentioned in section 2.2.3. of Chapter 2, the annual general meeting (AGM) must be held within four months after the end of each financial year. Written notice of at least fourteen days must be given to all the owners and the notice must be accompanied by a number of supporting documents to be discussed at the meeting, including the annual financial statements.

The fact that the audited annual financial statements should effectively be available three and a half months after the financial year end of a body corporate creates some problems in practice. Prescribed Management Rule 51(2) holds as follows:

“Unless otherwise decided at a general meeting or by the trustees, the financial year of the body corporate shall run from the first day of March in each year to the least day of February in the following year.”

As a result, many bodies corporate have February financial year-ends. This is usually a very busy time for accounting practitioners and, as the fiscal year-end of the government is also 28 February, bottle-neck situations sometimes occur. It also sometimes happens that the financial statements are not available for consideration at the AGM. In such cases the AGM is often postponed or the AGM continues without consideration of the annual financial statements. A possible solution that has been suggested by some authors (Constas & Bleijs, 2009, pp. 74, 100; Riddin, 2011, p. 1) is to change the financial year end of the body corporate. The problem regarding financial year ends of bodies corporate will be further alluded to in the discussion of the empirical results in Chapter 5.

The wording of Section 37(1) and PMR 56(a) is of importance. The Act states that the business transacted at the AGM should include *“the consideration of the financial*

statement and report". (Own emphasis.) The Act requires that the financial statements are "*considered*"; it does not require that it should be "*approved*", as is the case with the schedules of replacement values and the budget. The Oxford online dictionary describes the word "consider" as to "*think carefully about something, typically before making a decision*". The word "consideration" is described as "*careful thought, typically over a period of time*" and "*a fact or motive taken into account in deciding something*".

In practice, this specific rule is sometimes misinterpreted. During the course of the study some cases were noted where minutes of AGMs had a point on "approval of the financial statements". This is further evidenced by a discussion forum on the website of Sectional Titles Online, where one user stated that: "*...I am of the opinion that the Financial Statements should be discussed during the AGM in order for the Body Corporate to approve the Statements...*" (Own emphasis.) Yet another user commented: "*...I agree with the other two replies saying that the audited financial statements must be considered and approved at the AGM...*" (Own emphasis.)

Despite the wording of the Act mentioning that the financial statements should only be considered, the "incorrect" interpretation thereof is not necessarily wrong. In terms of good meeting procedure and principles of good corporate governance (see also section 1.3 in Chapter 1), certain material matters must be approved at an entity's annual general meeting. An example is the Companies Act, No. 71 of 2008 which states in Section 30(3)(c): "*The annual financial statements must... be approved by the board and signed by an authorised director...*" (SAICA, 2010, pp. ss29-31). (Own emphasis.) The same holds true for Section 58(3) of the Close Corporations Act 69 of 1984 which states: "*The annual financial statements shall be approved and signed by or on behalf of a member holding a member's interest of at least 51%, or members together holding members' interests of at least 51%, in the corporation...*" (SAICA, 2010, pp. ss58-62). (Own emphasis.) The mere consideration of the financial statements by the members of

the body corporate may not necessarily be sufficient to ensure the application of the principles of good corporate governance.

4.3.5.3. FINANCIAL STATEMENTS IN CONFORMITY WITH GENERALLY ACCEPTED ACCOUNTING PRACTICE

Section 37(1) requires the trustees to prepare “*a financial statement in conformity with generally accepted accounting practice*”. (Own emphasis.)

International Accounting Standard (IAS) 1 sets overall requirements for the presentation of financial statements as well as guidelines for their structure and minimum requirements for their content (IASB, 2011, p. A552). The newly revised IAS 1 brought about several changes regarding the wording used in financial statements. Previously IAS 1 used the titles “balance sheet”, “income statement” and “cash flow statement”. In order to better reflect the functions of the statements the titles were changed to “statement of financial position”, “statement of profit or loss and other comprehensive income” and “statement of cash flows” respectively. Significant changes also took place with regards to the statement of changes in equity in order to provide more useful information and group similar items together. As a result, an entity is no longer permitted to present components of comprehensive income (non-owner changes in equity) in the statement of changes in equity (IASB, 2011, pp. A553-A554).

According to “*A guide through IFRS*” (IASB, 2011, p. A559) a complete set of financial statements comprises of the following:

“(a) a **statement of financial position** as at the end of the period;

(b) a **statement of profit and loss and other comprehensive income** for the period;

(c) a **statement of changes in equity** for the period;

(d) a **statement of cash flows** for the period;

(e) **notes**, comprising a summary of significant **accounting policies** and other **explanatory information**; and

(f) a statement of financial position as at the beginning of the earliest comparative period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements.” (Own emphasis.)

For the sample of 60 sets of financial statements of bodies corporate over a period of two years, the annual financial statements were analysed. For the 2009 financial year, all 60 of the financial statements included only a “balance sheet”, an “income statement” and notes. None of the 2009 financial statements analysed included a statement of changes in equity or a cash flow statement, and all of the financial statements still contained the “old” wording.

For the 2010 financial year, 58 sets of financial statements included only a “balance sheet”, an “income statement” and notes. One set of financial statements included an “income statement”, a “balance sheet”, a statement of changes in equity, a “cash flow statement” and notes. One set of financial statements included only a “statement of financial position”, a “statement of comprehensive income” and notes. In other words, for 2010, 59 annual financial statements that were analysed did not contain a statement of changes in equity, nor did it contain a cash flow statement. As many as 59 of the financial statements still used the “old” wording.

During the interviews with the accounting practitioners (further discussed in Chapter 5), they revealed that they found it unnecessary and not cost effective to present a

statement of cash flows. According to all of them they did not feel that it added any additional value, and from past experience they realised that the inclusion thereof tend to confuse the users of the financial statements of bodies corporate. Furthermore, they stated that the use of the old wording was due to their accounting software packages (Pastel Accounting, Caseware and Quickbooks) was set up with the “old” wording and that the users of body corporate financial statements felt comfortable with the “old”, more widely-known wording.

Section 37(1) requires the financial statements prepared by the trustees to be “***in conformity with generally accepted accounting practice***”. (Own emphasis)

As mentioned in section 4.2. above, SA GAAP will be withdrawn and cease to apply in respect of financial years commencing on or after 1 December 2012. The withdrawal of SA GAAP will not only have an effect on companies, but also to entities other than companies, such as non-profit organisations, partnerships, sectional title schemes, etc. In their announcement, the APB and Financial Reporting Standards Council (FRSC) also indicated that other entities that are required to apply SA GAAP in terms of their governing legislation should follow the process of conversion to either full IFRS or IFRS for SMEs (SAICA, 2012). SAICA’s recently developed a guide on application of IFRS for SMEs to micro entities attempts to assist small companies, CCs, partnerships and sole-proprietors with applying IFRS for SMEs to their particular environments. It was not specifically developed for the sectional title industry and the applicability thereof to the sectional title industry was not yet tested as the product was launched late in 2012. However, that does not change the fact that full IFRS and IFRS for SMEs are the only two formally acknowledged sets of accounting standards currently in use.

Regarding repeal of legislation, Botha (2005, pp. 39-44), in his book on statutory interpretation, specifically refers to Section 12 of the Interpretation Act. Section 12 of the Interpretation Act 33 of 1957 states that:

“(1) Where a law repeals and re-enacts with or without modifications, any provision of a former law, references in any other law to the provision so repealed shall, unless the contrary intention appears, be construed as references to the provision so re-enacted.”

Taking the SAICA announcement and the principles of statutory interpretation into account, this means that, as from 1 December 2012, the sentence *“in conformity with generally accepted accounting practice”* in the Sectional Titles Act will have to be interpreted as either IFRS or IFRS for SMEs.

Riddin (2010, p. 1; 2009, pp. 1-2) shares the views of Van Wyk and Rossouw (2009, pp. 99-101) that full IFRS compliance is very onerous and costly and that applying full IFRS do not result in useful and cost-effective information being provided to the users of the financial statements of SMEs. As a sectional title accounting specialist, Riddin is of the opinion that between IFRS and IFRS for SMES, IFRS for SMEs is the “best fit” of the two for sectional title. He emphasises that good governance and reporting is very important and that compliance with a high quality reporting standard is necessary. He, however, feels that when doing accounting for sectional titles, there is a need to deviate from IFRS for SMEs, due to the fact that some accounting aspects are not applicable. He also mentions further that it may be necessary in future to revisit the needs of users of sectional title financial information in order to adopt a more meaningful reporting standard that is appropriate and useful. He proposes a reporting standard giving specific consideration to aspects such as compliance with rules, compliance with Sectional Titles Act restrictions, proper determination of levies and a different treatment of body corporate assets, to name but a few.

The fact that sectional titles have unique financial reporting requirements is not unique to South Africa. In the province of Ontario in Canada “sectional title” property is governed by the *Ontario Condominium Act, 1998*. In November 2001, the Institute of Chartered Accountants of Ontario issued a booklet called “*Accounting and Auditing Guidelines for Ontario Condominium Corporations*”. The guidelines were updated in 2008 by the CA profession’s *Committee on Accounting and Auditing for Condominium Corporations*. This comprehensive guide promotes best practices for the industry, detailing, amongst others, suggested financial statement formats, considerations for accounting and audits, tax issues and budgeting. Committee Chair, Steven Chesney, CA, stated that the adoption of the suggested financial statement formats by condominium corporations will help bring uniformity to financial reporting and possibly increase the public’s ability to access, understand and better use the available financial information. The publication is not an official announcement by the Institute, but presents the collective views of members of the task force.

Perhaps the accounting profession in South Africa should consider following the example of the Institute of Chartered Accountants in Ontario. The aspect of a possible tailor-made accounting standard for sectional titles were also addressed as part of the empirical study the results of which are discussed in detail in Chapter 5.

4.3.5.4. FAIRLY PRESENT THE STATE OF AFFAIRS, FINANCES AND TRANSACTIONS

Section 37(1) of the Sectional Titles Act states that the financial statements, as prepared by the trustees “*shall **fairly present the state of affairs** of the body corporate and its **finances and transactions** as at the end of the financial year concerned*”. (Own emphasis.)

As mentioned earlier in this chapter, as well as in Chapter 3, the accounting profession has very specific guidelines and standards which are issued by the International Accounting Standards Board (IASB). The problem with the words “*state of affairs*”, “*finances*” and “*transactions*” as stated in the Sectional Titles Act is that it does not form part of the acknowledged accounting terminology in IAS 1. These terms are very broad and can be interpreted in a number of ways.

IAS 1 (IASB, 2011, p. A561) states the following in paragraph 15:

“Financial statements shall present fairly the financial position, financial performance and cash flows of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions, and recognition criteria for assets, liabilities, income and expenses set out in the Framework. The application of IFRSs, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation.” (Own emphasis.)

A possible solution for the problem of the broad terminology used in Section 37(1) of the Act is to turn to the principles of statutory interpretation. In his book on statutory interpretation Botha (2005, p. 69) makes a very important comment when he states that where one encounters technical legislation applicable to specific trades, industries or professions, the wording of that legislation should be interpreted in its specialised, technical context.

Therefore the words “*state of affairs*”, “*finances*” and “*transactions*” as stated in the Sectional Titles Act should perhaps rather be read as “*financial position*”, “*financial performance*” and “*cash flows*”.

4.3.5.5. INFORMATION AND NOTES PERTAINING TO THE PROPER FINANCIAL MANAGEMENT

As part of Subsection 2 of Section 37 the Act prescribes the detail of further information to be contained in the annual financial statements of a sectional title scheme:

*“(2) The financial statement shall include **information and notes** pertaining to the **proper financial management** by the body corporate, including:*

*(a) the **age analysis of debts** in respect of **levies, special levies and other contributions**;*

*(b) the **age analysis of amounts owing** by the body corporate to the **creditors** and in particular to any **public or local authority** in respect of rates and taxes and charges for consumption or services, including but not limited to, water, electricity, gas, sewerage and refuse removal;*

*(c) the **expiry dates of all insurance policies.**” (Own emphasis.)*

The Act once again uses a term that is very broad and open to interpretation. The term “*proper financial management*” does not form part of the acknowledged accounting terminology in IFRS. Financial management is an entire discipline that deals with, amongst others, budgeting, risk assessment, making investment decisions, making financing decisions and ensuring profitability and solvency (Marx, De Swardt, Beaumont Smit, & Erasmus, 2011, p. 10).

Financial statements according to IFRS and IFRS for SMEs do not include information and notes on the financial management of an entity. In order to illustrate this, one can refer to the wording of IAS 1. IAS 1 (IASB, 2011, p. A559) states the following in paragraph 9 under the heading “*Purpose of financial statements*”:

“...Financial statements also show the results of management’s stewardship of the resources entrusted to it...” (Own emphasis.)

As part of their Pro-active Accounting Activities in Europe (PAAinE) initiative, the UK Accounting Standards Board issued a discussion paper on stewardship and accountability as an objective in financial reporting (ASB, 2007, p. 3). According to their research, commentators have suggested that there are a number of different interpretations of the term stewardship. According to their research, stewardship is inherently linked to the agency and stakeholder theory (See also 3.2. in Chapter 3) and that the stewardship objective is about assessing management’s competence and integrity including the success of their business management strategy (ASB, 2007, pp. 5-7). One important comment that was made in the paper (ASB, 2007, p. 11) was the following:

“The stewardship objective is about providing information about the past (including, for example, the transactions entered into, the decisions taken and the policies adopted) at a level of detail and in a way that enables the entity’s past performance to be assessed in its own right, rather than just as part of an assessment about likely future performance.”

It can, therefore, be concluded that one of the objectives of financial reporting is to show the result of management’s stewardship, and provide sufficient information in order to be able to assess an entity’s past performance. This does not mean that the financial statements should include specific information and notes about an entity’s “*proper financial management*”. That would be a nearly impossible task. Perhaps in this case the specific wording of the Act should be revisited.

For the 60 sets of annual financial statements over a period of two years, no other information pertaining to financial management was included except for the specific additional information as required by the Act.

Section 37 of the Act requires several other pieces of information to be included, which will be discussed below.

4.3.5.6. AGE ANALYSIS OF DEBTS

As part of the information and notes to the financial statements, section 37(2) requires the trustees to prepare an ***“age analysis of debts in respect of levies, special levies and other contributions”***. (Own emphasis.) The Act does not specify the format, content or level of detail of the age analysis of debts. The Act does not indicate whether the age analysis should include all debtors, or perhaps just those over 30 days. Usually, 30 days is an acceptable norm for outstanding debtors. Regarding the level of detail, the Act does not make mention of whether the age analysis should include the names of the individual debtors. On the one hand one may argue that this is sensitive or confidential information and that the body corporate has no right to publish the names of the individuals who have amounts outstanding on the financial statements. On the other hand one may argue that the members of the body corporate have the right to know who the individuals are that owe the body corporate money. Perhaps this is a legal question for which there is no clear answer yet.

For the 60 sets of annual financial statements over a period of two years the financial statements were analysed in order to determine whether it included an age analysis of debts. For the 2009 financial year 45 of the 60 (75%) financial statements analysed included an age analysis of debtors. For the 2010 financial year 53 of the 60 (88.33%) financial statements analysed included an age analysis of debtors. For both years this

was done using the total amount owing by debtors, and not stating individual debt and time outstanding per owner or resident. The total debtors amount was broken down into four categories being current, 30 days, 60 days and 90 days outstanding.

4.3.5.7. AGE ANALYSIS OF AMOUNTS OWING

As part of the information and notes to the financial statements, section 37(2) requires the trustees to prepare an *“age analysis of amounts owing by the body corporate to the **creditors** and in particular to any **public or local authority** in respect of rates and taxes and charges for consumption or services, including but not limited to, water, electricity, gas, sewerage and refuse removal”*. (Own emphasis.)

As was the case with the age analysis of debt, the Act does not specify the format, content or level of detail of the age analysis of amounts owing. The Act does not indicate whether the age analysis should include all creditors, or perhaps just those over 30 days. As was pointed out above, 30 days is usually an acceptable norm for outstanding amounts. Regarding the level of detail, the Act does not make mention of whether the age analysis should include the names of the individual creditors. Perhaps this is a legal question for which there is no clear answer yet.

For the 60 sets of annual financial statements over a period of two years the financial statements were analysed in order to determine whether it included an age analysis of amounts owing. None of the financial statements included any indication of a breakdown indicating how long the amounts have been outstanding.

4.3.5.8. EXPIRY DATES OF INSURANCE POLICIES

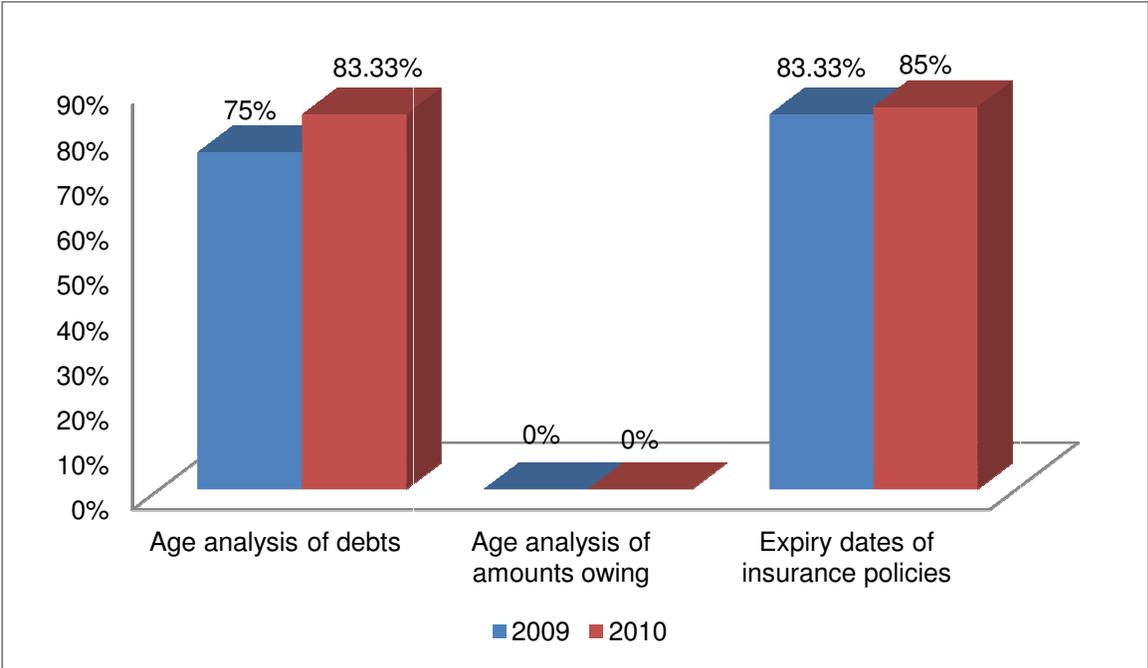
As part of the information and notes to the financial statements, section 37(2) requires the trustees to indicate “*the expiry dates of all insurance policies*”. Some of the requirements of the Act regarding insurance was already discussed in section 2.2.1.3. and 2.2.3.2. of Chapter 2. This is a very important aspect to include in the financial statements, so that the members of the body corporate can know that their property is properly insured against possible damage for the foreseeable future.

For the 2009 financial year 50 of the 60 financial statements that were analysed included references to the expiry dates of the insurance policies of the bodies corporate. Only 10 financial statements did not refer to the expiry dates of the insurance policies. For the 2010 financial year, 51 of the 60 financial statements that were analysed included references to the expiry dates of the insurance policies of the bodies corporate. Of these, 9 financial statements did not refer to the expiry dates of the insurance policies. Therefore, for 2009 83.33% of the financial statements analysed were correct according to the requirements of the Act, and for 2010 85% of the financial statements were correct.

In the sections that follow, the discussions are followed, where applicable, by graphs. In some cases the graphs are presented in two different formats for the sake of clarity and comparability.

The following graph is a graphic representation of the requirements of the Sectional Titles Act and whether it had been adhered to:

Figure 4.1 Application of Sectional Titles Act requirements



4.4. GENERAL EMPIRICAL FINDINGS

This section will contain a discussion of general observations and findings as part of the inspection of the 60 sets of financial statements over a period of three years. The financial statements with accompanying audit reports were obtained from a managing agent of bodies corporate for the financial years ending 2009 and 2010. Since the 2009 financial statements also have figures for the comparative financial year (2008), the data of three financial years is available for analysis. Furthermore, the sample was selected to include financial statements and audit reports drawn up and audited by various accounting and auditing practitioners appointed by the various bodies corporate. Where deemed necessary, a distinction was made between small (consisting of fewer than 10 units), medium (between 10 and 50 units) and large (more than 50 units) schemes and indicated as such.

4.4.1. ACCOUNTING PRACTITIONERS

Only 7 of the 60 (12%) bodies corporate for which the financial statements were analysed changed to a different accounting/auditing practitioner from 2009 to 2010. This is not an uncommon occurrence in the sectional title industry, as many bodies corporate have serious financial constraints. The prospect of lower accounting and auditing fees often result in bodies corporate changing from one practitioner to another. This will also be discussed as part of the empirical findings in Chapter 5. The following figure depicts the number of schemes that changed from one accounting/auditing practitioner to another:

Figure 4.2 Change in accounting/auditing practitioner



4.4.2. FINANCIAL STATEMENT AVERAGES AND RATIOS

During the empirical study the financial data was used to calculate average amounts for the total sample as well as for the small, medium and large schemes separately. These averages were subsequently used to calculate various ratios. The detail of the results is presented in the following sections.

4.4.2.1. AVERAGES FOR THE TOTAL SAMPLE

Where average amounts were calculated, the amounts of all 60 sets of financial statements were added up on a line by line basis per year and then divided by 60. The average number of units per complex was calculated as 23.12.

At this point it should be noted that the data as per the financial statements were captured exactly as it was received from the managing agent. Some of the captured financial statements contained minor rounding or calculation errors, none of which were considered to be material. For the sake of data integrity, and due to the fact that these errors were not material, no changes were made to the data as originally captured. As a result, these minor non-material errors were incorporated in and are reflected on the average financial statements below. This will result in some of the totals in the columns of the financial data (i.e. Fig. 4.3) not balancing exactly.

The formats of the financial statements also differed from complex to complex and therefore, only the most prevalent categories and line items were indicated on the face of the illustrative summarised financial statements. One concerning observation that was made during the summarising of the financial statements was the fact that many of the financial statements contained a line item called “other” on the face of the income

statement, which was usually quite large. In the summarised financial statements the item “other” accounted for 20.42% of total average expenses in 2008, 20.86% in 2009 and 26.72% in 2010. Even though individual amounts may not be material (IASB, 2011, p. A26), allocating more than 20% of expenses to a non-descriptive line item such as “other” is not necessarily in accordance with good, transparent accounting practices and does not comply with the qualitative characteristic of faithful representation (IASB, 2011, pp. A26-A27). In some cases, though, the amounts were detailed in the notes to the financial statements.

As mentioned in 4.3.5.3. above, most of the financial statements still contained the “old” wording in the titles, namely “balance sheet” and “income statement”. For purposes of illustration, the current wording as per IAS 1 will be used. Two additional columns were added to the financial statements, indicating the variance from 2008 to 2009 and 2009 to 2010 respectively.

The following figure represents the averages for the entire sample in the format of a summarised financial statement:

Figure 4.3 Averages for the total sample in financial statement format (23.12 units per scheme on average)

STATEMENT OF FINANCIAL POSITION					
	2008 R	2009 R	Variance %	2010 R	Variance %
Assets	61,107.47	70,008.47	14.57%	96,449.86	37.77%
Non-current assets	4,662.34	5,798.38	24.37%	7,696.52	32.74%
Investments / long-term deposits	0.00	596.33	100.00%	1,949.90	226.98%
Other	4,662.34	5,202.05	11.58%	5,746.62	10.47%
Current assets	56,445.14	64,210.08	13.76%	88,753.34	38.22%
Trade and other receivables	11,157.24	15,105.15	35.38%	19,111.80	26.53%
Cash and cash equivalents	43,421.38	44,887.87	3.38%	66,410.70	47.95%
Deposits	1,728.10	4,083.59	136.30%	2,884.45	-29.36%
Current tax receivables	116.57	123.48	5.93%	346.39	180.53%
Other	21.85	10.00	-54.23%	0.00	-100.00%
Equity and liabilities	61,107.47	70,007.82	14.57%	96,449.86	37.77%
Members' funds and reserves	41,308.80	49,187.48	19.07%	65,007.54	32.16%
Accumulated surplus/(shortage)	40,672.01	46,931.66	15.39%	67,707.16	44.27%
Other reserves	636.79	2,255.83	254.25%	-2,699.62	-219.67%
Liabilities	19,798.67	20,820.34	5.16%	31,442.32	51.02%
Non-current liabilities	0.00	0.00	0.00%	0.00	0.00%
Long-term loans	0.00	0.00	0.00%	0.00	0.00%
Other	0.00	0.00	0.00%	0.00	0.00%
Current liabilities	19,798.67	20,820.34	5.16%	31,442.32	51.02%
Current tax payable	2,001.26	3,644.62	82.12%	5,123.35	40.57%
Trade and other payables	16,604.95	15,344.97	-7.59%	23,905.42	55.79%
Other	1,192.46	1,830.75	53.53%	2,413.55	31.83%

STATEMENT OF PROFIT AND LOSS AND OTHER COMPREHENSIVE INCOME					
	2008	2009	Variance	2010	Variance
	R	R	%	R	%
Income	135,252.13	147,669.14	9.18%	170,187.44	15.25%
Levies	115,536.93	120,467.64	4.27%	135,994.80	12.89%
Fines	37.36	25.00	-33.08%	18.65	-25.41%
Interest received	3,331.56	5,720.34	71.70%	4,093.71	-28.44%
Other	16,346.28	21,456.16	31.26%	30,080.28	40.19%
Expenses	127,354.95	138,994.04	9.14%	151,065.40	8.68%
Bank charges	935.46	1,579.05	68.80%	894.55	-43.35%
Management fees	9,781.55	12,098.85	23.69%	13,367.42	10.49%
Rates and taxes	10,544.15	5,005.02	-52.53%	1,259.90	-74.83%
Repairs and maintenance	40,194.04	42,844.02	6.59%	44,969.30	4.96%
Audit / accounting fee	1,912.87	1,433.03	-25.08%	1,653.39	15.38%
Tax admin fee	329.74	302.59	-8.23%	630.84	108.48%
Legal fees	48.55	68.91	41.92%	65.36	-5.15%
Insurance	17,525.00	19,749.56	12.69%	24,278.96	22.93%
Water and electricity	16,992.94	23,102.45	35.95%	20,941.24	-9.35%
Bad debt	864.64	1,431.43	65.55%	0.00	-100.00%
Other	26,001.81	29,001.05	11.53%	40,359.19	39.16%
Taxation	2,224.19	2,378.09	6.92%	2,645.24	11.23%
Surplus / (deficit) for year	7,897.19	8,673.82	9.83%	19,122.04	120.46%

4.4.2.2. RATIOS FOR THE TOTAL SAMPLE

4.4.2.2.1. ANALYSIS OF INCOME

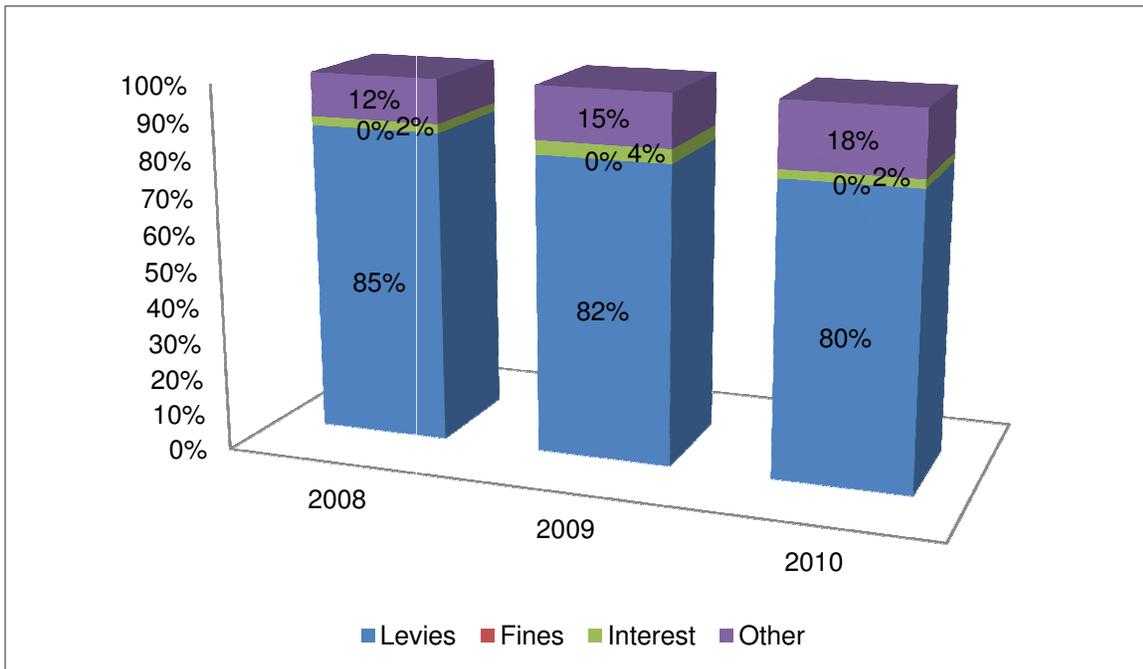
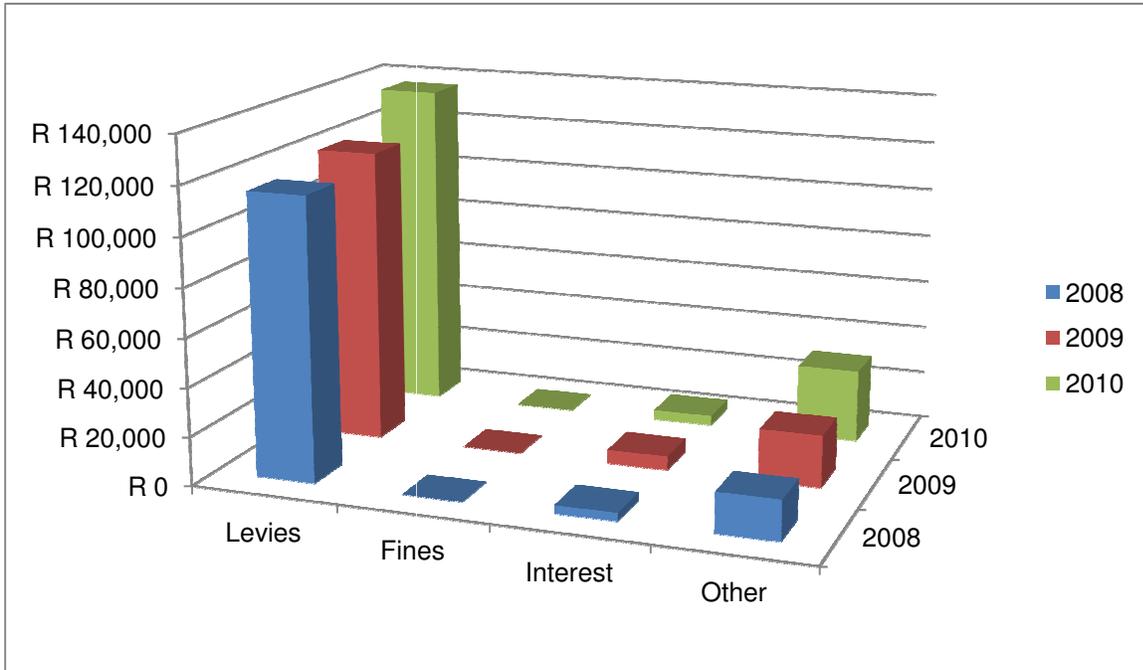
The analysis of the total average income for the total sample indicated that levies were the largest single contributing factor to total average income. Expressed in rand terms, total average levies amounted to R135 252.13 in 2008, R147 669.14 in 2009 and R170 187.44 in 2010. Total average levies increased by 4.27% from 2008 to 2009 and

12.89% from 2009 to 2010. Levies accounted for 85% (2008), 82% (2009) and 80% (2010) of total average income.

Despite the general increasing trend in total average levies from 2008 to 2010, the fact that levies expressed as a percentage of total average income showed a decreasing trend over the three years is causing concern. Seen in the light of the economic downturn that was experienced throughout South Africa as from 2008 and financial difficulties faced by many bodies corporate, one would certainly not want to see levies as a percentage of total average income decrease.

Fines were by far the smallest single contributor, almost insignificant, and amounted to 0.03% (2008), 0.02% (2009) and 0.01% (2010) of total income. Interest received accounted for 2% (2008), 4% (2009) and 2% (2010) of total average income. Income items classified as "other income" amounted to 12% (2008), 15% (2009) and 18% (2010) of total income. Expressed in rand terms, other income amounted to R16 346.28 in 2008, increasing by 31.26% to R21 456.16 in 2009 and again increasing by 40.19% to R30 080.28 in 2010. It is causing concern that this "unclassified" type of income expressed as a percentage of total average income shows an increasing trend, albeit small, while total average levies expressed as a percentage of total average income (as mentioned above) is showing a decreasing trend. The following is a graphic representation (presented in two different formats for the sake of clarity) detailing the breakdown of income items:

Figure 4.4 Analysis of amounts making up total average income for the total sample in graph format



Average total levies for the sample amounted to R115 536.93 (2008), R120 467.64 (2009) and R135 994.80 (2010) per year. The average number of units for the total sample was 23.12 units. As a result, expressed in rand per unit, the average total levies per year amounted to R4 997.99 (2008), R5 211.28 (2009) and R5 882.98 (2010). This amounted to R416.50 (2008), R434.27 (2009) and R490.25 (2010) per unit per month.

4.4.2.2. ANALYSIS OF EXPENSES EXCLUDING TAXATION

Analysis of the total average expenses of the total sample revealed that the six largest expenses were management fees, rates and taxes, audit fee, insurance, water and electricity and repairs and maintenance. These expenses accounted for a total of 76% (2008), 75% (2009) and 70% (2010) of average total expenses.

For the total sample, repairs and maintenance were by far the largest single expense at 32% (2008), 31% (2009) and 30% (2010) of average total expenses. The average annual total repairs and maintenance expense amounted to R40 194.04 (2008), R42 844.02 (2009) and R44 969.30.

Water and electricity and insurance were the second largest expenses for the schemes. Water and electricity amounted to 13% (2009), 17% (2009) and 14% (2010), and insurance amounted to 14% (2008), 14% (2009) and 16% (2010) of average total expenses. The average annual total expense for water and electricity amounted to R16 992.94 (2008), R23 102.45 (2009) and R20 941.24 (2010), and the average annual total expense for insurance was R17 525 (2008), R19 749.56 (2009) and R24 278.96 (2010). For the financial statements analysed, the expenses for water and electricity were shown as a total amount and not separately.

The reason for the decline in the average water and electricity expense from 2009 to 2010 was the fact that a number of complexes in the sample had individual prepaid electricity meters installed. This resulted in owners paying for their own electricity and not being invoiced for the electricity of their units by the body corporate. The only remaining amount of electricity on the financial statements of such a body corporate would be the amount for electricity usage of the common property, such as electronic gates, a complex lawn mower, electrified fencing and the pump of a communal swimming pool.

Management fees accounted for 8% (2008), 9% (2009) and 9% (2010) of average total expenses. The amounts for average annual total management fees were R9 781.55 (2008), R12 098.85 (2009) and R13 367.42 (2010).

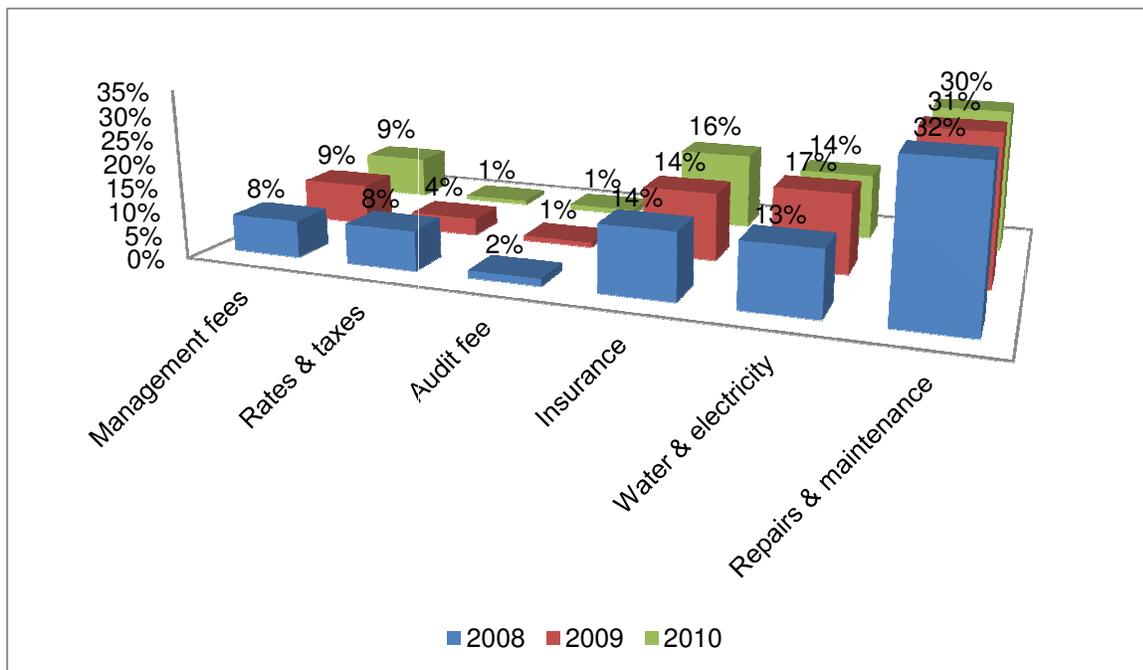
Audit fees was the smallest of the six expenses at 2% (2008), 1% (2009) and 1% (2010) of average total expenses. The amounts for average annual total audit fees were R1 912.87 (2008), R1 433.03 (2009) and R1 653.39 (2010). A detailed analysis of audit fees was done in section 3.3.7.3.3. of Chapter 3.

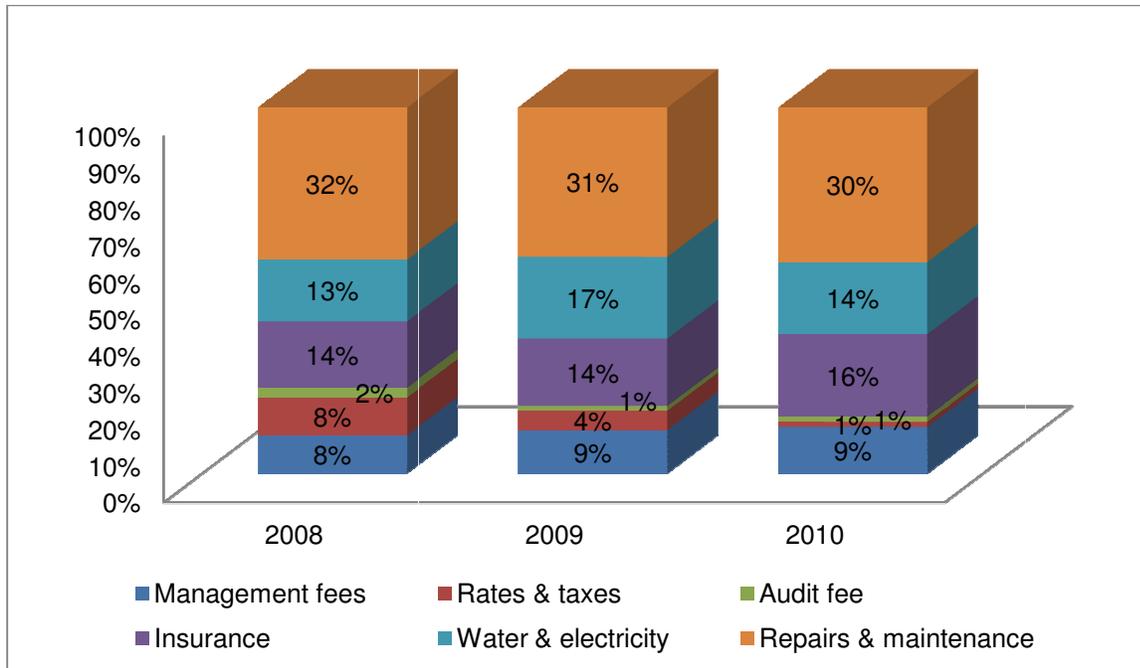
Over the three years there was a significant drop in rates and taxes as a percentage of total expenses from 8% (2008) to 4% (2009) and then to 1% (2010) of average total expenses. Expressed in rand terms, the total average expense for rates and taxes went down from R10 544.15 (2008) to R5 005.02 (2009) to R1 259.90 (2010). The reason for the significant drop was due to changes in legislation. In the past, the owner of a sectional title unit did not pay rates directly to the municipality. The municipality billed the rates to the body corporate of the sectional title scheme. The body corporate in turn recovered this from each owner in the scheme as part of their levy (Hodgon, 2007, p. 18). Since the promulgation of the Local Government: Municipal Property Rates Act 6 of 2004, a system of individual rating of sectional title units has been introduced

(Pienaar, 2010, p. 139). As from July 2009, all municipalities were required to individually value and rate sectional title units, so that the owner of the individual unit is responsible for paying the rates and taxes on the unit directly to the municipality. This explains the significant drop in the amount of rates and taxes paid by the schemes that formed part of the sample. For future research purposes, it should be kept in mind that rates and taxes will not play a significant role in the analysis of expenses, as were the case in the past.

The two figures below graphically represent the above information in two different formats, for the sake of clarity:

Figure 4.5 The six largest expenses as a percentage of total expenses for the total sample in graph format





4.4.2.2.3. ANALYSIS OF TAXATION

Section 10(1)(e) of the Income Tax Act No. 58 of 1962 deals with income tax exemptions. According to Section 10(1)(e)(i)(aa) any levy received by, or accrued to any body corporate in terms of the Sectional Titles Act of 1986 (Act No. 59 of 1980) from its members, shall be exempt from normal tax. As from the commencement of years of assessment ending on or after 1 January 2009, a basic threshold exemption of R50 000 was also introduced in respect of income from a source other than levy income (SARS, 2011, p. 3). Examples of this type of income would be rental income derived from the letting of property, investment income, income received for services rendered and penalty income (SARS, 2011, p. 8).

Expenditure which relates directly to receipts and accruals that do not qualify for exemption will qualify for deduction in determining taxable income. The only provision is that it should meet the requirements for deductibility under the Act. Other general

expenditure incurred (e.g. audit fees and bank charges), may be allowed as a deduction to the extent that it is in the production of income. The deduction of a fixed percentage of the general expenditure that is attributable to all the income is not acceptable. General expenditure must be allocated pro rata to the receipts and accruals of the entity unless accurate records relating to the expenditure incurred in the production of the different sources of income have been kept. SARS has clear examples available on the calculation of body corporate taxation (SARS, 2011, pp. 9-10).

Bodies corporate are not registered at the Tax Exemption Unit for income tax purposes but at a SARS branch office. A body corporate is not required to apply for exemption under section 10(1)(e)(i)(aa) and the levy income exemption and the basic threshold exemption are automatically applied on assessment. Even though it is possible that a body corporate may never have an income tax liability, they are required to register for income tax purposes and submit annual income tax returns (SARS, 2011, pp. 6-7).

For the total sample selected, the average amount of taxation expressed in rand terms was R2 224 (2008), R2 378.09 (2009) and R2 645.24 (2010). Total average taxation amounted to 1.64% (2008), 1.61% (2009) and 1.55% (2010) of total average income.

4.4.2.2.4. ANALYSIS OF SURPLUS/DEFICIT

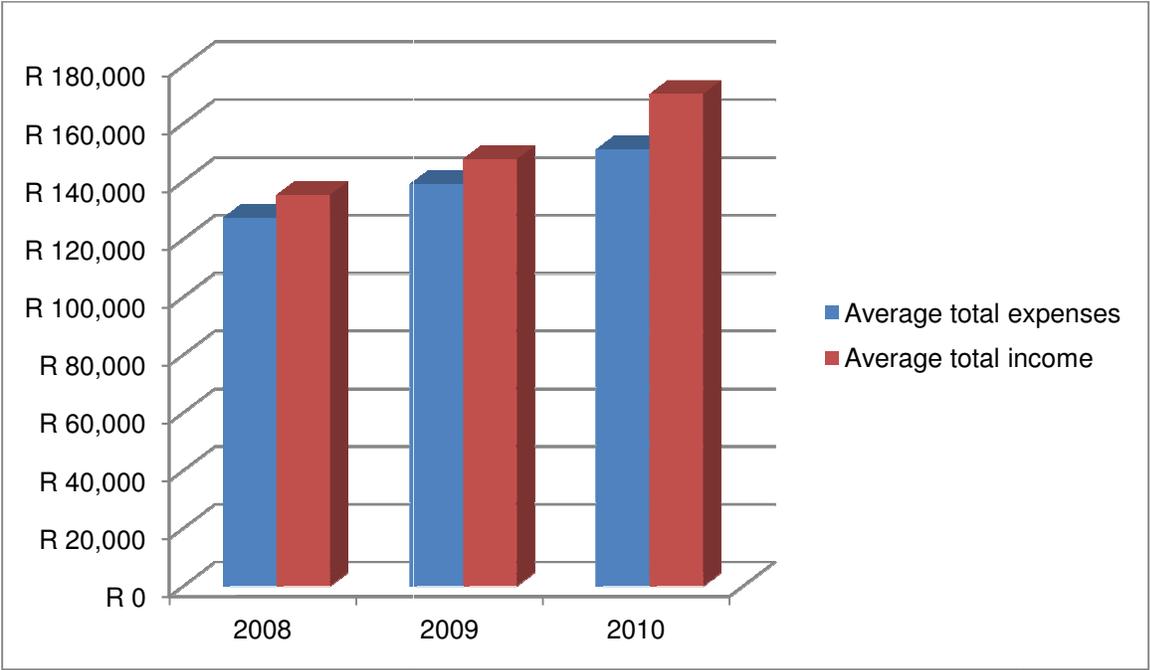
For the total sample selected, the average surplus/deficit amount (total income less total expenses) for the total sample expressed in rand was R3 179.34 (2008), R8 985.57 (2009) and R9 785.19 (2010). Expressed as a percentage of total income the surpluses amounted to 5.84% (2008), 5.87% (2009) and 11.24% (2010) of average total income. The reason for the large increase in surplus from 2009 to 2010 could not be established with the available financial data.

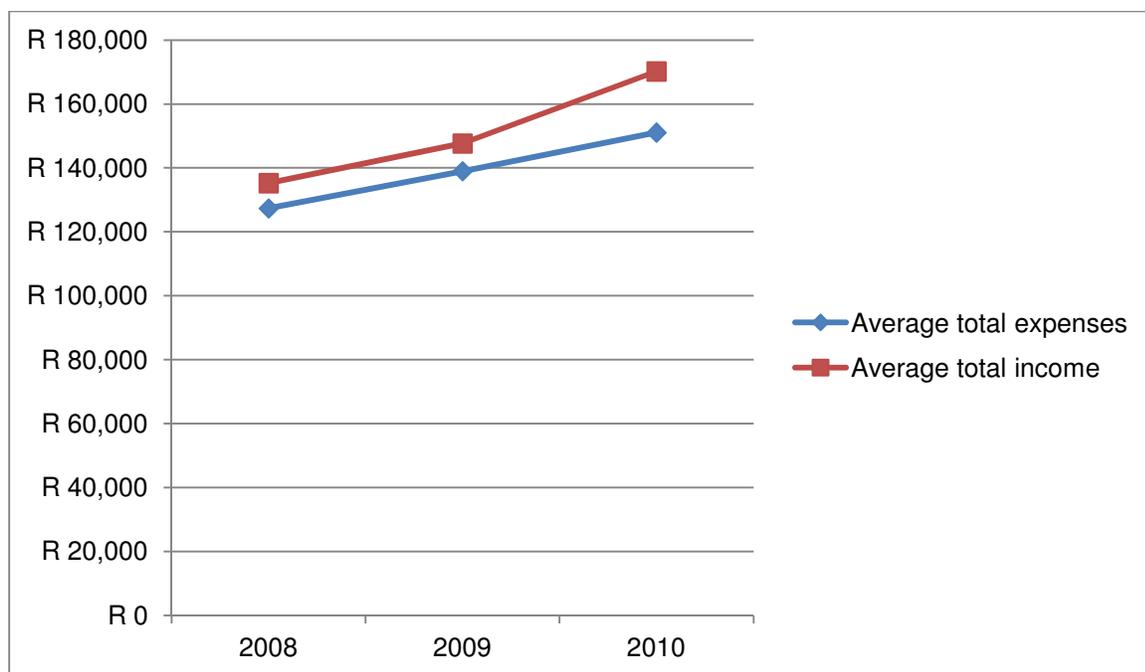
Further analysis of the sample indicated that, for 2008, 41 of the 60 bodies corporate showed a surplus and 19 showed a deficit. For 2009, 37 of the 60 bodies corporate showed a surplus and 23 showed a deficit. In comparison, 41 of the 60 bodies corporate showed a surplus for 2010, and 19 showed a deficit.

4.4.2.2.5. ANALYSIS OF GROWTH

For the sample selected, the financial figures showed an increasing trend from year to year. From 2008 to 2009 and again from 2009 to 2010 there was a 9% increase in total average expenses. From 2008 to 2009 there was a 9.18% increase in average total income and from 2009 to 2010 there was a 15.25% increase in average total income. The figures below illustrate the growth in two different formats, for the sake of clarity:

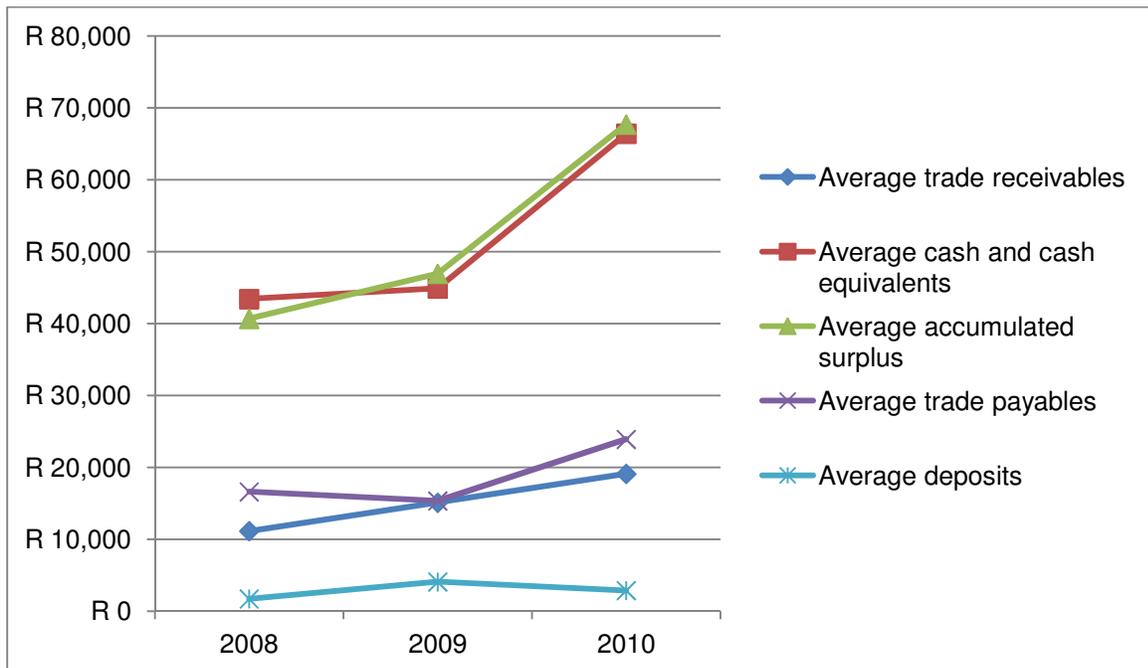
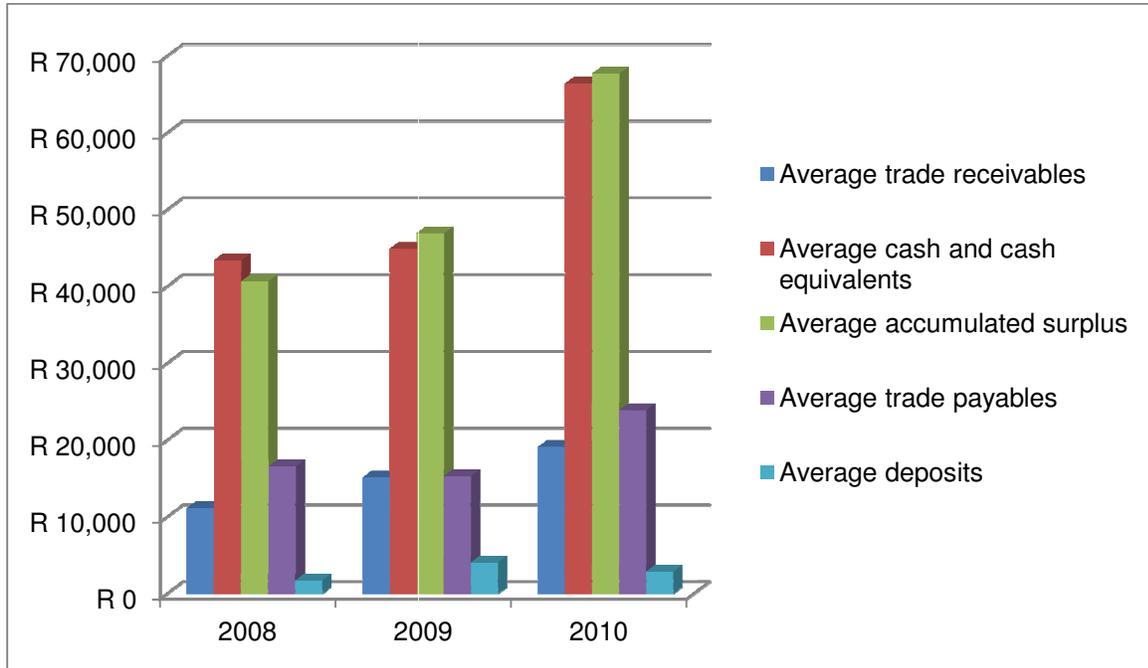
Figure 4.6 Growth of items on the statement of comprehensive income





The total average trade receivables, cash and cash equivalents and accumulated surplus all showed an increase from 2008 to 2009 as well as from 2009 to 2010. Total average deposits and trade payables showed varying trends. Total average trade receivables increased by 35% from 2008 to 2009 and by 27% from 2009 to 2010. During the interviews with the managing agents (further discussed in Chapter 5), they revealed that a high increase in average debtors were evident from 2008 to 2010, which they attributed to many debtors experiencing financial difficulties due to the economic downturn in the country. Total average cash and cash equivalents increased by 3% from 2008 to 2009 and by 48% from 2009 to 2010. Total average accumulated surplus increased by 15% from 2008 to 2009 and with 44% from 2009 to 2010. Total average trade payables decreased with 8% from 2008 to 2009 and then increased by 56% from 2009 to 2010. Total average deposits increased by 136% from 2008 to 2009 and then decreased with 29% from 2009 to 2010. The reason for the varying trends from 2008 to 2010 could not be established with the available financial data. The two figures below graphically represent the above information in two different formats, for the sake of clarity:

Figure 4.7 Growth of items on the statement of financial position



4.4.2.2.6. FINANCIAL STRENGTH

One of the main concerns for any type of entity is the ability to honour obligations as they become due and to obtain funds needed timeously (Koen & Oberholster, 1999, p. 50; Gordon, 1992, pp. 61-65; Kew & Watson, 2012, p. 568). Literature on financial management and financial statement analysis and interpretation refer to a number of standard ratios used to calculate financial strength. However, many of these ratio formulas use line items such as inventory, sales, purchases, shareholders' interest or share capital. Due to the nature of sectional title schemes some of these concepts do not apply to the industry and some of the published ratios cannot be used in their standard format. Furthermore, several variations can be calculated on various ratios and different authors use varying terms to describe the same item (Koen & Oberholster, 1999, p. 53). As a result, the titles of ratios may differ from source to source.

The analysis and interpretation of financial ratios is not the main purpose of this study; the calculation thereof is simply done in order to identify some basic benchmarks for the industry. Therefore, only a few ratios were selected for use. The following financial strength ratios were calculated: accumulated surplus to total assets, total assets to total liabilities, current assets to current liabilities, receivables to levies, payables to expenses, receivables to total assets, cash to total assets and bad debts to receivables.

The ratio of accumulated surplus to assets was calculated instead of the traditional total shareholders' interest to total assets ratio (Service, 2012, p. 1032). The ratio shows to what extent the assets of the body corporate are financed by way of accumulated funds. The ratios for the average of the total sample were 0.67:1 (2008), 0.67:1 (2009) and 0.7:1 (2010). So far, no academic research has been done on what the accepted norms should be for the sectional title industry and therefore no benchmarks were available.

The solvency ratio calculated as total assets to total liabilities show to what extent liabilities are covered by assets. It is also an indication of whether an entity will be able to honour obligations in future. Using the average total assets and average total liabilities, the average ratios for the total sample amounted to 3.09 (2008), 3.36 (2009) and 3.07 (2010). This means that the total liabilities are, on average, covered more than three times by the total assets of the bodies corporate.

Regarding liquidity, the ratio of current assets to current liabilities is an indication of the ability of an enterprise to repay short-term debts as they become due. The ratio is usually called the current ratio and refers to the availability of cash in the near future after taking into account the financial commitments for a specific period. Generally, a current ratio of 2:1 is considered good. (Kew & Watson, 2012, pp. 568-569; Koen & Oberholster, 1999, p. 53). The average current ratio for the total sample was 2.85:1 (2008), 3.08:1 (2009) and 2.82:1 (2010). Over the three years, the current liabilities were covered between two and three times by the current assets and it is well above the generally accepted norm.

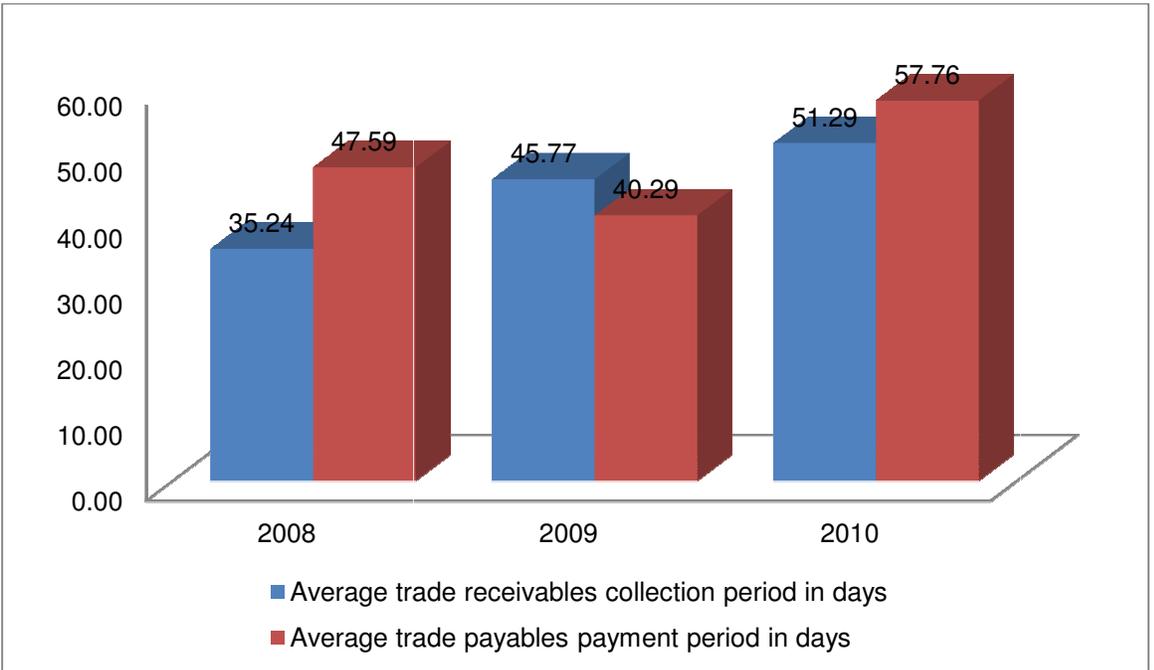
Traditional working capital ratios include the inventory line item as part of the ratio analysis - more specifically, to calculate ratios such as the acid test ratio. Bodies corporate, however, do not buy or sell inventory. As a result, not all of the traditional working capital ratios are relevant, and the traditional working capital ratios have to be adjusted in order to be applicable to the sectional title industry.

For the sample selected, the total average debtors' collection period was calculated using total average levies instead of sales as per the traditional ratio. The collection period amounted to 35.24 days in 2008, 45.77 days in 2009 and 51.29 days in 2010. The increasing trend in the average receivables collection period may be indicative of possible problems regarding the collection of levies and may be attributed to the current

difficult economic circumstances in the country. An increase in debtors' collection period from 35 days to 51 days over a period of two years is a concerning trend, and something which trustees should take note of. (See also the figure below for further detail.)

For the sample selected, the total average creditors' payment period was calculated using total expenses instead of credit purchases as per the traditional ratio. The payment period went down from 47.59 days in 2008 to 40.29 days in 2009 and then up to 57.76 days in 2010. The figure below graphically represents the above information:

Figure 4.8 Average collection and payment periods



During the course of the empirical study, it was mentioned that the cut-off of debtors and creditors can vary significantly between bodies corporate. For example, some

managing agents close the debtors system on the 15th of every month. Financial statements are prepared as on the 30th/31st of the month and debtors have to settle their accounts by the 7th. Other managing agents close their debtors earlier or later or have different collection policies, which makes it difficult to compare the financial results of schemes. Creditors can also create some inconsistencies. Some municipal accounts have a long time lag; for example, a body corporate may be billed in August for electricity usage in May/June. Another problem is that municipal accounts for water are sometimes issued at estimated amounts and not the amount of actual usage. This can create havoc on a set of financial statements if an account with billing for actual usage is eventually received and the water was either over- or underpaid for a few months due to incorrect estimates. These issues will be discussed in more detail in Chapter 5.

In the next sections a similar process will be followed as for the analysis of the total sample, but the analysis will be done separately for small (consisting of fewer than 10 units), medium (between 10 and 50 units) and large (more than 50 units) schemes.

4.4.2.3. COMPARISON OF AVERAGES BETWEEN SMALL, MEDIUM AND LARGE SCHEMES IN THE SAMPLE

As mentioned in 3.3.7.3.2. in Chapter 3 and in 4.4. above, a distinction was made between small (consisting of fewer than 10 units), medium (between 10 and 50 units) and large (more than 50 units) schemes. For the sample of 60 sets of financial statements of bodies corporate over a period of three years, the annual financial statements were analysed and 11 were classified as small (consisting of fewer than 10 units), 46 were classified as medium (between 10 and 50 units) and three schemes were classified as large (more than 50 units). Refer also to 1.6.5. in Chapter 1 for more detail on the background to the quantitative research methodology.

One of the 11 small schemes that were identified is a commercial scheme operating with a large amount of government funding. The financing structure of this scheme is totally different from that of the other schemes in the sample. Initial analysis and interpretation indicated that the inclusion of this scheme caused skewed data and incoherent results. For that reason the financial data of the scheme was excluded for purposes of analysis and interpretation of the small-sized schemes.

For the calculation of the average amounts of the small schemes, the total amounts of all 10 remaining sets of financial statements were added up on a line by line basis per year and then divided by 10. For the medium-sized schemes, the total amounts of all 46 sets of financial statements were added up on a line by line basis per year and then divided by 46. For the large-sized schemes, the same approach was followed for the 3 sets of financial statements.

The average number of units for the small-sized schemes was 7.5 units per scheme. For the medium-sized units there were, on average, 21.24 units per scheme, and for the large-sized schemes there were, on average, 111.67 units per scheme.

As was mentioned in 4.4.2.1. above, the data as per the financial statements were captured exactly as it was received from the managing agent. Some of the captured financial statements contained minor rounding or calculation errors, none of which were considered to be material. For the sake of data integrity, and due to the fact that these errors were not material, no changes were made to the data as originally captured. As a result, these minor non-material errors were incorporated in and are reflected on the average financial statements below.

During the analysis of the various bodies corporate of different sizes, the same observation regarding amounts classified as “other” income was made as in 4.4.2.1.

The following figures represent the averages for the small-, medium- and large-sized entities respectively in the format of a summarised financial statement:

Figure 4.9 Averages for the small schemes in the sample in financial statement format (7.5 units per scheme on average)

STATEMENT OF FINANCIAL POSITION					
	2008 R	2009 R	Variance %	2010 R	Variance %
Assets	12,042.17	11,807.49	-1.95%	17,595.05	49.02%
Non-current assets	0.00	0.00	0.00%	0.00	0.00%
Investments / long-term deposits	0.00	0.00	0.00%	0.00	0.00%
Other	0.00	0.00	0.00%	0.00	0.00%
Current assets	12,042.17	11,807.49	-1.95%	17,595.05	49.02%
Trade and other receivables	4,157.60	3,968.04	-4.56%	8,739.78	120.25%
Cash and cash equivalents	7,365.06	7,385.74	0.28%	8,314.88	12.58%
Deposits	408.63	425.48	4.12%	522.42	22.78%
Current tax receivables	41.99	28.24	-32.75%	17.96	-36.40%
Other	68.90	0.00	-100.00%	0.00	0.00%
Equity and liabilities	12,042.17	11,807.49	-1.95%	17,595.15	49.02%
Members' funds and reserves	8,654.53	8,470.14	-2.13%	9,378.65	10.73%
Accumulated surplus/(shortage)	8,654.53	8,470.14	-2.13%	9,378.65	10.73%
Other reserves	0.00	0.00	0.00%	0.00	0.00%
Liabilities	3,387.65	3,337.36	-1.48%	8,216.50	146.20%
Non-current liabilities	0.00	0.00	0.00%	0.00	0.00%
Long-term loans	0.00	0.00	0.00%	0.00	0.00%
Other	0.00	0.00	0.00%	0.00	0.00%
Current liabilities	3,387.65	3,337.36	-1.48%	8,216.50	146.20%
Current tax payable	167.21	265.31	58.67%	175.87	-33.71%
Trade and other payables	3,220.44	3,072.05	-4.61%	8,040.63	161.74%
Other	0.00	0.00	0.00%	0.00	0.00%

STATEMENT OF PROFIT AND LOSS AND OTHER COMPREHENSIVE INCOME					
	2008	2009	Variance	2010	Variance
	R	R	%	R	%
Income	35,152.88	35,833.15	1.94%	46,568.87	29.96%
Levies	34,335.75	34,344.96	0.03%	45,828.35	33.44%
Fines	50.00	0.00	-100.00%	0.00	0.00%
Interest received	642.13	1,089.19	69.62%	570.77	-47.60%
Other	125.00	399.00	219.20%	169.75	-57.46%
Expenses	34,147.69	36,002.14	5.43%	45,580.58	26.61%
Bank charges	447.03	724.54	62.08%	486.09	-32.91%
Management fees	4,314.69	4,600.52	6.62%	5,939.24	29.10%
Rates and taxes	2,919.86	0.00	-100.00%	0.00	0.00%
Repairs and maintenance	7,469.77	9,863.86	32.05%	11,950.72	21.16%
Audit / accounting fee	823.77	1,106.59	34.33%	1,273.00	15.04%
Tax admin fee	295.20	347.50	17.72%	515.00	48.20%
Legal fees	0.00	0.00	0.00%	-10.41	100.00%
Insurance	9,664.01	11,306.82	17.00%	12,019.07	6.30%
Water and electricity	4,024.50	4,240.16	5.36%	8,684.25	104.81%
Bad debt	0.00	0.00	0.00%	0.00	0.00%
Other	4,020.48	3,638.26	-9.51%	4,723.62	29.83%
Taxation	168.38	173.89	3.27%	0.00	-100.00%
Surplus / (deficit) for year	1,005.20	-176.69	-117.58%	988.29	-659.34%

Figure 4.10 Averages for the medium schemes in the sample in financial statement format (21.24 units per scheme on average)

STATEMENT OF FINANCIAL POSITION					
	2008 R	2009 R	Variance %	2010 R	Variance %
Assets	57,191.07	62,777.70	9.77%	72,363.45	15.27%
Non-current assets	6,112.84	7,563.11	23.72%	10,038.93	32.74%
Investments / long-term deposits	0.00	777.83	100.00%	2,543.35	226.98%
Other	6,112.84	6,785.28	11.00%	7,495.59	10.47%
Current assets	51,078.23	55,214.59	8.10%	62,324.52	12.88%
Trade and other receivables	10,478.69	14,164.70	35.18%	18,415.98	30.01%
Cash and cash equivalents	39,023.89	36,417.63	-6.68%	40,591.00	11.46%
Deposits	1,418.81	4,466.58	214.81%	2,883.20	-35.45%
Current tax receivables	143.50	152.64	6.37%	434.34	184.56%
Other	13.33	13.04	-2.17%	0.00	-100.00%
Equity and liabilities	57,175.76	62,776.85	9.80%	72,363.43	15.27%
Members' funds and reserves	37,685.71	45,729.55	21.34%	51,225.16	12.02%
Accumulated surplus/(shortage)	36,866.11	42,787.17	16.06%	54,746.40	27.95%
Other reserves	819.60	2,942.38	259.00%	-3,521.24	-219.67%
Liabilities	19,490.05	17,047.30	-12.53%	21,138.28	24.00%
Non-current liabilities	0.00	0.00	0.00%	0.00	0.00%
Long-term loans	0.00	0.00	0.00%	0.00	0.00%
Other	0.00	0.00	0.00%	0.00	0.00%
Current liabilities	19,490.05	17,047.30	-12.53%	21,138.28	24.00%
Current tax payable	1,017.70	1,244.86	22.32%	619.67	-50.22%
Trade and other payables	16,908.91	13,414.50	-20.67%	17,370.50	29.49%
Other	1,563.44	2,387.93	52.74%	3,148.11	31.83%

STATEMENT OF PROFIT AND LOSS AND OTHER COMPREHENSIVE INCOME					
	2008	2009	Variance	2010	Variance
	R	R	%	R	%
Income	113,371.67	125,833.12	10.99%	141,927.30	12.79%
Levies	95,928.07	100,444.39	4.71%	113,929.22	13.43%
Fines	37.87	32.61	-13.89%	24.32	-25.41%
Interest received	2,979.07	5,244.20	76.03%	3,054.55	-41.75%
Other	14,426.67	20,111.92	39.41%	24,919.21	23.90%
Expenses	110,192.33	116,847.55	6.04%	132,142.11	13.09%
Bank charges	1,019.70	1,718.31	68.51%	935.48	-45.56%
Management fees	8,873.14	10,994.22	23.90%	11,896.37	8.21%
Rates and taxes	8,195.82	5,257.53	-35.85%	1,571.08	-70.12%
Repairs and maintenance	33,097.71	33,279.36	0.55%	33,630.09	1.05%
Audit / accounting fee	2,134.50	1,542.50	-27.73%	1,684.21	9.19%
Tax admin fee	330.05	295.65	-10.42%	656.53	122.06%
Legal fees	52.20	127.37	144.00%	169.52	33.09%
Insurance	17,157.63	18,943.27	10.41%	23,973.03	26.55%
Water and electricity	20,644.60	22,544.13	9.20%	25,767.48	14.30%
Bad debt	1,133.64	1,867.08	64.70%	0.00	-100.00%
Other	16,666.53	19,375.49	16.25%	32,140.06	65.88%
	0.00	0.00		0.00	
Taxation	886.81	902.65	1.79%	-281.74	-131.21%
Surplus / (deficit) for year	3,179.34	8,985.57	182.62%	9,785.19	8.90%

Figure 4.11 Averages for the large schemes in the sample in financial statement format (111.67 units per scheme on average)

STATEMENT OF FINANCIAL POSITION					
	2008 R	2009 R	Variance %	2010 R	Variance %
Assets	288,081.71	389,951.68	35.36%	738,707.35	89.44%
Non-current assets	0.00	0.00	0.00%	0.00	0.00%
Investments / long-term deposits	0.00	0.00	0.00%	0.00	0.00%
Other	0.00	0.00	0.00%	0.00	0.00%
Current assets	288,081.71	389,951.68	35.36%	738,707.35	89.44%
Trade and other receivables	22,120.80	55,672.11	151.67%	44,856.85	-19.43%
Cash and cash equivalents	254,619.20	322,513.71	26.67%	681,507.82	111.31%
Deposits	11,341.71	11,765.86	3.74%	12,285.96	4.42%
Current tax receivables	0.00	0.00	0.00%	56.71	100.00%
Other	0.00	0.00	0.00%	0.00	0.00%
Equity and liabilities	288,081.71	389,951.68	35.36%	738,707.35	89.44%
Members' funds and reserves	217,241.47	265,527.35	22.23%	488,454.39	83.96%
Accumulated surplus/(shortage)	217,241.47	265,527.35	22.23%	488,454.39	83.96%
Other reserves	0.00	0.00	0.00%	0.00	0.00%
Liabilities	70,840.24	124,424.32	75.64%	250,252.96	101.13%
Non-current liabilities	0.00	0.00	0.00%	0.00	0.00%
Long-term loans	0.00	0.00	0.00%	0.00	0.00%
Other	0.00	0.00	0.00%	0.00	0.00%
Current liabilities	70,840.24	124,424.32	75.64%	250,252.96	101.13%
Current tax payable	23,600.70	53,306.10	125.87%	92,731.52	73.96%
Trade and other payables	47,239.54	71,118.23	50.55%	157,521.45	121.49%
Other	0.00	0.00	0.00%	0.00	0.00%

STATEMENT OF PROFIT AND LOSS AND OTHER COMPREHENSIVE INCOME					
	2008	2009	Variance	2010	Variance
	R	R	%	R	%
Income	696,067.53	745,392.13	7.09%	867,472.71	16.38%
Levies	572,415.17	595,691.99	4.07%	615,535.93	3.33%
Fines	0.00	0.00	0.00%	0.00	0.00%
Interest received	18,490.58	30,289.73	63.81%	32,991.57	8.92%
Other	105,161.78	119,410.41	13.55%	218,945.20	83.36%
Expenses	597,363.69	697,106.25	16.70%	644,545.67	-7.54%
Bank charges	1,842.74	2,910.91	57.97%	2,019.81	-30.61%
Management fees	46,266.44	59,220.52	28.00%	66,095.29	11.61%
Rates and taxes	74,698.12	19,484.91	-73.92%	1,108.15	-94.31%
Repairs and maintenance	262,372.27	287,202.55	9.46%	299,349.94	4.23%
Audit / accounting fee	2,856.32	1,320.23	-53.78%	3,000.00	127.23%
Tax admin fee	550.13	360.10	-34.54%	791.67	119.85%
Legal fees	171.91	-289.80	-268.58%	-1,257.34	333.86%
Insurance	54,169.23	70,538.03	30.22%	84,916.10	20.38%
Water and electricity	19,029.14	110,997.92	483.31%	3,150.04	-97.16%
Bad debt	0.00	0.00	0.00%	0.00	0.00%
Other	105,632.40	112,254.43	6.27%	128,147.23	14.16%
Taxation	29,774.99	33,106.45	11.19%	57,224.78	72.85%
Surplus / (deficit) for year	98,703.84	48,285.89	-51.08%	222,927.03	361.68%

4.4.2.4. RATIOS FOR SMALL, MEDIUM AND LARGE SCHEMES IN THE SAMPLE

For the small, medium and large schemes in the sample the same approach for the ratio analysis will be followed as for the total sample.

4.4.2.4.1. ANALYSIS OF INCOME FOR SMALL, MEDIUM AND LARGE SCHEMES

As was the case for the total sample, the analysis of the total average income analysed for the different sizes of schemes in the sample indicated that levies were the largest contributing factor to total average income.

For the small-sized schemes in the sample, levies amounted to 97.68% (2008), 95.85% (2009) and 98.41% (2010) of total average income. Expressed in terms of rand per unit, total average levies for the small-sized schemes amounted to R4 578.10 in 2008, R4 579.33 in 2009 and R6 110.45 in 2010. Total average levies increased by 0.03% from 2008 to 2009 and by 33.44% from 2009 to 2010. The large increase from 2009 to 2010 is a cause for concern, and trustees should take note of this. The reason for the large increase could, however, not be identified with the limited financial data available.

Levies accounted for 84.61% (2008), 79.82% (2009) and 80.27% (2010) of total average income for medium-sized schemes in the sample. Expressed in rand per unit, total average levies for the medium-sized schemes amounted to R4 516.39 in 2008, R4 729.02 in 2009 and R5 363.90 in 2010. Total average levies increased by 4.71% from 2008 to 2009 and 13.43% from 2009 to 2010. As was the case for the small schemes, the large increase from 2009 to 2010 is a cause for concern, and trustees should take note of this. The reason for the large increase could, however, not be identified with the limited financial data available.

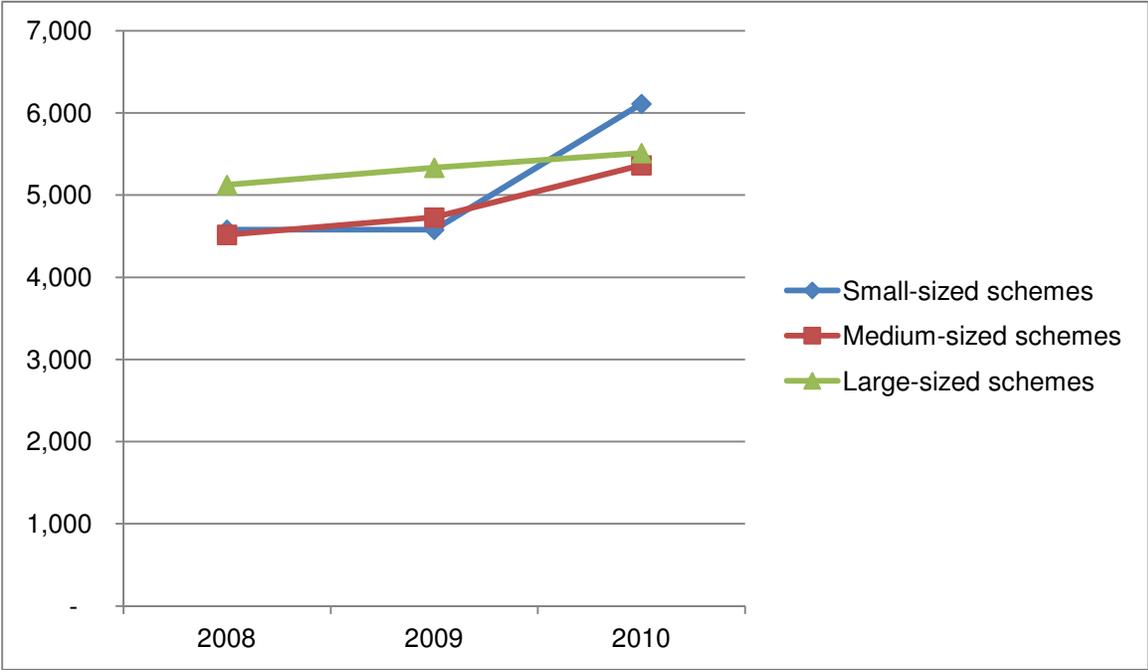
For the large-sized schemes in the sample, levies amounted to 82.24% (2008), 79.92% (2009) and 70.96% (2010) of total average income. Expressed in rand per unit, total average levies for the large-sized schemes amounted to R5 125.95 in 2008, R5 334.40

in 2009 and R5 512.10 in 2010. Total average levies increased by 4.07% from 2008 to 2009 and 4.33% from 2009 to 2010.

The same observation was made during the analysis of the various sizes of schemes as was made during the analysis of the total sample. Despite the general increasing trend in total average levies from 2008 to 2010, the fact that levies expressed as a percentage of total average income showed a decreasing trend over the three years is causing concern. Once again, seen in the light of the economic downturn that was experienced throughout South Africa as from 2008 and financial difficulties faced by many bodies corporate, one would certainly not want to see levies as a percentage of total average income decrease.

The following figure is a graphic representation of annual levies per unit analysed for the different sized schemes:

Figure 4.12 Analysis of annual average levies expressed in rand per unit for small, medium and large schemes in the sample

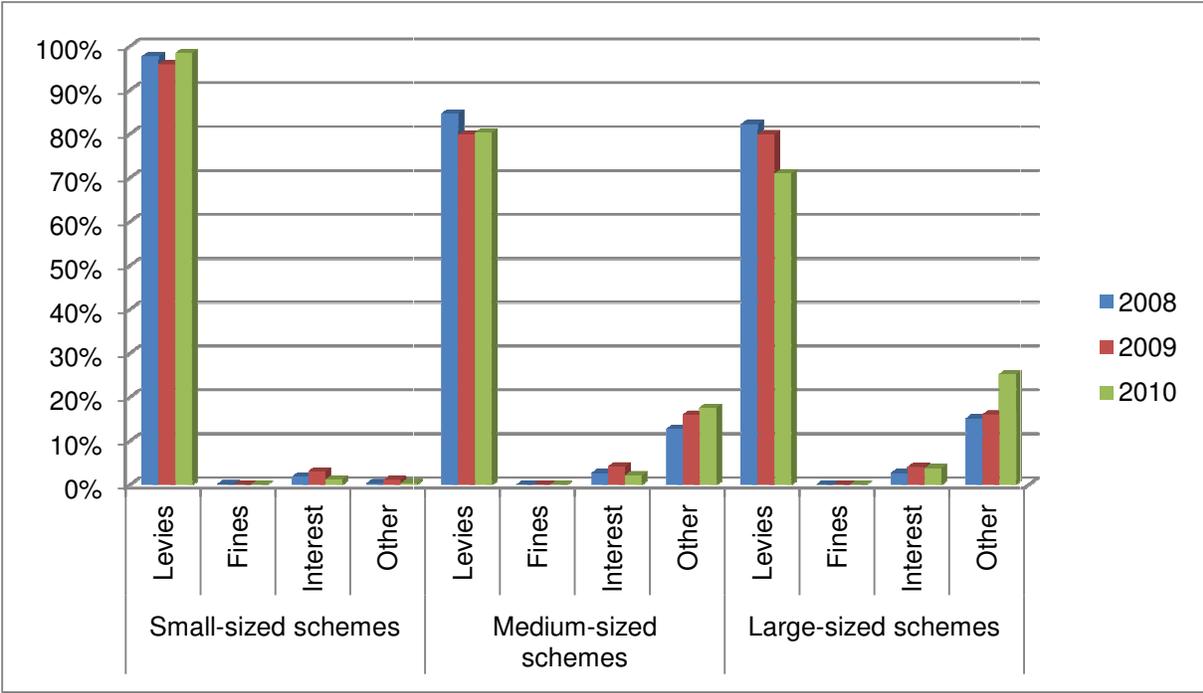


Fines were, as was the case for the total sample, by far the smallest single contributor, almost insignificant, and amounted to 0.14% (2008), 0% (2009) and 0% (2010) of total income for the small schemes in the sample, 0.03% (2008), 0.03% (2009) and 0.02% (2010) of total income for the medium schemes in the sample and 0% of total income over all three years for the large schemes in the sample.

Interest received accounted for 1.83% (2008), 3.04% (2009) and 1.23% (2010) of total average income for small schemes in the sample, 2.63% (2008), 4.17% (2009) and 2.15% (2010) of total average income for the medium schemes in the sample and 2.66% (2008), 4.06% (2009) and 3.80% (2010) of total average income for the large schemes in the sample.

Income items classified as “other income” accounted for 0.36% (2008), 1.11% (2009) and 0.36% (2010) of total average income for the small schemes in the sample, 12.73% (2008), 15.98% (2009) and 17.56% (2010) of total average income for the medium schemes in the sample and 15.11% (2008), 16.02% (2009) and 15.24% (2010) of total average income for the large schemes in the sample. The following is a graphic representation detailing the breakdown of income items:

Figure 4.13 Analysis of income categories as a percentage of total average income for small, medium and large schemes in the sample



4.4.2.4.2. ANALYSIS OF EXPENSES EXCLUDING TAXATION

Analysis of the total average expenses of the small-, medium- and large-sized schemes in the sample revealed that, as was the case for the total sample, the six largest

expenses were management fees, rates and taxes, audit fee, insurance, water and electricity and repairs and maintenance. These expenses accounted for a total of 86% (2008), 86% (2009) and 87% (2010) of average total expenses for the small schemes in the sample, 82% (2008), 79% (2009) and 75% (2010) of average total expenses for the medium schemes in the sample and 77% (2008), 79% (2009) and 71% (2010) of average total expenses for the large schemes in the sample.

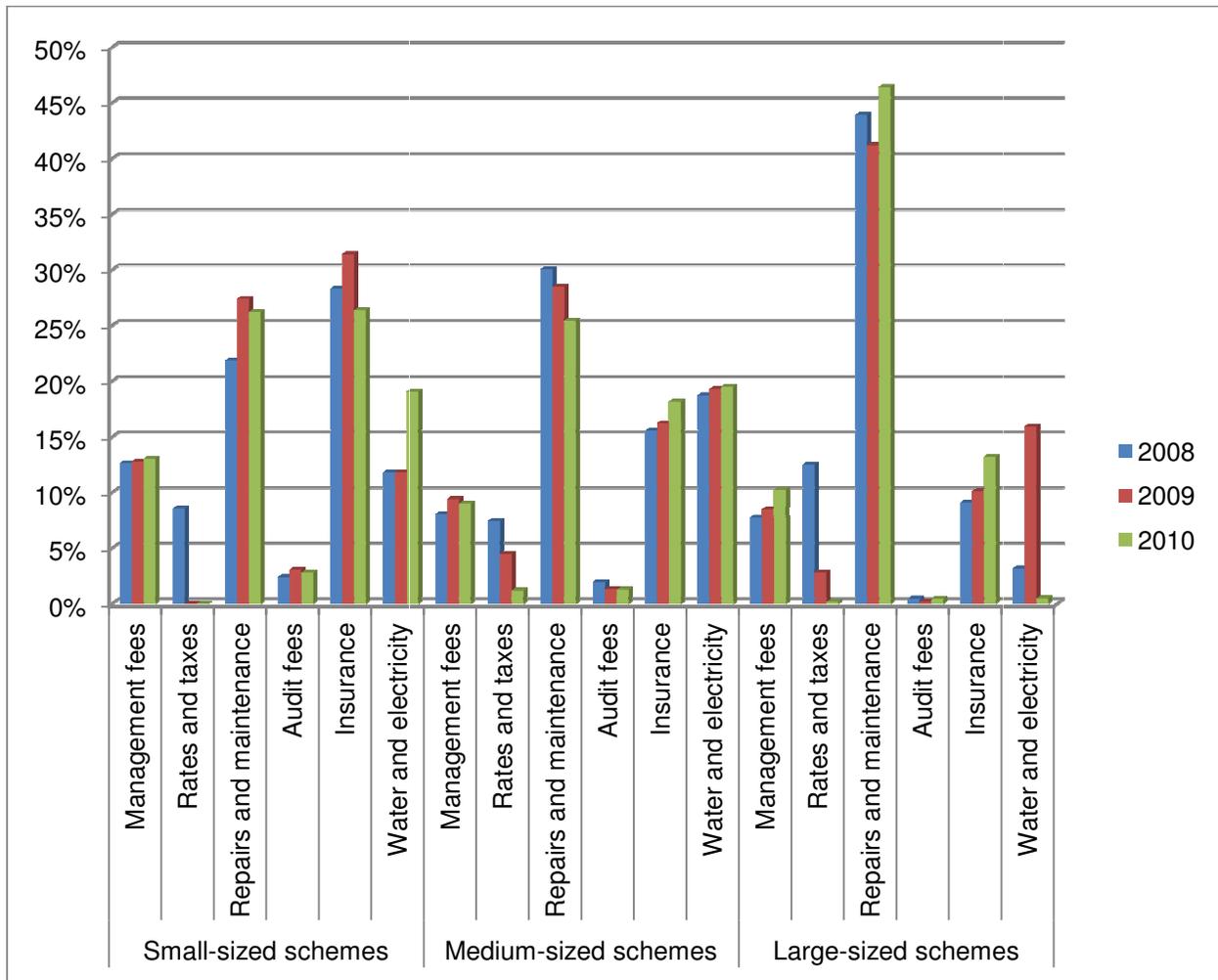
For the small-sized schemes in the sample, insurance was the largest expense at 28% (2008), 31% (2009) and 26% (2010) of average total expenses amounting to R9 664.01 (2008), R11 306.82 (2009) and R12 019.07 (2010). Water and electricity and management fees were the third and fourth largest expenses for the small schemes in the sample, followed by rates and taxes and audit fees.

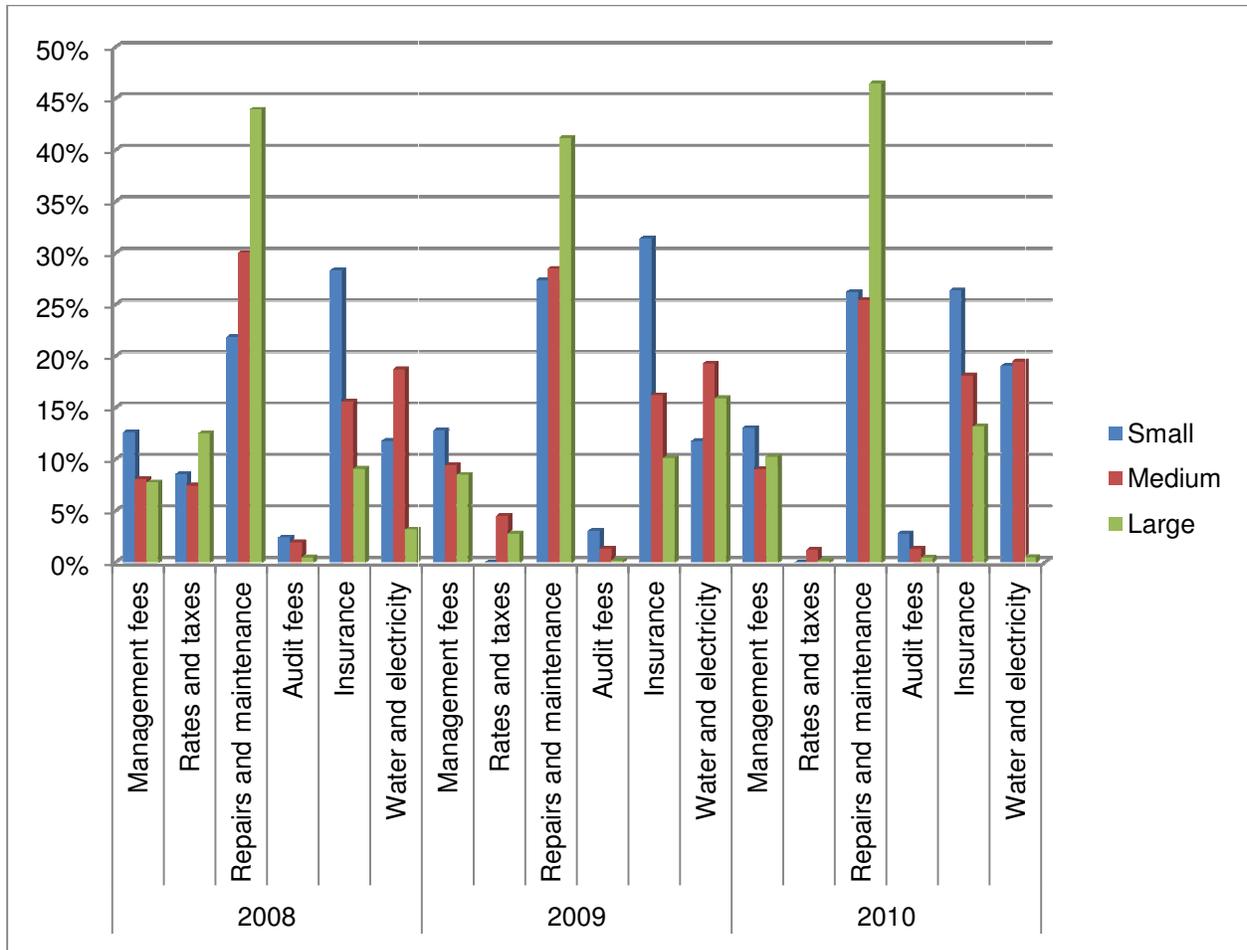
For the medium-sized schemes in the sample, water and electricity was the largest expense, which amounted to 19% of total average expenses for 2008 and 2009 and 20% of total average expenses for 2010. The average annual water and electricity expense for the medium-sized schemes in the sample amounted to R20 664.60 (2008), R22 544.13 (2009) and R25 767.48 (2010). Insurance and management fees were the third and fourth largest expenses for the small schemes in the sample, followed by rates and taxes and audit fees.

For the large schemes in the sample, repairs and maintenance was the single largest expense. Repairs and maintenance accounted for 44% (2008), 41% (2009) and 46% (2010) of total average expenses for the large schemes in the sample, at R262 372.27 (2008), R287 202.55 (2009) and R299 349.94 (2010). Water and electricity and management fees were the third and fourth largest expenses for the large schemes in the sample, followed by rates and taxes and audit fees.

As was the case for the total sample, the analysis amounts for rates and taxes for all the different sizes of schemes in the sample dropped significantly from 2008 to 2009 due to the change in legislation. The following is a graphic representation of the above in two different formats, for the sake of clarity and comparability:

Figure 4.14 The six largest expenses as a percentage of total expenses for the small, medium and large schemes in the sample in graph format





4.4.2.4.3. ANALYSIS OF TAXATION

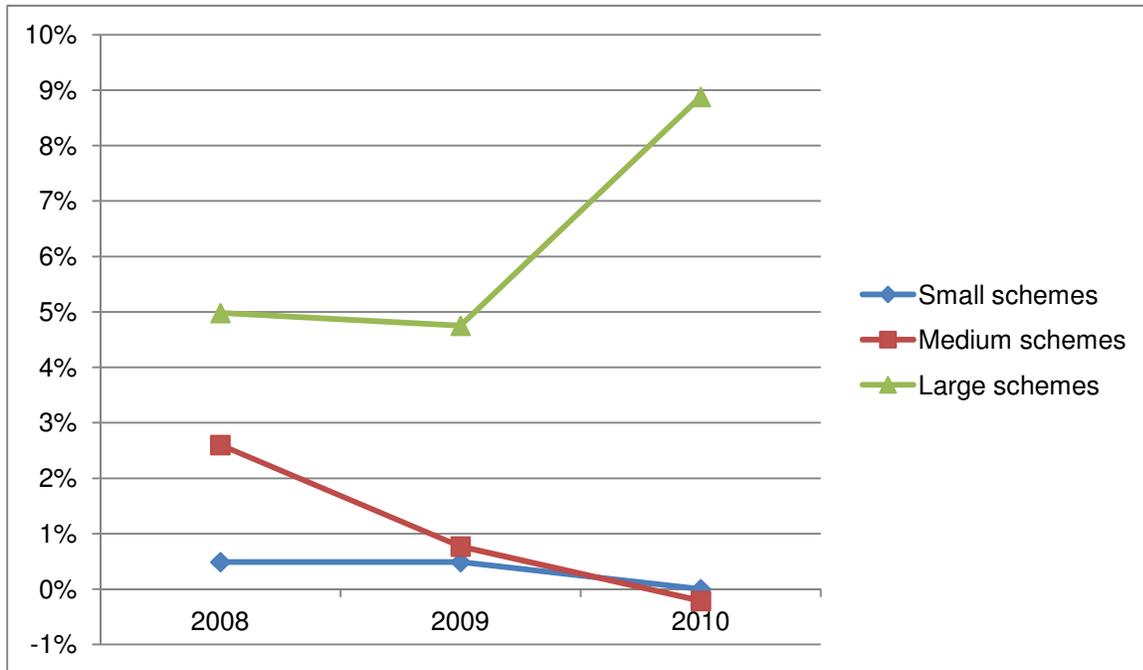
As mentioned in the discussion of the total sample, bodies corporate have very specific rules regarding tax.

For the small-sized schemes in the sample, the average amount of taxation expressed in rand terms was R166.38 (2008), R173.89 (2009) and R0 (2010). Total average taxation amounted to approximately 0.48% (2008), 0.49% (2009) and 0% (2010) of total average income. For the medium-sized schemes in the sample, taxation accounted for 0.78% (2008), 0.72% (2009) and -0.20% (2010) at amounts of R886.81 (2008),

R902.65 (2009) and –R281.74. For the large-sized schemes in the sample, the average amount of taxation expressed in rand terms was R29 774.99 (2008), R33 106.45 (2009) and R57 224.78 (2010). Expressed as a percentage of total average income, taxation for the large schemes in the sample amounted to approximately 4.28% (2008), 4.44% (2009) and 6.60% (2010).

The significant drop in taxation over the three years for the small and medium schemes in the sample can probably be attributed to the introduction of the R50 000 basic threshold exemption by SARS as from January 2009, which was explained in section 4.4.2.2.3. Further analysis of the large schemes in the sample showed that these schemes had much larger amounts non-levy income in 2010 (such as investment income, rental income and penalty income) than the small and medium schemes. As a result, the effect of the above-mentioned legislation on the large schemes was not that evident on the ratios. The following graph is a representation of the above information:

Fig. 4.15 Taxation indicated as a percentage of total average income for small, medium and large schemes



4.4.2.4.4. ANALYSIS OF SURPLUS

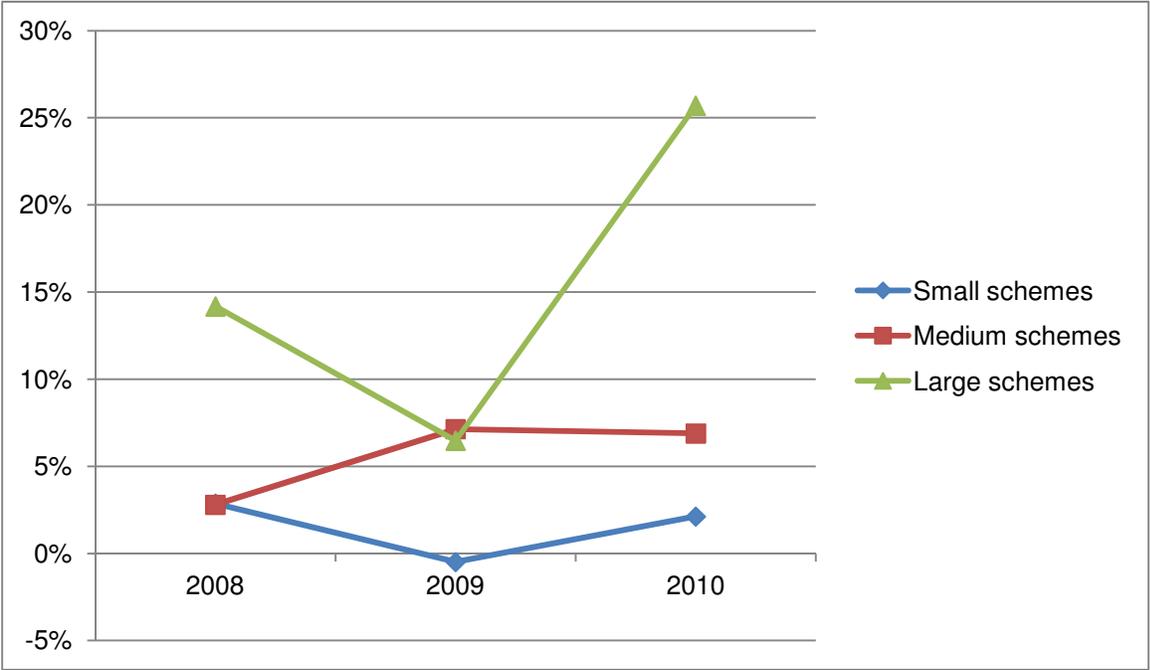
For the small-sized schemes in the sample, the average surplus/deficit amount (total income less total expenses) for the total sample expressed in rand was a surplus of R1 005.20 (2008), a deficit of R176.69 (2009) and R988.29 (2010). Expressed as a percentage of total income the surpluses amounted to 2.86% (2008), -0.49% (2009) and 2.12% (2010) of average total income. In 2008, 5 of the 10 small schemes in the sample showed a deficit and 5 showed a surplus. In 2009, 7 schemes showed a deficit and 3 showed a surplus, and in 2010, 3 showed a deficit in 7 showed a surplus.

For the medium-sized schemes in the sample, the average surplus/deficit amount (total income less total expenses) for the total sample expressed in rand was a surplus of R3 179.34 (2008), R8 985.57 (2009) and R9 785.19 (2010). Expressed as a percentage of total income the surpluses amounted to 2.80% (2008), 7.14% (2009) and 6.89% (2010) of average total income. In 2008 as well as in 2009, 14 of the 46 small schemes in the sample showed a deficit and 32 showed a surplus. In 2010, 16 of the 46 showed a deficit in 30 showed a surplus.

For the large-sized schemes in the sample, the average surplus/deficit amount (total income less total expenses) for the total sample expressed in rand was a surplus of R98 703.84 (2008), R48 285.89 (2009) and R222 927.03 (2010). Expressed as a percentage of total income the surpluses amounted to 14.18% (2008), 6.48% (2009) and 25.70% (2010) of average total income. In 2008 and again in 2010, none of the 3 large schemes in the sample showed a deficit. In 2009, 2 of the three large schemes showed a deficit and one showed a surplus.

From the above analysis, the conclusion can be drawn that, on average, the large schemes in the sample showed larger surpluses as a percentage of their total average income than their small and medium counterparts. The figure below is a graphic representation thereof:

Fig. 4.16 Surplus/deficit indicated as a percentage of total average income for small, medium and large schemes



4.4.2.4.5. ANALYSIS OF GROWTH

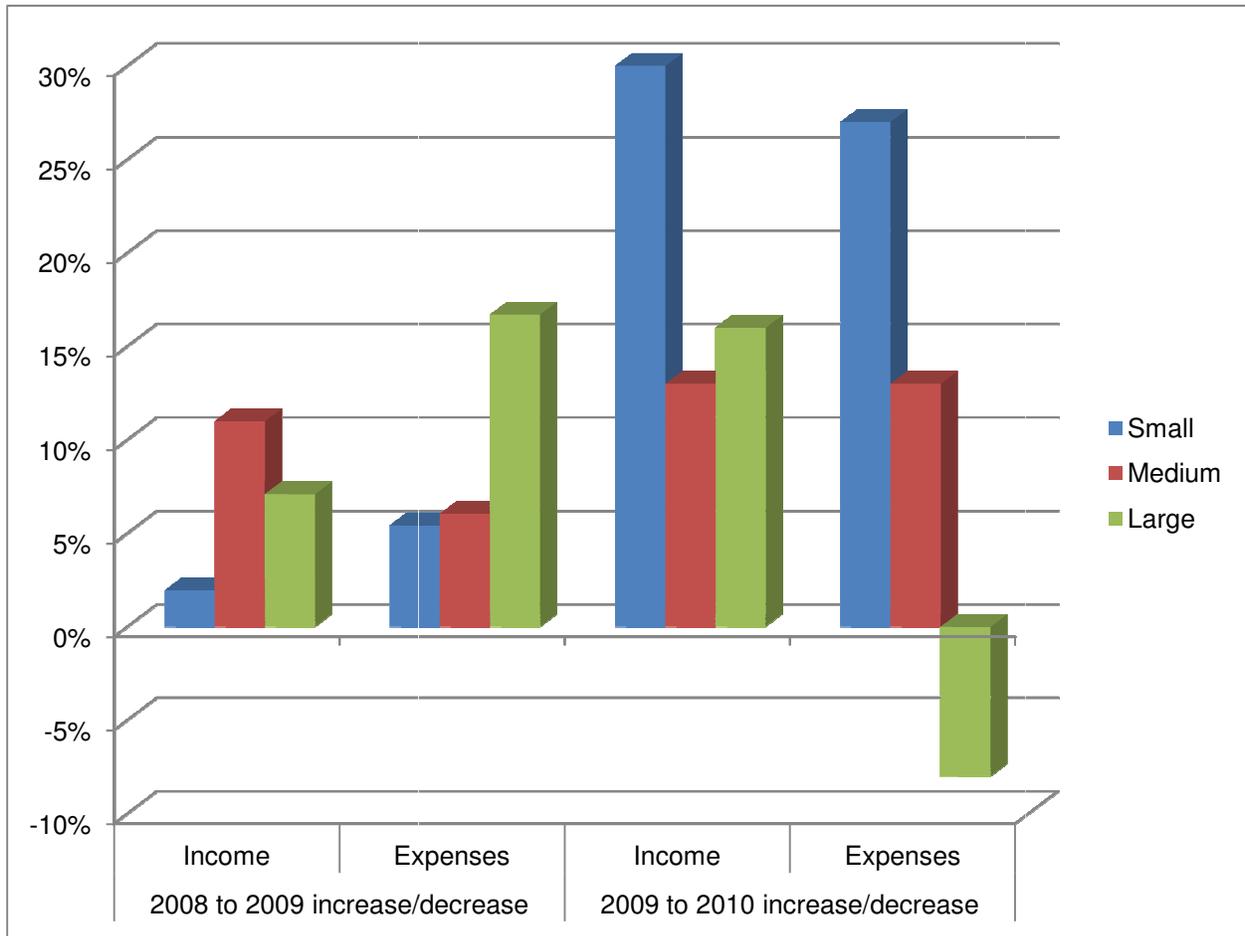
For the small-sized schemes in the sample, the financial figures showed an increasing trend from year to year. From 2008 to 2009 there was an increase in total expenses of 5.43% and from 2009 to 2010 there was a 27% increase in total average expenses. From 2008 to 2009 there was a 1.94% increase in average total income and from 2009 to 2010 there was a 30% increase in average total income.

For the medium-sized schemes in the sample selected, the financial figures showed an increasing trend from year to year. From 2008 to 2009 there was an increase in total expenses of 6.04% and from 2009 to 2010 there was a 13% increase in total average

expenses. From 2008 to 2009 there was a 10.99% increase in average total income and from 2009 to 2010 there was a 13% increase in average total income.

For the large-sized schemes in the sample, there was an increase in total expenses of 16.70% in total expenses from 2008 to 2009, and from 2009 to 2010 there was an 8% decrease in total average expenses. From 2008 to 2009 there was a 7.09% increase in average total income and from 2009 to 2010 there was a 16% increase in average total income. The figure below illustrates the growth/decline:

Figure 4.17 Growth/decline of items on the statement of comprehensive income for small, medium and large schemes in the sample



No clear trends could be identified during the comparison of the growth/decline in balance sheet items of the small, medium and large schemes in the sample.

For the small schemes in the sample, trade and other receivables showed a decline of 4.56% from 2008 to 2009 and an increase of 120.25% from 2009 to 2010. For the medium schemes in the sample, trade and other receivables showed an increase of 3.185% from 2008 to 2009 and 30.01% from 2009 to 2010. For the large schemes in

the sample, trade and other receivables increased by 151.67% from 2008 to 2009 and declined by 19.43% from 2009 to 2010.

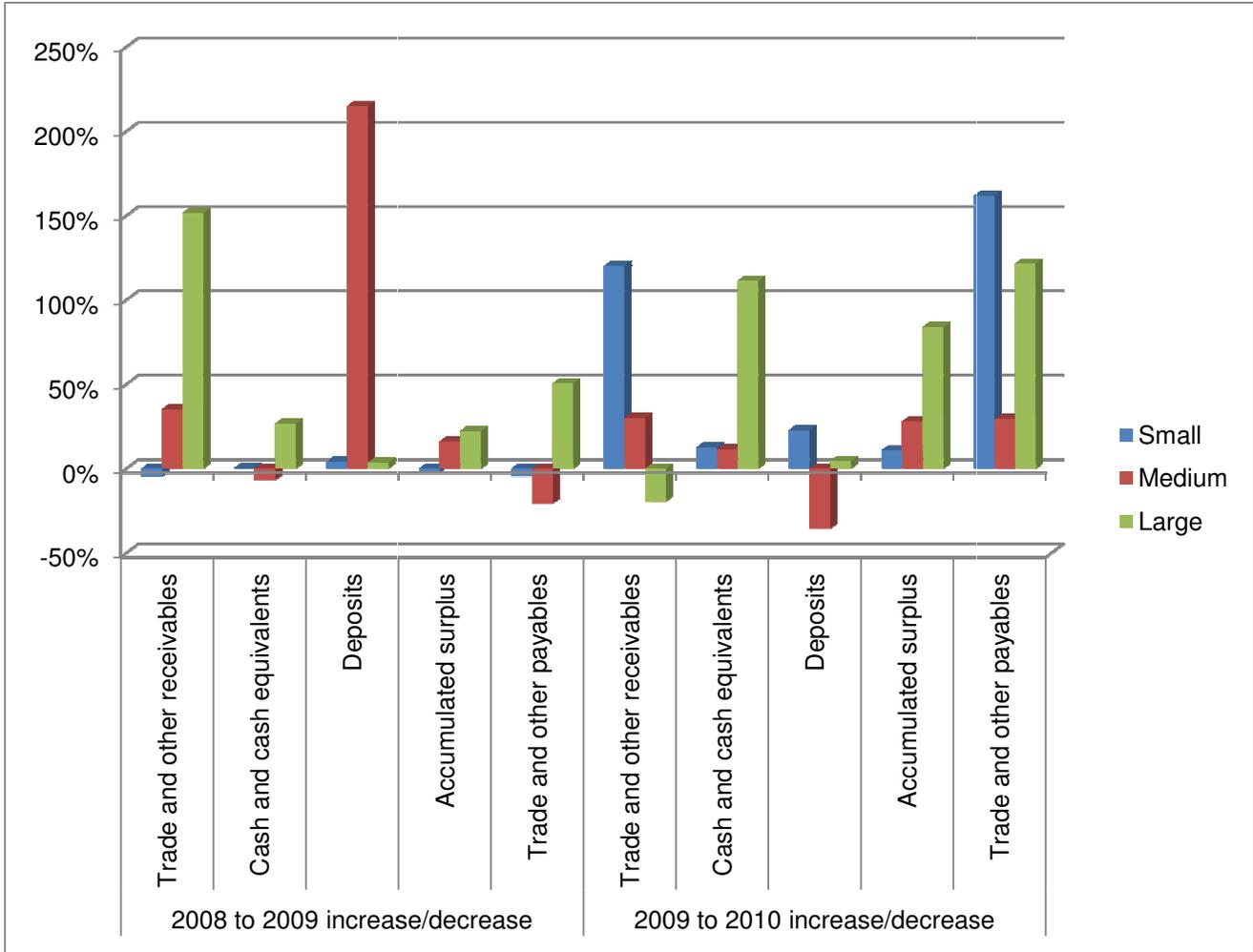
For the small schemes in the sample, cash and cash equivalents showed an increase of 0.28% from 2008 to 2009 and an increase of 12.58% from 2009 to 2010. For the medium schemes in the sample, cash and cash equivalents showed a decline of 6.68% from 2008 to 2009 and an increase of 11.46% from 2009 to 2010. For the large schemes in the sample, cash and cash equivalents increased by 26.67% from 2008 to 2009 and 111.31% from 2009 to 2010.

Deposits increased by 4.12% from 2008 to 2009 for the small schemes in the sample, and by 22.87% from 2009 to 2010. For the medium schemes in the sample, deposits showed an increase of 214.81% from 2008 to 2009 and an decline of 35.45% from 2009 to 2010. For the large schemes in the sample, deposits increased by 3.74% from 2008 to 2009 and 4.42% from 2009 to 2010.

The accumulated surplus of the small schemes in the sample declined by 2.13% from 2008 to 2009, and increased by 10.73% from 2009 to 2010. The accumulated surplus of the medium schemes in the sample increased by 16.06% from 2008 to 2009, and increased by 27.95% from 2009 to 2010. For the large schemes in the sample, accumulated surplus increased by 22.23% from 2008 to 2009 and by 83.96% from 2009 to 2010. In 2008, one of the small schemes in the sample showed an accumulated shortage. In 2009, 3 small schemes showed an accumulated shortage, and in 2010, one small scheme showed an accumulated shortage. In 2008 and 2009, 4 of the medium schemes in the sample had an accumulated shortage, compared to 5 schemes in 2010. None of the large schemes showed an accumulated shortage from 2008 to 2010.

The small schemes in the sample showed a decline in trade and other payables amounting to 4.61% from 2008 to 2009 and an increase of 161.74% from 2009 to 2010. The medium schemes in the sample showed a decline in trade and other payables of 20.67% from 2008 to 2009 and an increase of 29.49% from 2009 to 2010. The large schemes in the sample showed an increase of 50.55% in trade and other payables from 2008 to 2009 and an increase of 121.49% from 2009 to 2010. The figure below is a graphic representation of the above-mentioned analysis:

4.18 Growth/decline of items on the statement of financial position for small, medium and large schemes in the sample

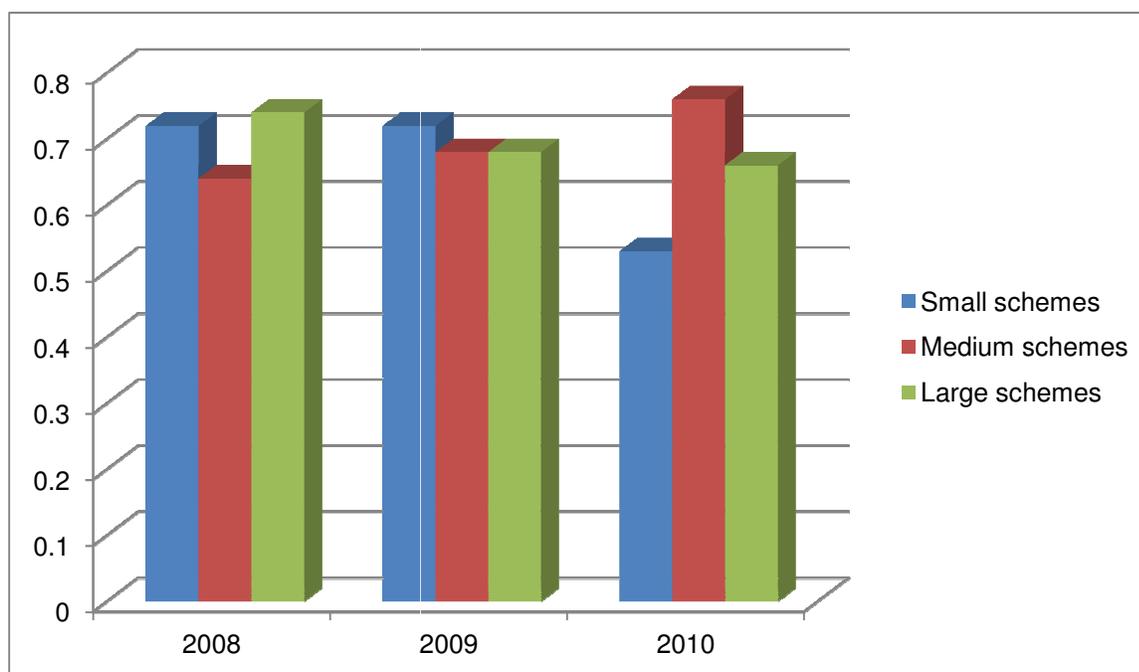


4.4.2.4.6. FINANCIAL STRENGTH

The same ratios were calculated for the small, medium and large schemes as was the case for the total samples. The following financial strength ratios were calculated: accumulated surplus to total assets, total assets to total liabilities, current assets to current liabilities, receivables to levies, payables to expenses, receivables to total assets, cash to total assets and bad debts to receivables.

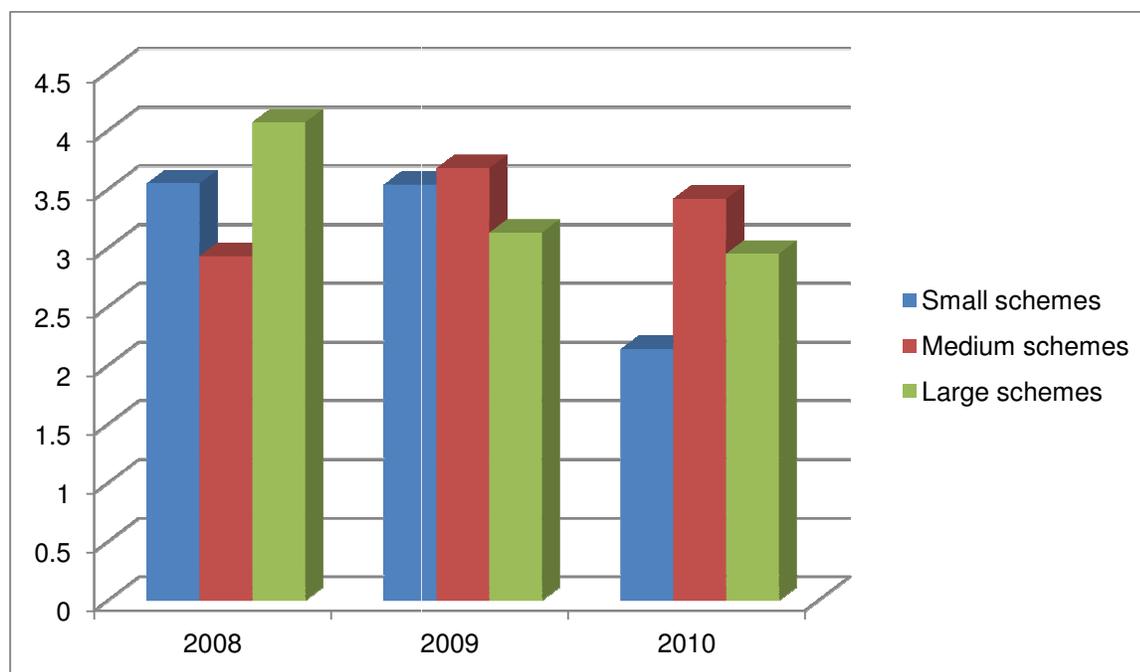
The ratio of accumulated surplus to assets was calculated instead of the traditional total shareholders' interest to total assets ratio (Service, 2012, p. 1032). The ratio shows to what extent the assets of the body corporate are financed by way of accumulated funds. The ratios for the small schemes in the sample were 0.72:1 in 2008 and 2009 and 0.53:1 in 2010. For the medium schemes in the sample, the ratios were 0.64:1 (2008), 0.68:1 (2009) and 0.76:1 (2010). For the large schemes in the sample, the ratios were 0.74:1 (2008), 0.68:1 (2009) and 0.66:1 (2010). The medium schemes showed an increasing trend over the three years and the small and large schemes showed a decreasing trend. So far, no academic research has been done on what the accepted norms should be for the sectional title industry and therefore no benchmarks were available. The following figure represents the analysis in the form of a graph:

Fig. 4.19 Ratio of accumulated surplus to assets for small, medium and large schemes in the sample



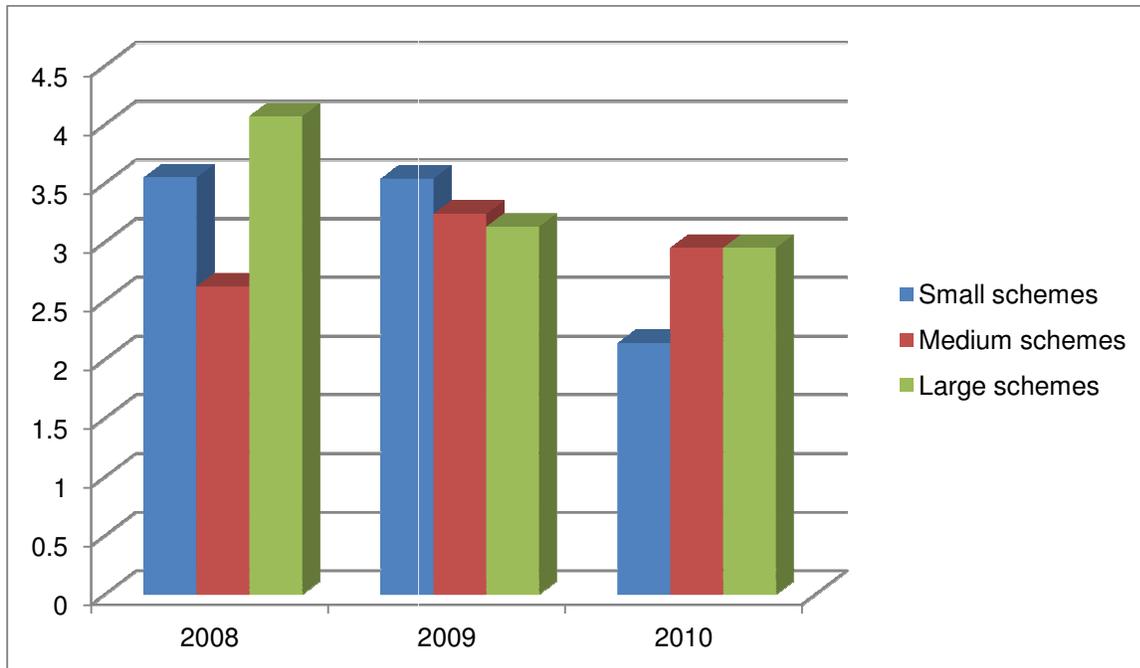
The solvency ratio calculated as total assets to total liabilities show to what extent liabilities are covered by assets. It is also an indication of whether an entity will be able to honour obligations in future. Using the average total assets and average total liabilities the average ratios for the small schemes in the sample showed a declining trend of 3.55 (2008), 3.54 (2009) and 2.14 (2010). The average ratios for the medium schemes in the sample were 2.93 (2008), 3.68 (2009) and 3.42 (2010). As was the case for the small schemes, the large schemes in the sample showed a declining trend of 4.07 (2008), 3.13 (2009) and 2.95 (2010). Despite the declining trend identified for some schemes, the total liabilities were, on average, still covered more than three times by the total assets of the bodies corporate. There seems to be no great cause for concern regarding the solvency of the schemes. The following figure represents the above information in the form of a graph:

Fig. 4.20 Solvency ratios for small, medium and large schemes in the sample



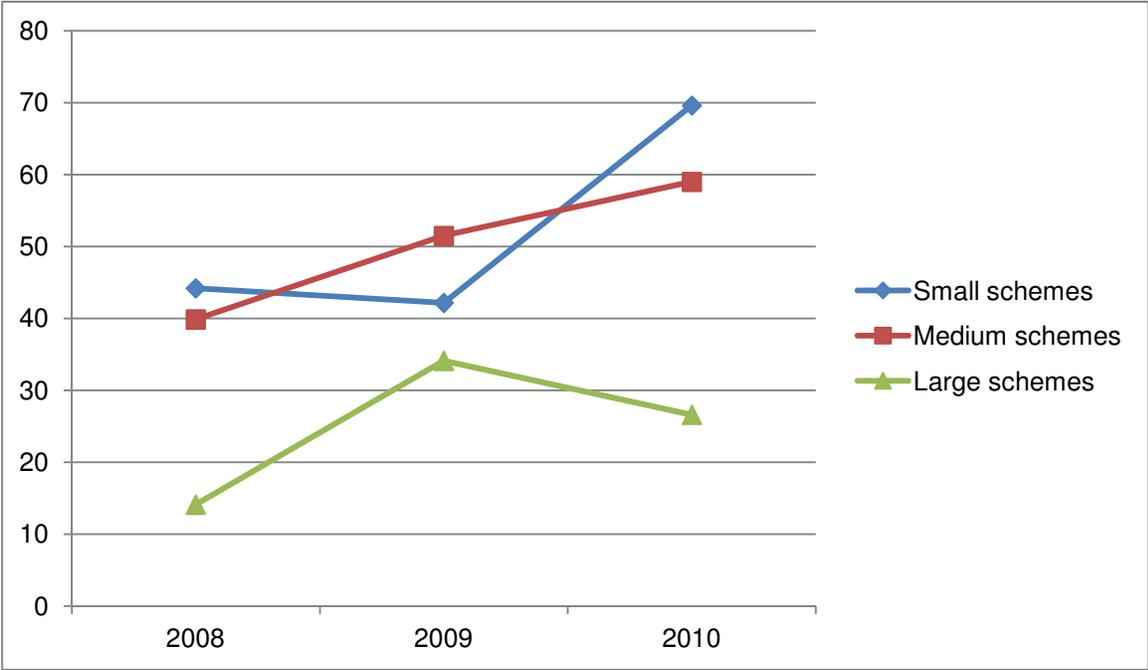
Regarding liquidity, the ratio of current assets to current liabilities is an indication of the ability of an enterprise to repay short-term debts as they become due. The ratio is usually called the current ratio and refers to the availability of cash in the near future after taking into account the financial commitments for a specific period. If a ratio is 2:1 or higher, it is usually considered to be good (Kew & Watson, 2012, pp. 568-569; Koen & Oberholster, 1999, p. 53). The average current ratio for the small schemes in the sample showed a declining trend of 3.55 (2008), 3.54 (2009) and 2.14 (2010). For the medium schemes in the sample, the current ratio was 2.62 (2008), 3.24 (2009) and 2.95 (2010). The large schemes in the sample also showed a declining trend at 4.07 (2008), 3.13 (2009) and 2.95 (2010). Despite the declining trend for the small and large schemes in the sample the averages for the different sizes of schemes over the three years indicated that the current liabilities were covered between two and four times by the current assets, and this is also well above the accepted norm of 2:1. The following figure is a graphic representation of the various liquidity ratios:

Fig. 4.21 Liquidity ratios for small, medium and large schemes in the sample



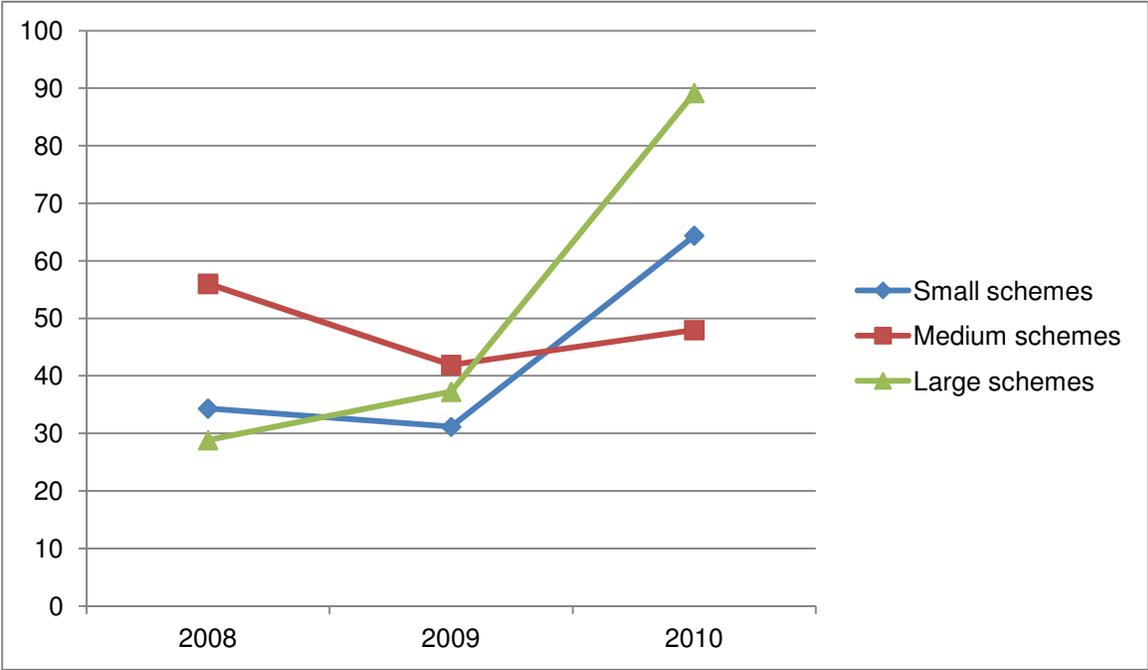
For the different sizes of schemes in the sample the total average debtors' collection period was calculated using total average levies instead of sales as per the traditional ratio. For the small schemes in the sample, the collection period amounted to 44.20 days in 2008, 42.17 days in 2009 followed by a sharp increase to 69.61 days in 2010. For the medium schemes in the sample, there was a definitive increasing trend in the debtors collection period from 39.87 days in 2008 to 51.47 days in 2009 to 59.00 days in 2010. The debtors' collection period for the large schemes in the sample was much shorter than for the small and medium schemes, at 14.11 days in 2008, 34.11 days in 2009 and 26.60 day in 2010. The increasing trend in the average receivables collection period of the small and medium schemes may be indicative of possible problems regarding the collection of levies. The reason for the shorter collection period of the large schemes could not be determined with the available financial data. The following figure is a graphic representation of the average debtors' collection period for the different sizes of schemes in the sample:

Fig. 4.22 Average debtors collection period in days for small, medium and large schemes in the sample



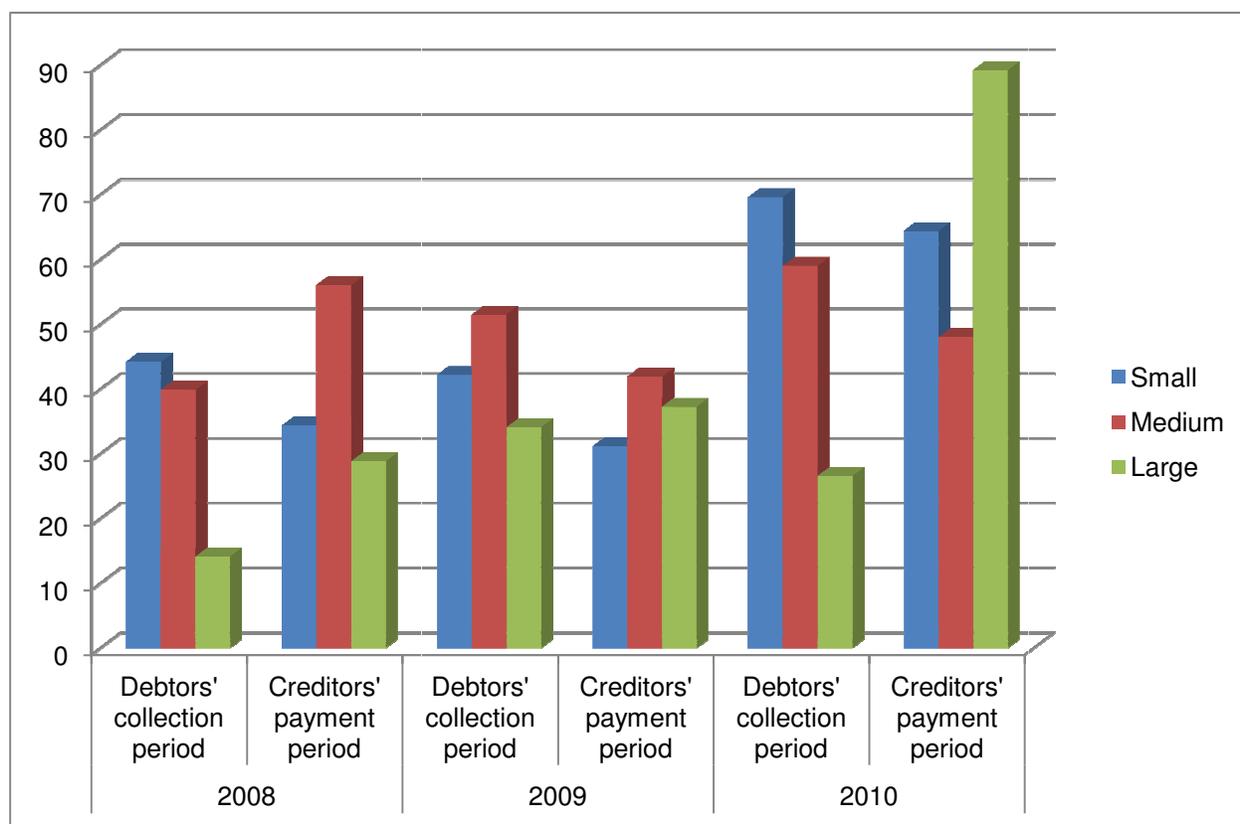
For the sample selected, the total average creditors’ payment period was calculated using total expenses instead of credit purchases as per the traditional ratio. For the small schemes in the sample, the creditors’ payment period was 34.33 in 2008, 31.15 in 2009 and 64.39 in 2010. For the medium schemes in the sample, the creditors’ payment period was 56.01 in 2008, 41.90 in 2009 and 47.98 in 2010. For the large schemes in the sample, the creditors’ payment period was 28.86 in 2008, 37.24 in 2009 and 89.20 in 2010. The reason for the large increase in the creditors’ payment period of the small and large schemes from 2008 to 2010 is a great cause for concern, but could not be determined with the available financial data. Trustees should take note of this increase. The following figure depicts the average creditors’ payment period in days for the different sizes of schemes:

Fig. 4.23 Average creditors' payment period in days for small, medium and large schemes in the sample



Every year, the creditors' payment period for the small schemes in the sample was a few days shorter than the debtors' collection period. In 2008, the creditors' payment period for the medium schemes were longer than the debtors' collection period, but for 2009 and 2010, the creditors' payment was shorter than the debtors' collection period. Every year, the creditors' payment period for the large schemes in the sample was longer than the debtors' collection period. The following figure is a comparison between debtors' collection periods and creditors' payment periods for the different sizes of schemes:

Fig. 4.24 Comparison of debtors' collection period and creditors' payment period in days for small, medium and large schemes in the sample



4.5. CONCLUSION

The Chapter commenced with the background to accounting and financial reporting in South Africa. The sections in the Sectional Titles Act relating to accounting and reporting aspects of sectional title were discussed. In various discussions of the legal requirements in the chapter, vagueness or ambiguity was identified in the legislation. In many cases, the legislation contains wording that is not true to the acknowledged subject terminology of, for example, IFRS. Parts of the legislation also make use of outdated terminology.

Concern was raised as to the applicability of currently available accounting standards, and the aspect of a possible tailor-made accounting standard for sectional titles was addressed. Many users of body corporate financial statements are probably “unsophisticated” and have no knowledge of International Financial Reporting Standards. It is an open question whether applying IFRS is useful, especially for small and medium schemes.

In the Chapter general observations and findings were discussed as part of the analysis of the financial ratios of a sample of 60 sets of annual financial statements of bodies corporate over a period of three years. The sample was analysed as a whole, and also split into small, medium and large schemes. Very little, if any, academic research has been done on the sectional title industry, and the mentioned observations and findings can be used as a starting point and benchmarks in creating industry standards.

The next chapter contains the results of the empirical study which was done by means of questionnaires and interviews with various role players in the sectional title industry.

CHAPTER 5 – EMPIRICAL STUDY OF THE SECTIONAL TITLE INDUSTRY IN SOUTH AFRICA

*“Once upon a time, when the world was just a pancake
Fears would arise, that if you went too far, you'd fall
But with the passing of time, it all became more of a ball
We're as sure of that
As we all once were, when the world was flat...”*

- Dodo, Dave Matthews

5.1. INTRODUCTION

In Chapter 1 of the study, it was mentioned that the sectional title industry plays a vital role in addressing the housing problem in South Africa. It was also indicated that very little, if any, research has so far been done on the industry, and various unclear aspects, problems and challenges has been identified and discussed in the study. Against this background, and in order to address some of the problems, ambiguity and challenges, questionnaires were developed (see Annexures A to F) to determine the opinions of the most important role players in the sectional title industry, limited to the Bloemfontein area in South Africa.

As mentioned in section 1.6.4. of Chapter 1, the empirical study was done by way of standardised interviews, incorporating the use of properly structured questionnaires. For the purposes of this study, the interviewees were divided into a sample of three main groups of role players. The first group being chairmen of bodies corporate of sectional title schemes, the second group managing agents of sectional title schemes, and the third group accounting and auditing professionals involved in the sectional title industry.

The chapter will start with the opinions of chairmen of bodies corporate, followed by the viewpoints of the managing agents and that of the accountants and auditors of sectional title schemes. The chapter will conclude with an overview of the empirical findings as well as a summary of the chapter.

5.2. OPINIONS OF CHAIRMEN OF BODIES CORPORATE

In this section, the results of the information from the questionnaires and interviews with chairmen of bodies corporate will be discussed. These aspects will be discussed under the following headings: operations, problems and risks, managing agents, meetings and financial matters.

5.2.1. OPERATIONS

The 5 chairmen interviewed had varying numbers of units, namely 5, 6, 17, 42, 47 in their complexes respectively. The boards of trustees of which they were chairmen also varied in size. One of the five (20%) chairmen stated that he used to be the only trustee for a period of 3 years, but that there are currently four trustees. Three of the five (60%) chairmen said that their boards consisted of 3 trustees, and one (20%) chairman stated that the board consisted of 4 trustees. Four of the five (80%) chairmen were of the opinion that the majority of the trustees should be residents of the scheme, as they are more in touch with the day-to-day problems and how the scheme should be managed.

The chairmen differed in their opinions on what the optimal number would be for a well-functioning board of trustees. One chairman said 3 to 8 trustees would be sufficient, depending of the size of the scheme. Two chairmen were of the opinion that 3 to 5

would be sufficient, depending on the size of the scheme. One chairman said that 5 trustees would be sufficient and the remaining one said 4 trustees is an optimal number.

All of the chairmen interviewed (100%) stated that the trustees serving on the boards of their bodies corporate received no remuneration. They stated that if they as chairmen incurred expenses on behalf of the body corporate, they are reimbursed for the expenses incurred. All of the chairmen interviewed received a honorarium of between R400 and R1 200 per month. All of them were of the opinion that trustees as well as chairmen should receive some form of remuneration. The concept of remuneration was also discussed in section 1.3. of Chapter 1 and section 5.3.3. of this chapter.

Three of the five (60%) chairmen interviewed said that they were entirely up to date with the latest stipulations of the Sectional Titles Act. One chairman (20%) said the he is not up to date, and the remaining one (20%) said that he does not know all the relevant legislation, but it trying to familiarise himself with it.

Four of the five (80%) chairmen interviewed stated that there is a definite need for sectional title training courses for trustees as well as chairmen. They mentioned, however, that the available training courses provided by some managing agents and the National Association of Managing Agents (NAMA) are too expensive and time-consuming. One chairman (20%) said that he does not see a need for trustee training.

5.2.2. PROBLEMS AND RISKS

According to the results of the interviews, the single biggest problem experienced by chairmen of bodies corporate is residents not adhering to management and conduct rules. All of the chairmen (100%) stated that they spend most of their time dealing with

complaints regarding transgression of rules, such as parking problems, pets, unauthorised changes and extensions to units and noise. They were all of the opinion that the trustees were very unpopular in their complexes due to the fact that they enforced the management and conduct rules. Two of the five (40%) chairmen stated that they think the problem with non-adherence to rules stems from owners, and sometimes even fellow trustees, being uninformed and ignorant, not understanding the way a body corporate functions. This viewpoint was also shared by managing agents and auditors interviewed, as discussed in sections 5.3.2. and 5.4.1.

Three of the five (60%) chairmen interviewed were of the opinion that uninvolved owners are the biggest problem experienced by them, especially non-resident owners. They stated that the owners were only interested in receiving rental income and did not care about the day-to-day operations of the complex.

Another frustration, which is experienced by all chairmen (100%), and that was also mentioned by managing agents as well as accounting practitioners in sections 5.3.2. and 5.4.2 below, regards local authorities. The biggest problems with local authorities are a lack of communication, poor municipal service delivery, account estimates, corrections on statements, inaccurate balances and incorrect allocations on statements. One chairman mentioned the example of a water account of over R40 000 which was received by the owner of a unit in a specific month. No results were achieved with queries and complaints to the local authority and the owner had to settle the full amount.

One of the chairmen (20%) mentioned that managing agents receive kickbacks from service providers, such as insurance institutions and service contractors. He said that managing agents are not always acting in the best interest of the bodies corporate, and simply use or suggest the services of institutions from which they receive kickbacks.

Only three of the five (60%) chairmen had any experience with developers. All three said that the developers cut corners and used cheap materials during the building process, and did not want to take responsibility afterwards. One chairman mentioned that the developers did not install any geyser switches within a certain distance from the geysers according to government regulation. The trustees only realised this after receiving a complaint from an owner who wanted to sell his unit, who could not get an electricity clearance certificate because of this problem. The chairman said that they had to threaten the developer with legal action before receiving a response. Another chairman stated that they waited for three years to receive electricity certificates from the developers. Problems with developers were also mentioned by managing agents in section 5.3.2. below.

A concern raised by two of the five (40%) chairmen was also mentioned by the accounting and auditing practitioners in section 5.4.3. below. The chairmen had a problem with the fact that the managing agent did not open a separate bank account for the body corporate and that all levies had to be deposited in the bank account of the managing agent. They stated that the body corporate never earned any interest on surplus funds and that the managing agent simply told him that it is generally accepted practice and that is the way the system is set up. One of the chairmen said that after various requests the managing agent opened an “investment” account for the body corporate. The managing agent transfers surplus funds to this account after doing his calculations and reconciliations. The chairman said that there are large amounts of money in the bank account of the managing agent, since levies are received by the first week of a month and creditors are only paid days or even weeks later. He said that the body corporate never receives any interest on these funds, since the managing agent only pays the surplus funds over at the end of the month at his own discretion. The chairman also added that the managing agent earns “loyalty points” from his bank on the balances and transactions of this bank account for his own benefit. This matter will be dealt with in more detail in section 5.4.3 below.

According to two of the five (40%) chairmen they have noticed that many residents are falling behind on their payments. They also stated that they regard debt collection as a great challenge. The problem was also mentioned by the managing agents in section 5.3.2. below.

5.2.3. MANAGING AGENTS

All of the chairmen interviewed (100%) stated that their bodies corporate made use of the services of a managing agent. The managing agents assisted the bodies corporate with the day-to-day management of the complex, administrative tasks, preparation of budgets and financial statements, collection of levies, etc.

During the interviews the chairmen were asked to rate the services of their managing agent, with the options ranging from very satisfied to very dissatisfied. Two of the five (40%) chairmen stated that they were satisfied with the services of the managing agents, while three of the five (60%) chairmen said that they were not satisfied with the services of the managing agents. The dissatisfied chairmen stated that making use of a managing agent is very expensive, and that they did not always feel that they were getting value for their money and that the managing agent is not prepared to walk the extra mile for them. These chairmen also added that the managing agents do not seem to care about smaller bodies corporate and did not give the necessary attention to their needs. These chairmen stated that even though they are not satisfied with the service they receive from their managing agent, they cannot operate without one, and that other available managing agents have an even worse reputation. The dissatisfied chairmen also mentioned that the lack of continuity of staff members at managing agents were frustrating. This viewpoint was shared by managing agents and audit practitioners in sections 5.3.2. and 5.4.2. below.

Two of the five (40%) chairmen stated that they had no idea how their managing agents calculated their management fees, while the other 3 (60%) said that they knew how it was calculated.

All of the chairmen (100%) stated that they have never changed from one managing agent to another, and that they have made use of the services of their managing agent since they became involved in the body corporate. This comment opposes the viewpoints of the managing agents as discussed in sections 5.3.2. and 5.3.8., as well as those of the auditors in section 5.4.2.

All of the chairmen (100%) stated that the most important factor to take into account when deciding on a managing agent is service delivery and a genuine interest in the complex. This is an interesting comment, because, as mentioned above, 60% of the chairmen were not satisfied with the service they received from their managing agents.

According to two of the five (40%) chairmen another factor that they consider as important when choosing a managing agent, is that the managing agent must be trustworthy regarding the finances of the body corporate. One chairman (20%) said that affordability of the management fees is important.

5.2.4. MEETINGS

According to all of the chairmen, the annual general meeting (AGM) of their body corporate is poorly attended, an opinion shared by the managing agents interviewed in section 5.3.7. below. All of the chairmen stated that their annual general meetings (AGMs) never have a quorum and have to be postponed, despite various communication efforts such as registered mail and sms-messages. Two of the five

(40%) chairmen complained that there are high costs involved in postponing an AGM, since the managing agent charges them an after-hours meeting fee for each meeting, including the postponed one.

Another comment by the chairmen, which corresponded with what the managing agents said in 5.3.7., was that one of the biggest problems at AGMs is the approval of budgets. The chairmen stated that increases in budgets and the resulting levies are always met with negativity. One chairman mentioned that everybody wants to stay in a well-maintained complex, but nobody wants to contribute financially.

As was mentioned by some managing agents in 5.3.7., the chairmen interviewed also stated that owners do not adhere to proper meeting procedures during AGMs, and that owners regularly want to discuss operational matters which fall outside the scope of the agenda.

Four of the five (80%) chairmen stated that the election of trustees at the AGM is usually problematic, because very few people want to serve as trustees.

One of the five (20%) chairmen said that they have monthly trustee meetings, two of the five (40%) chairmen said that the board of trustees meet quarterly, and the other two chairmen (40%) stated that the board of trustees only meet once a year, after the AGM.

All of the chairmen (100%) stated that there are never any meetings held other than the AGM and trustee meetings, but that if the need arises they would arrange a special meeting.

5.2.5. FINANCIAL MATTERS

Most of the comments below by the chairmen interviewed were also made by the managing agents interviewed, as discussed in section 5.3.8.

According to all of the chairmen (100%) the annual financial statements of their schemes are prepared, and the audits performed by firms of chartered accountants (CA(SA)). All of the chairmen (100%) stated that the auditors are appointed by the members of the body corporate at the AGM. They stated that their managing agents recommend audit firms which, according to them, give good service.

All of the chairmen interviewed (100%) stated that they try to incorporate a reserve fund into the budget of their body corporate (see also section 5.2.4. above), but that many owners just want to keep costs at a minimum and do not want to make provision for a reserve.

Four of the five (80%) chairmen were of the opinion that cost is the most important factor to take into account when choosing an audit firm. Four of the five (80%) chairmen also stated that they also take into account whether the audit firm can deliver the financial statements and audit report on time. One of the five (20%) chairmen mentioned that the auditor should be trustworthy and transparent.

Two of the five (40%) chairmen interviewed said that they experience bottle-neck situations regarding the receipt of financial statements and audit reports for their schemes. The other three (60%) chairmen remarked that they never experienced any timing problems. This problem is also discussed from the viewpoint of accounting and auditing practitioners in section 5.4.2. below.

All of the chairmen (100%) were of the opinion that the audit of the financial statements adds value to sectional title schemes; an opinion which agrees with that of managing agents as well as accounting and auditing practitioners, as discussed in sections 5.3.8. and 5.4.1. below. The chairmen stated that they need an independent opinion on the financial matters of the body corporate.

5.3. OPINIONS OF MANAGING AGENTS OF SECTIONAL TITLE SCHEMES

In the rest of this section the results of the information from the questionnaires and interviews with managing agents will be discussed. These aspects will be discussed under the following headings: clients and services, problems and risks, trustees, training and staff, fees, developers, meetings and financial matters.

5.3.1. CLIENTS AND SERVICES

The 5 managing agents interviewed had varying numbers of sectional title schemes as clients, the numbers being 25, 36, 45, 125 and 260 schemes. The managing agents provided a range of services to their clients, which were not all utilised to the same extent. The following figure is a representation of the different service offerings of the managing agents and the percentage of clients making use of the services:

Fig. 5.1. Summary of service offerings by managing agents, indicating the percentage of clients utilising the services.

	Managing agent				
	A	B	C	D	E
Day-to-day management of the complex	50%	100%	30%	100%	100%
Administrative tasks	100%	100%	90%	100%	100%
Compiling of financial statements	100%	100%	100%	50%	100%
Preparation of budgets	100%	100%	100%	50%	100%
Collection of levies and amounts payable	100%	100%	100%	100%	100%
Assistance with insurance	100%	100%	100%	100%	100%
General maintenance of the complex	60%	70%	80%	90%	100%

5.3.2. PROBLEMS AND RISKS

According to the managing agents, one of the biggest problems experienced with the managing of sectional title schemes is problems with municipal accounts, a frustration shared by chairmen and accounting practitioners, as discussed in sections 5.2.2. and 5.4.2. Three of the five (60%) managing agents mentioned that account estimates, corrections on statements, incorrect allocations on statements and poor communication and service from local authorities caused countless problems when managing schemes. It also makes it very difficult to perform analytical procedures on the account balances.

Three of the five (60%) managing agents stated that debt collection is a great challenge. They said that they spend a lot of time and money collecting outstanding amounts, and that the legal processes that have to be followed in the case of non-payment are cumbersome and expensive. One agent mentioned that in the case of tenants, the

available deposits are not always sufficient to cover outstanding balances in the case of non-payment.

Three of the five (60%) managing agents stated that uninformed owners and trustees cause many problems when managing schemes. They said that there is a general ignorance among owners and trustees regarding the legislation governing sectional titles. One of the managing agents mentioned that estate agents selling sectional title property are largely to blame, since they do not inform prospective owners of exactly what they are buying into. The problem of uninformed owners was also mentioned by the chairmen of bodies corporate in 5.2.2. above.

One of the managing agents remarked that attracting and retaining competent staff is a great challenge. He said that due to cost constraints, many managing agents cannot afford to employ highly qualified and skilled staff. Another problem that they experience is a high staff turnover, which he attributes to staff members simply using the employment at a managing agent as a stepping stone to another higher paying job.

According to two of the five (40%) managing agents they experience frustrations when registering new schemes with the South African Revenue Service (SARS). They claim that SARS requires large amounts of information and several documents, which they perceive as being very time consuming.

According to three of the five (60%) managing agents, the biggest risk involved in being a managing agent is the fact that, on the one hand bodies corporate give them the freedom to perform the necessary management activities, but on the other hand hold them responsible if they are unhappy with the outcome of the managing agent's decisions or actions. One of the five (20%) managing agents stated that a big risk is the

fact that they are only contracted for the first year and thereafter the body corporate can change to a different managing agent with one month's notice. The managing agent stated that this happens quite often. The problem was also raised by accounting and auditing practitioners in section 5.4.2. below, but contradicted by the chairmen interviewed in section 5.2.3. One of the five (20%) managing agents also stated that they perceived the biggest risk to be taking over a scheme from another managing agent. The managing agent stated that, in the past, they experienced that for such cases it is difficult to verify balances and that the whole process creates various administrative challenges.

5.3.3. TRUSTEES

The managing agents had varying opinions on whether the trustees of the schemes managed by them are actively involved. Two of the five (40%) managing agents said that they have only actively involved trustees. These two managing agents stated that they have ongoing communication with the trustees and that they go to great lengths to ensure that the trustees are well-informed. Two of the five (40%) managing agents said that 50% of trustees are actively involved, while the other 50% is not involved at all. One managing agent (20%) stated that approximately 25% of the schemes managed by him have actively involved trustees, 70% have trustees who are not involved at all and approximately 5% do not have any board of trustees.

An observation that was made regarding the above, was that the more schemes the managing agents managed, the less involved they perceived their trustees to be. The managing agents managing the smallest number of schemes all commented that they have actively involved trustees.

The managing agents differed in their opinions on what the optimal number would be for a well-functioning board of trustees. One managing agent said more than 3; one said no more than 6; one said 2 to 3 for small schemes and 5 for larger schemes; one said 2 to 5, depending on the size of the scheme; and one said 3 to 5, depending on the size of the scheme.

Two of the five (40%) managing agents stated that, on average the boards of trustees of the schemes managed by them consisted of 5 trustees. One managing agent (20%) said the average is 4 trustees, one (20%) said the average is 3 trustees, and the remaining (20%) agent said the current average is 3 to 5 trustees.

An important observation was that three of the five (60%) managing agents are of the opinion that the average chairman of a board of trustees does not have sufficient skills and knowledge to act as chairman. One of the five (20%) managing agents said that 70% of chairmen are knowledgeable and 30% are not. The remaining (20%) managing agent said that they give formal training to all trustees, and therefore he thinks that the average chairman of a board of trustees has sufficient skills and knowledge to act as chairman. He mentioned that that is only the case for the schemes managed by him, and that he is of opinion that chairmen of other boards of trustees do not have sufficient skills and knowledge to act as chairmen. This problem is also discussed from the viewpoint of auditing and accounting practitioners in section 5.4.5. below.

Five of the five (100%) managing agents remarked that trustees are never compensated for their services. Two of the five (40%) managing agents said that only approximately 10% of the chairmen of boards of trustees receive an honorarium of about R500 per month, and that the rest do not receive any form of compensation. Three of the five (60%) managing agents stated that chairmen of trustees never receive any form of remuneration. One of the managing agents remarked that he thinks

trustees and chairmen would take their tasks more seriously if they were remunerated. As mentioned in section 1.3. of Chapter 1, being a trustee of a body corporate is a “thankless” job, and perhaps it may be easier to find individuals willing to serve as trustees if they were remunerated. The fact was also mentioned in section 1.3. that bodies corporate should be run like “businesses”, and the remuneration of trustees may be a starting point in achieving that. The chairmen of bodies corporate interviewed in section 5.2.1. also felt that remuneration of trustees as well as chairmen should be instated. This comment of the managing agent as well as the other role players should be taken note of by the industry.

Five of the five (100%) managing agents said that if a trustee or chairman made purchases or payments on behalf of the body corporate, they are always reimbursed, provided that they have the necessary invoices.

5.3.4. TRAINING AND STAFF

All of the managing agents interviewed (100%) said that they are entirely up to date with the latest stipulations of the Sectional Titles Act.

All of the managing agents interviewed (100%) said that they give formal sectional-title specific training to all of their newly appointed staff members. Four of the five (80%) managing agents sated that they also give training to current employees, while the remaining managing agent (20%) said that they do not.

Three of the five (60%) managing agents said that there is a need for specialised training courses covering legal aspects, insurance, accounting and the National Credit Act. One of the five (20%) managing agents said that there is no time available to send

staff members on training, so they would not be interested in training courses. One of the five (20%) managing agents said that in their business, the areas of work involving more expertise (such as insurance and accounting) are done by outside specialists. Therefore, they have no need for training.

5.3.5. FEES

Four of the five (80%) managing agents said that one of the main factors taken into account when determining their management fee is the size of the scheme. All of the managing agents said that they have a general fee per unit, which they use as a guideline. The fee is adjusted up or down depending on a number of variables.

Four of the five (80%) managing agents said that the level of involvement of the trustees also has an impact on their management fee. They stated that they adjust fees upward if the trustees are not actively involved in the management of the scheme.

One managing agent remarked that there should be greater transparency by the managing agents on how their fees are calculated as many trustees complain that they are left in the dark regarding this.

5.3.6. DEVELOPERS

The general viewpoint of the managing agents was that they prefer managing schemes where no developers are involved. The managing agents experienced a number of problems where developers were involved in schemes. Problems with developers were also mentioned by the trustees in section 5.2.2. above.

Three of the five (60%) managing agents mentioned that some developers finish building, but leave units without, for example, ceilings, windows or floor tiles. The developer then claims that the units are unoccupiable and refuse to pay levies on those units. The units in the finished section have to subsidise the developer's units with their levies. The managing agents said that this creates budgeting problems and infuriates owners. In some cases the situation is worsened by developers using the water and electricity of the complex during the completion of the building process instead of paying for the water and electricity used by them. One managing agent mentioned that they experienced instances where the developer did not pay the water and electricity bill for the development period and the body corporate had to settle the full outstanding amounts.

Two of the five (40%) managing agents said that developers do not take their role seriously enough in the early phases of the existence of the body corporate. Random sets of management and conduct rules are often registered without taking the interests of the potential future owners into account.

Three of the five (60%) managing agents said it takes a long time (sometimes up to two years) to obtain occupation and electricity certificates from developers. Instances were mentioned where owners wanted to sell their units, and could not do so because of outstanding certificates from developers.

One managing agent also remarked that it happens regularly that developers do not ensure that proper valuation of the scheme is done on completion of every development phase. This creates problems with calculations and budgeting of rates and taxes.

5.3.7. MEETINGS

Four of the five (80%) managing agents stated that in general meetings are poorly attended. All of them stated that 50% to 60% of initial annual general meetings (AGMs) do not have a quorum and have to be postponed. This is despite various communication efforts such as registered mail and sms-messages. Only one (20%) managing agent said that AGMs are well-attended. He attributes the good attendance to the fact that he sends all documents to owners via mail and e-mail beforehand, and sends reminder sms-messages to owners 14 days as well as 7 days before an AGM or other meeting.

One of the biggest problems at AGMs is the approval of budgets. Three of the five (60%) managing agents stated that owners do not understand financial statements and budgets. They remarked that owners do not see increases in perspective and that increases in budgets and the resulting levies are often met with resistance. One of the five (20%) managing agents also stated that at most AGMs, owners want to put impossible cost restrictions on audit fees and management fees. This is a viewpoint that is shared by accounting and auditing practitioners as well, as discussed in section 5.4.2. below.

Three of the five (60%) managing agents also said that owners do not adhere to proper meeting procedures during AGMs, and that owners regularly want to discuss operational matters which fall outside the scope of the agenda.

Two of the five (40%) managing agents stated that the election of trustees at the AGM is usually problematic. They said that it is often difficult to find persons willing to serve as trustees, and in some cases trustees are not re-elected, mainly due to past clashes or disagreements with owners.

All of the problems mentioned above were also experienced by the chairmen interviewed in 5.2.4. above.

5.3.8. FINANCIAL MATTERS

Four of the five (80%) managing agents stated that the annual financial statements of their clients are prepared by firms of chartered accountants (CA(SA)). The other managing agent (20%) said that the financial statements of approximately 85% of his clients are prepared by a firm of chartered accountants, and the financial statements of the remaining 15% are prepared by a Certified Professional Accountant (CPA).

Five of the five (100%) managing agents said that the audits of financial statements of their clients are done by firms of chartered accountants (CA(SA)).

All of the managing agents (100%) said that the appointment of the auditors is done by the members of the body corporate at the AGM. They stated that they do, however, make recommendations regarding audit firms which give good service in cases when they are asked for advice regarding the appointment of auditors.

All of the managing agents (100%) were of the opinion that cost is the most important factor to take into account when choosing an audit firm. Four of the five (80%) managing agents stated that they also take into account whether the audit firm can deliver the financial statements and audit report on time. One of the five (20%) mentioned that he takes the auditor's knowledge of the Sectional Titles Act into account

when choosing an auditor. Only one (20%) managing agent said that the auditor's quality of work is a deciding factor.

Three of the five (60%) managing agents said that they experience bottle-neck situations regarding the receipt of financial statements and audit reports for schemes with February year-ends. They did, however, add that only approximately 25% of their clients have February year-ends. The other two (40%) managing agents remarked that they never experienced any timing problems. This problem is also discussed from the viewpoint of accounting and auditing practitioners in section 5.4.2. below.

All of the managing agents (100%) were of the opinion that the audit of the financial statements adds value to sectional title schemes; an opinion which agrees with that of accounting and auditing practitioners, as discussed in section 5.4.1. below. The managing agents stated that an objective opinion on the financial matters of a scheme is imperative. They remarked that it is even more important to perform an audit in cases where a scheme changed from one managing agent to another.

Another budgeting-related matter (see also section 5.3.7. above) which was mentioned by three of the five (60%) practitioners is special levies. They were of the opinion that bodies corporate should try to avoid special levies and properly plan and budget for repairs and maintenance and capital projects well in advance. All of the managing agents said that they advise the trustees to build up some form of reserve into the budget every year.

Most of the above-mentioned opinions were shared by the chairmen interviewed in section 5.2.5.

The responses of the managing agents regarding the handling of “trust” money are discussed in section 5.4.3. below.

5.4. OPINIONS OF ACCOUNTING AND AUDITING PRACTITIONERS INVOLVED IN THE SECTIONAL TITLE INDUSTRY

In the rest of this section the results of the information from the questionnaires and interviews with accounting and auditing practitioners will be discussed. These aspects will be discussed under the following headings: clients and services, problems experienced, risks, training and staff, trustees, managing agents and fees.

5.4.1. CLIENTS AND SERVICES

The 5 accounting and auditing practitioners interviewed had varying numbers of sectional title schemes as clients. The number of sectional title clients of the practitioners was 10, 30, 63, 132 and one practitioner had more than 300 clients.

Three of the five (60%) practitioners stated that their sectional title clients require them to prepare the financial statements as well as perform the audit. One of these practitioners completes additional tax returns for approximately 2% of their sectional title clients. One of the five (20%) practitioners stated that approximately 80% of their clients require them to prepare the financial statements as well as perform the audit, while 20% of the clients want only an audit done. This practitioner also provides additional business advice to approximately 10% of their sectional title clients, and assists with the preparation of budgets for more or less 20%. One of the five (20%) practitioners stated that approximately 90% of their clients require them to prepare the financial statements as well as perform the audit, while 5% of the clients want only

accounting work to be performed and another 5% of the clients want only an audit done. This practitioner also provides additional business advice to approximately 10% of their sectional title clients, and assists with the preparation of budgets for more or less 20%.

Regarding the time spent compiling financial statements and performing audits, the responses of the practitioners differed significantly. The table below summarises their responses:

Fig. 5.2. Summary of average time spent by practitioners compiling financial statements and performing an audit of a sectional title scheme

	Practitioner				
	A	B	C	D	E
Compiling financial statements of a sectional title scheme:	2 hours	3 to 8 hours	2 hours	15 hours	16 hours
Auditing of a sectional title scheme:	6 hours	20 to 36 hours	14 to 18 hours	10 hours	16 to 40 hours

Only one of the five (20%) practitioners said that they regularly attend the annual general meetings (AGM) of their sectional title clients. The practitioner said that he attends, on average, the first 15 to 30 minutes of the AGM in order to present the annual financial statements to the members of the body corporate. Two of the five (40%) practitioners said that they attend the AGMs of approximately 5% to 10% of his sectional title clients, but only if they are specifically asked to do so. The other 2 (40%) practitioners stated that they never attended any AGM.

All 5 (100%) of the practitioners interviewed were of the opinion that the auditing of the financial statements adds value to sectional title schemes. One practitioner stated that audits are important, because it gives a form of assurance to the generally ignorant and uninformed trustees and members of bodies corporate. Another practitioner said the fact that trust money is involved makes an audit absolutely essential. One of the practitioners mentioned that audits are imperative because it will indicate whether the managing agents are doing their work in terms of debt collection and keeping to budgeted amounts.

Three of the five (60%) practitioners are of the opinion that a full audit is the most applicable way of providing assurance to a sectional title scheme. The other two (40%) practitioners also felt that an audit is applicable, but they mentioned that the possibility of Agreed-upon Procedure Engagements or Independent Reviews can also be investigated. These practitioners stated that there are still many grey areas regarding Independent Reviews, and that alternatives to full audits may not necessarily result in cost savings for the client.

A very important observation was made regarding accounting standards, which correlates with the literature that was discussed in section 4.2. of Chapter 4. The practitioners were asked which accounting standards they deem to be the most applicable in compiling the annual financial statements of bodies corporate, with the options being IFRS, IFRS for SMEs, a custom-made standard or another alternative. All of the practitioners (100%) were of the opinion that a specific standard should be developed for sectional title schemes, as it is a very unique and highly specialised industry. They all felt that neither IFRS nor IFRS for SMEs is applicable to bodies corporate. This is certainly a finding that the accounting professional bodies in South Africa should take note of. Two of the five (40%) practitioners mentioned that they are uncertain of the accounting treatment of certain transactions in the sectional title industry, such as the capitalisation of assets, treatment of certain VAT components and

allocation of repair and maintenance payments. The practitioners are of the opinion that additional guidance is needed from the accounting professional bodies, similar to the guidance available to non-profit entities.

5.4.2. PROBLEMS EXPERIENCED

According to all of the practitioners, one of the biggest problems experienced with the accounting and auditing of sectional title schemes is problems with municipal accounts. This problem was also mentioned by the chairmen and managing agents in sections 5.2.2. and 5.3.2. above. Three of the five (60%) practitioners mentioned that account estimates, corrections on statements and incorrect allocations between water and electricity on statements caused problems when doing accounting and audit work. It also makes it very difficult to perform analytical procedures on the account balances.

According to three of the five (60%) practitioners, bodies corporate put pressure on accounting and audit fees. This results in restrictions on the scope of the work, due to limited time available. They also mentioned that many trustees and managing agents have a misperception of exactly what an audit entails and the amount of work involved to complete an audit. This is, perhaps, another example of the expectation gap which was discussed in section 3.3.7.4.1. of Chapter 3. The viewpoints from the perspective of managing agents were also discussed in section 5.3.7. above.

Three of the five (60%) practitioners felt that a big part of information and source documents received from trustees and managing agents are incomplete or not detailed enough, which complicates the process of preparing financial statements. They also remarked that some managing agents capture accounting information according to the cash-flow basis of accounting, and information often has to be converted to principles of accrual accounting.

One of the five (20%) practitioners mentioned that bodies corporate changing from one managing agent to another or from one audit firm to another creates problems. According to the practitioner this happens often, as trustees do “managing agent-hopping” or “auditor-hopping” from year to year in order to try to save money. (The fact was also confirmed by a managing agent in section 5.3.2. above, but contradicted by the chairmen interviewed in section 5.2.3.) As a result of poor communication to owners and tenants, fees are still paid over to the old managing agent, and some managing agents refuse to hand over the control of the body corporate’s bank account after changing to another agent. Verifying opening balances of accounts and financial statements can also become problematic.

One of the five (20%) practitioners mentioned one of the frustrations experienced is that there is not sufficient continuity amongst the staff of managing agents, and as soon as a person is familiar with a particular body corporate and auditor, they leave the employment of the managing agent. This agrees with the opinion of one of the managing agents mentioned in section 5.3.2. as well as the viewpoints of chairmen in section 5.2.3.

One of the five (20%) practitioners commented that there is uncertainty regarding the format and level of detail required in the financial statements of bodies corporate. The practitioner mentioned that no guidance is given by the accounting professional bodies regarding this.

Regarding time constraints, four of the five (80%) practitioners stated that there are certain times of the year that they experience bottle-neck situations with sectional title clients. This problem was also addressed in section 4.3.5.2. of Chapter 4. The 4 practitioners mentioned that bottle-neck situations usually occur around February and June each year, and according to them, the main reason is that managing agents do not

send the financial information through to them on time. The other practitioner stated that he does not have many sectional title clients, and therefore, does not experience any timing problems. In section 5.3.8. it was also mentioned that some of the managing agents interviewed had problems with the response time of auditors for clients with February year-ends.

Two of the four (50%) practitioners who experienced timing problems said that moving the financial year-ends of bodies corporate could be a solution to the problem. They mentioned that it is a great practical challenge and, therefore, they are not in favour thereof. The other two practitioners said that managing agents should improve their service and have financial information available sooner after year-end in order to solve the said problem.

Two of the five (40%) practitioners said that they never experienced any problems with the South African Revenue Service (SARS) regarding their sectional title clients. One of the five (20%) practitioners stated that the SARS staff is not up to date with the current tax legislation governing bodies corporate. (See also section 4.4.2.2.3. in Chapter 4.) Two of the five (40%) practitioners mentioned that they sometimes experience problems when SARS has to pay out money to their clients and that sectional title clients' tax returns are sometimes handed in late, mainly due to the bottle-neck situations mentioned above.

5.4.3. RISK

One of the five (20%) practitioners viewed the risk of auditing sectional title schemes as very low, compared to auditing clients in other industries. The practitioner mentioned that sectional title audits are very easy and not complex. Two of the five (40%)

practitioners viewed the risk of auditing sectional title schemes as relatively low to moderate, compared to auditing clients in other industries.

One of the five (20%) practitioners viewed the risk of auditing a sectional title schemes as moderate to high, compared to auditing clients in other industries. The practitioner stated that some sectional title clients, such as combined residential and commercial schemes have complex structures and challenging tax calculations. The practitioner also mentioned that due to the fact that there is trust money involved, great care has to be taken during the audit of bodies corporate. He stated that cost pressures and resulting time constraints make it difficult to perform all the procedures required by the auditing standards, which increases the risk.

One of the five (20%) practitioners viewed the risk of auditing a sectional title schemes as high, compared to auditing clients in other industries. The practitioner stated that segregation of duties is a big problem in sectional title schemes, and creates opportunity for fraud. He also mentioned that there is often no clear audit trail available to provide evidence of transactions. The practitioner is of the opinion that large amounts of trust money involved in sectional title schemes increases the risk of auditing such clients. He mentioned that it is difficult to perform all the necessary risk assessment procedures, due to time constraints when auditing sectional title clients.

An interesting observation was made when comparing the above risk assessment with the time spent by the practitioners in section 5.4.1. The higher the practitioner perceived the risk of a sectional title audit to be, the more time they spent on the audit of sectional titles. The practitioners who perceived the risk of sectional title audit to be low spent the least number of hours auditing sectional title schemes, compared to the other practitioners.

As part of the interviews, the practitioners were asked what they perceived to be the greatest risks related to the audit of sectional title schemes. Three of the five (60%) practitioners stated that cut-off of debtors and creditors is a great risk, as it is not always easy to determine correct balances at year-end. This was also briefly mentioned in section 4.4.2.2.6. of Chapter 4. The practitioners mentioned that invoices from local authorities for water and electricity often results in problems with cut-off, due to incorrect estimates on statements, and statements being delivered late. Three of the five (60%) stated that collectability of debtors is a great concern, a comment which agrees with the analysis of financial information in section 4.4.2.2.6. in Chapter 4. The practitioners stated that it is very difficult for them to determine provisions for doubtful debt and that in some cases it raises red flags regarding going concern.

A serious concern that was raised by all (100%) of the practitioners is the practice of some managing agents to use one trust account in which all of the funds of the bodies corporate managed by them are deposited. The problem was also addressed in section 2.3.4.6. of Chapter 2. According to the practitioners interviewed, some managing agents refuse to issue the auditors with a bank statement of the large (“only”) trust account due to the fact that it contains, as the managing agents put it, “confidential” information of other bodies corporate. These managing agents are only willing to provide the auditors with their own summary of the bank account and transactions of the body corporate under audit.

It was mentioned that many unallocated deposits relating to a specific body corporate which was deposited into the managing agent’s “pool” trust account remain unnoticed and unallocated due to the fact that the information is not made available to the auditors. The practitioners were of the opinion that it is virtually impossible to reconcile the bank balances with the little information that is provided to them. They also mentioned that the interest accrued on this large trust account is never allocated to the individual bodies corporate, and that the managing agent is the sole beneficiary thereof.

All of the practitioners stated that they do not feel comfortable with this practice, and they would rather see managing agents open a separate bank account for each body corporate. The question to be asked here is whether the handling of the interest received as “income” of the managing agent is not against the legal aspects of the handling of “trust money”. This problem was also mentioned by one of the chairmen interviewed in section 5.2.2. above.

In response to the above concern, one of the managing agents interviewed stated that it is accepted practice and that, over and above the large “pool” trust account, they also open separate “investment” accounts for each of their bodies corporate. He said that they do monthly account calculations and reconciliations of income and expenses and the surplus funds of each body corporate is to its “investment” account. Another managing agent stated that using only one trust account is a common practice in the industry, and that many managing agents do not, in fact, even open “investment” accounts. It was further observed that the other managing agents who were contacted regarding this matter seemed hesitant to respond.

One of the practitioners interviewed also mentioned that they do not get sufficient co-operation from financial institutions when it comes to the audits of bodies corporate, to such an extent that they do not even ask for bank confirmations any more. He stated that it takes several weeks to obtain a bank confirmation and in many cases requests are ignored by banks. It is also impossible for the financial institutions to split the above mentioned trust accounts into the relevant sections dealing with the individual bodies corporate.

In conclusion it seems that the handling of “trust” money by managing agents is a matter which accounting and auditing practitioners should be well aware of. Usually,

interest “earned” on trust funds should not accrue to the managing agent, but to the bodies corporate. This is a serious aspect that should be taken note of by the industry.

5.4.4. TRAINING AND STAFF

Four of the five (80%) of the practitioners interviewed were of the opinion that they are up to date with the latest requirements of the Sectional Titles Act. The remaining practitioner said that he is not up to date.

None of the practitioners provide any form of formal training for their staff members. Three of the five (60%) practitioners mentioned that they have only one experienced staff member responsible for the accounting and auditing of their sectional title clients. That person did not undergo any sectional-title-specific training. If such a staff member leaves the employment of the firm, he/she will have to provide on-the-job training to a junior member who will take over his/her work.

All of the practitioners (100%) stated that it would be very useful if a good basic training course can be made available covering the legal, accounting and auditing aspects surrounding sectional title. One practitioner stated that the reason for formal training not being given is the fact that developing such a training course in an audit firm is time consuming and very expensive. He also mentioned that they do not always get a high “return on training investment” due to the high turnover of staff. Another practitioner mentioned that good training is not only important for the staff of the audit firms, but also for the staff of managing agents. He said that some managing agents employ staff members to do accounting or capturing work, who are not qualified or skilled to do the work.

As part of the interviews, the practitioners were asked about the average post level or qualification of the staff members doing work on their sectional title clients, which resulted in varying responses. The figure below is a summary thereof:

Fig. 5.3. Summary of average post level or qualification of staff members compiling financial statements and performing an audit of a sectional title scheme

	Practitioner				
	A	B	C	D	E
Compiling financial statements of a sectional title scheme:	2 nd year trainee or higher	3 rd year trainee or higher	1 st year to 3 rd year trainee	3 rd year trainee or higher	Manager with at least SAIPA qualification, assisted by 2 nd year trainee
Auditing of a sectional title scheme:	2 nd year trainee or higher	Trainee with at least a B.Com (Acc) qualification	1 st year to 3 rd year trainee	3 rd year trainee or higher	Manager with at least SAIPA qualification, assisted by 2 nd year trainee

An interesting observation was made when comparing the above qualification levels of staff with the practitioners' perceived risk of sectional title audit in section 5.4.3. The practitioners who perceived the risk of sectional title audit to be low used staff members at a lower post grade to do the work on sectional title clients, compared to the other

practitioners. The higher the practitioner perceived the risk of a sectional title audit to be, the higher the post level and qualification of the staff members used to do the work.

5.4.5. TRUSTEES

The practitioners had different opinions on the optimal number of trustees that would result in a well-functioning board of trustees. One practitioner stated that it depends on the size of the scheme, but that there must be no more than 5 trustees on the board. Another practitioner is also of the opinion that it depends on the size of the scheme, but anything between 3 and 7 trustees would be sufficient, as long as it is an uneven number to prevent a deadlock in voting. One practitioner felt that at least 3 trustees are necessary for a well-functioning board, while the remaining two practitioners prefer 4 and 5 trustees, respectively.

One alarming observation was that four of the five (80%) practitioners are of the opinion that the average chairman of a board of trustees does not have sufficient skills and knowledge to act as chairman. This corresponds with the opinion of the managing agents in 5.3.3. above.

5.4.6. MANAGING AGENTS

When asked whether they thought that the average managing agent has the necessary skills and competence to act as such, only two of the five (40%) practitioners agreed. Another two of the five (40%) practitioners were of the opinion that the managing agents they came into contact with were not knowledgeable and did a poor job, while the remaining one practitioner (20%) said that he was unsure. He said that some managing agents are doing good work, while the skills and competence of others are sub-

standard. One practitioner also mentioned the fact that many managing agents have no idea how the budgeting process works and how to prepare a budget. He stated that amounts are simply adjusted with inflation year after year.

5.4.7. FEES

The practitioners take different measures into account when determining their fees. Two of the five (40%) practitioners mentioned that quality of information received from the managing agent, as well as their relationship with the managing agent, plays an important role in determining their fees. Fees would be higher if they are not familiar with the managing agent, or if they experiences problems or received sub-standard information from the managing agent in the past. Two of the five (40%) of the practitioners stated that the more complex the transactions of the scheme is, and the more hours they need to spend completing the work, the higher the fees would be. One of the five (20%) practitioners commented that they determine their fees based on a minimum fee of R1 500 plus an additional amount based on the number of units in the scheme.

One of the five (20%) practitioners made the remark that they would initially do the work of a body corporate for a much lower fee, if they can possibly gain good exposure and attract additional clients from the assignment. Two of the five (40%) practitioners said that they would charge a higher fee if the necessary information is not readily available to enable them to complete the work.

5.5. OVERVIEW OF EMPIRICAL FINDINGS AND RECOMMENDATIONS

In this section a brief overview will be given of the main observations from the interviews with the various role players.

For the chairmen of bodies corporate the main concerns were rule enforcement, uninformed and uninvolved owners, difficulties with municipalities and poor meeting attendance. They also mentioned a lack of trustee remuneration and certain problems where developers were involved. Financial pressures, debt collection and difficulties in getting budgets approved were also raised as concerns.

The managing agents also had problems with ignorant and uninvolved owners as well as poor meeting attendance. Municipal accounts caused serious concerns as well as debt collection. A high staff turnover, pressures on management fees and obtaining budget approval created further problems for managing agents. Some problems with timely receipt of financial statements and audit reports were mentioned. Furthermore, the managing agents had various problems with developer involvement.

The accounting and auditing practitioners who were interviewed regarded municipal accounts, pressures on audit fees, time constraints, as well as uninformed trustees and owners as problems. They also had concerns about staff continuity at managing agents and the use of only one bank account for the cash transactions of bodies corporate by the managing agent. The practitioners also had various accounting-related questions on which they need clarity from their professional bodies.

All of the role players were of the opinion that auditing the financial statements of bodies corporate adds value and should be continued. Another recommendation that should be taken note of by the industry is the possibility of remuneration of trustees.

5.6. CONCLUSION

In this chapter the results of interviews with a sample of role players, namely chairmen of bodies corporate, managing agents and accounting and auditing practitioners in the sectional title industry were discussed. Various problems, concerns and recommendations were mentioned of which the industry should take note. The empirical findings can also be used as a basis for future research. The next chapter will contain the conclusion of the study as well as recommendations for future research.

CHAPTER 6 – CONCLUSION

In order to improve the mind, we ought less to learn, than to contemplate.

– René Descartes

No research is ever quite complete. It is the glory of a good bit of work that it opens the way for something still better, and this repeatedly leads to its own eclipse.

– Mervin Gordon

6.1. INTRODUCTION

The housing problem in South Africa is one of the greatest challenges facing the country, especially seen in the light of the current population growth, immigration statistics and the government's backlog in housing delivery. The sectional title industry plays an important role in addressing this challenge.

Library, archive and internet searches revealed that very little academic research has so far been done on sectional titles in South Africa. The academic research identified was mostly postgraduate research in the fields of law, cost accounting, taxation and regional planning, meaning that no academic research has been done specifically from an accounting and auditing perspective to date on the sectional title industry in South Africa.

The main aim of the study was an overview of practical problems experienced from an accounting and auditing perspective regarding risks associated with sectional titles, as well as auditing- and accounting-specific problems relating to sectional title. The

second, two-fold aim of the study was to find possible solutions to the above-mentioned problems and to make recommendations in this regard. The third aim of the study was to set industry benchmarks from the analysis of annual financial statements by way of analysis and interpretation of a sample of annual financial statements of sectional title schemes over a three-year period. These benchmarks can be of assistance as an industry standard for owners, trustees, managing agents, auditors and accountants rendering a professional service.

In Chapter 1 of the study, the background to the housing problem and the sectional title industry in South Africa was introduced briefly. The chapter also included a brief discussion of the governance of sectional title, as well as some background on financial reporting in South Africa. The need for a study regarding an accounting and auditing perspective on sectional title property in South Africa was addressed. The problem statement, aim of the study, research methodology and the contents of the study was also discussed.

The second chapter dealt with the legal aspects surrounding the sectional title industry in South Africa, with specific consideration given to legal aspects relating to accounting, financial, auditing and management matters of sectional title schemes. The purpose of the chapter was not to engage in a legal study, but set a theoretical legal framework with which bodies corporate, managing agents and other role players in the sectional title industry have to comply and consideration was only given to accounting, financial, auditing and management aspects. The chapter was structured according to the functions and responsibilities of the various role players in sectional title schemes, being the body corporate, the trustees and managing agents. In this chapter, additional aspects covered by the prescribed management rules were also discussed.

In the third chapter, the auditing and assurance aspects of sectional title schemes were researched. The chapter started with a brief history and background of auditing. Definitions and various aspects relating to assurance engagements and sectional titles were evaluated using various sources. An analysis was also made of assurance-related aspects of a sample of audit reports of body corporate annual financial statements.

Chapter 4 dealt with accounting and reporting of sectional title schemes. The chapter examined the legal requirements for financial reporting by bodies corporate and briefly dealt with reporting frameworks currently available. The chapter also addressed the question as to whether International Financial Reporting Standards is not perhaps too cumbersome and expensive for the users of body corporate financial statements. The chapter also investigated the possibility of a sectional title-specific reporting framework. Findings based on an analysis of a sample of body corporate financial statements over a period of three years were also discussed in this chapter.

In Chapter 5, an empirical study of the sectional title industry in South Africa was undertaken. The study was based on interviews held with role players in the industry. The chapter was divided into four parts. The first part dealt with interviews held with chairmen of boards of trustees of bodies corporate, part two with interviews held with managing agents of sectional title schemes, while part three dealt with interviews held with accountants and auditors of sectional title schemes. The fourth part of this chapter summarised the findings from the interviews held with the various role players.

6.2. LIMITATIONS OF THE STUDY

One of the limitations of the study was that the population from which the samples for the empirical study was limited to the Bloemfontein-area in South Africa. Even though

the study was limited to the Bloemfontein area, the literature review indicated that the ambiguity, problems and unclear aspects were pervasive in the industry throughout South Africa.

The sample of 60 annual financial statements, including audit reports thereto, was selected at random, covering only a period of three years as well as a variety of sizes of bodies corporate. In the analysis of the financial information, a distinction was made between small, medium and large schemes, but no distinction was made between residential, commercial and combined bodies corporate.

All of the bodies corporate in the sample made use of the services of a managing agent. No self-managed schemes were incorporated into the study. Future samples can be selected to include owner-managed as well as agent-managed schemes.

For the empirical study, the samples were limited to 5 role players in each category, namely chairmen of bodies corporate of sectional title schemes, managing agents of sectional title schemes, and accounting and auditing practitioners involved in the sectional title industry. In future studies, the sample can be extended to include more role players in each category.

6.3. IMPORTANT FINDINGS FROM THE LITERATURE REVIEW

The literature review of this study covered three main aspects in respect of sectional title schemes, namely legal aspects relating to accounting and auditing matters of sectional title schemes, auditing and assurance aspects and accounting and reporting aspects.

From the literature it was clear that there is much uncertainty, ambiguity and confusion on what is expected regarding the financial, accounting and auditing-related matters of bodies corporate. In many cases, it was noted that the legislation contains wording that is not true to the acknowledged subject terminology.

A further conclusion that was drawn from the literature review was that most of the auditing-related issues probably stem from the expectation gap. There is a distinct difference between what the audit profession perceives their objectives to be, and what the sectional title role players, and even the legislator, expects from an audit, or “thinks” that the auditor does.

As part of the literature review, concern was also raised as to the applicability of currently available accounting standards, and the aspect of a possible tailor-made accounting standard for sectional titles was addressed. Many users of body corporate financial statements are probably “unsophisticated” and have no knowledge of International Financial Reporting Standards. It is an open question whether applying IFRS is useful, especially for small and medium schemes.

6.4. IMPORTANT FINDINGS FROM THE EMPIRICAL STUDY

The literature review paved the way for a detailed analysis of the auditing and accounting aspects relating to the sample of body corporate financial statements and an empirical study performed on the sectional title industry in Bloemfontein in South Africa by way of interviewing a sample of role players in the industry.

From the analysis of the sample of annual financial statements it was evident that auditing and accounting practitioners are not always acting consistently and that they are also not consistent in their application of the Sectional Titles Act.

The observations and findings from the analysis and interpretation of the sample of annual financial statements can be used as a starting point and benchmarks in creating industry standards and benchmarks.

From the results of the interviews with the industry role players, various concerns were identified. For all of the role players, the main concerns were uninvolved and uninformed owners, difficulties with municipalities and developers, financial pressures and problems with debt collection. The managing agents experienced specific problems with high staff turnover and timely receipt of financial statements and audit reports from practitioners. The trustee chairmen cited rule enforcement and lack of trustee remunerations as additional concerns. The trustee chairmen as well as the managing agents complained about poor meeting attendance. The accounting and auditing practitioners as well as the trustee chairmen had concerns about staff continuity at managing agents and the use of one managing agent's bank account for the cash transactions of a number of bodies corporate. The practitioners also had various accounting-related questions on which they need clarity from their professional bodies. All of the role players were of the opinion that auditing the financial statements of bodies corporate adds value and should be continued.

6.5. SUMMARY OF RECOMMENDATIONS AND POSSIBLE FURTHER RESEARCH

Throughout Chapters 1 to 5 various possibilities for future research have been identified, which will be further alluded to in this section.

As mentioned in Chapter 1, as well as in section 6.2 above, the empirical research done in this study focused only on role players in the sectional title industry in the Bloemfontein area in South Africa. An empirical study could be undertaken amongst the role players throughout South Africa, covering a larger geographical area. A comparison could be made between role players in different provinces in the country. Furthermore, an internationally comparative study could also be undertaken, comparing sectional title accounting and auditing aspects in South Africa with similar entities around the globe.

In Chapter 1 a brief overview of governance in the sectional title industry was given. A detailed study could investigate past governance failures, fraud, etc. and expand on the importance of governance in the sectional title industry. In addition, Chapter 2 mentioned the aspect of ethics and codes of conduct in the sectional title industry in South Africa. Further research could be done on ethical awareness in the industry as well as the development and implementation of codes of conduct for the industry.

There are various interest groups for the different industries in South Africa. In the light of the findings in Chapters 3 to 5, SAICA could possibly consider establishing an interest group for the sectional title industry in South Africa.

Against the background of the findings in Chapters 4 and 5, a further study could also be undertaken to develop a specific accounting framework for the sectional title industry in South Africa, possibly under the guidance of SAICA, as mentioned in the previous paragraph.

As mentioned in section 6.2. above, the financial information only covered a period of three years and no distinction was made between residential, commercial and

combined bodies corporate. In future research studies, the financial information can, for instance, be split into those categories. Furthermore, financial information can be obtained for more than three years, in order to identify clearer trends.

In Chapter 5 possible irregularities were briefly discussed regarding the holding of “trust” money and the resulting handling of interest by managing agents. A more in-depth research study can be undertaken on this matter.

Another aspect that was mentioned in section 6.2. above is the fact that all the bodies corporate in the sample made use of the services of a managing agent and no self-managed schemes were incorporated into the study. Future samples can be selected to include owner-managed as well as agent-managed schemes for purposes of comparative studies.

6.6. CONCLUSION

This study was the first of its kind undertaken in South Africa. The study provides a valuable background on accounting and auditing aspects in the sectional title industry which can be used by bodies corporate, trustees managing agents, accounting and auditing practitioners, researchers and other role players in the industry. It also laid the foundation for several possible further academic research studies that can be undertaken regarding the sectional title industry.

“Research means that you don’t know, but that you are willing to find out.”

– Charles F Kettering

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ANNEXURE A

Questionnaire for trustee chairpersons

1 What are the three (3) biggest problems that you have experienced as chairperson of the board of trustees?

i)

ii)

iii)

2 Are you up to date regarding the latest stipulations of the Sectional Titles Act?

Yes

No

3 Do you feel that there is a need for special courses or training for trustees and trustee chairpersons?

- Training for trustees?

Yes

No

- If yes, specify:
-

- Training for trustee chairpersons?

Yes

No

- If yes, specify:
-

4 In your opinion, what is the optimal number of trustees for a well-functioning board of trustees?

--

5 How many people serve on the board of trustees of the sectional title scheme of which you are the chairperson?

--

6 Are the trustees of the board of which you are the chairperson remunerated for their services?

Yes
No

- If they are remunerated, what is the average annual amount per trustee?

--

7 Are you as chairperson of the board of trustees remunerated for your services, over and above the remuneration mentioned in 6 (above)?

Yes
No

- If you are, what is the amount of your annual remuneration/honorarium?

--

8 Are the services of a management agent used in your sectional title scheme?

Yes
No

If yes, what services are rendered?

- Day-to-day management of complex
- Administrative tasks
- Drawing up of financial statements
- Drawing up of budgets
- Collection of levies, amounts receivable, etc.
- Other (specify)

9 If your complex is managed by a managing agent, are you aware of how the management fees are calculated?

Yes
No

10 If your complex is managed by a managing agent, what is your level of satisfaction (choose only one option) with the services of the managing agent?

- Very satisfied
- Satisfied
- Dissatisfied
- Very dissatisfied

11 If your complex is managed by a managing agent, how long has the managing agent been managing your sectional title scheme?

--

12 In your opinion, what two (2) factors play the most important roles in the decision about the appointment of a managing agent?

i) _____

ii) _____

13 What is your opinion about developers who are involved in sectional title schemes?

14 Are there any specific problems experienced when developers are involved in a sectional title scheme?

15 Is the annual general meeting (AGM) of your sectional title scheme generally well attended?

Yes
No

16 What are the three (3) most common problems that are experienced regarding the annual general meeting?

i) _____

ii) _____

iii) _____

17 Are any other meetings held for the board of trustees, besides the annual general meeting?

Yes
No

- If there are, specify the type of meetings:

- How often are these meetings held?

18 Are any other meetings, over and above the annual general meeting, held for the **residents** of the sectional title scheme?

Yes
No

- If so, specify the type of meetings:

- How often are these meetings held?

19 Are any other meetings, other than the annual general meeting, held for the **owners** of the units of the sectional title scheme?

Yes
No

- If so, specify the type of meetings:

- How often are these meetings held?

20 Are the annual financial statements of your sectional title scheme drawn up by a chartered /professional accountant/firm?

Yes
No
Sometimes

- If so, specify the type of firm that does the work:

CA(SA)
SAIPA
Other

- If other, specify:

21 Are the annual financial statements of your sectional title scheme audited by a chartered/professional accountant/firm?

Yes
No
Sometimes

- If so, specify the type of firm that does the work:

CA(SA)
SAIPA
Other

- If other, specify:

-
- If the financial statements are not audited, what kind of assurance is obtained?
-
-

22 Who appoints the auditors of your sectional title scheme?

- The trustee chairperson
- The trustees
- The members of the board of control during the AGM
- The management agent

23 In your opinion, what two (2) factors play the most important role in the decision about the appointment of the accountant/auditor?

i)

ii)

24 Do you find that the time pressure experienced by auditors/accountants of complexes causes bottleneck situations?

Yes
No
Unsure

- If yes, can you suggest a possible solution(s) to the problem?

25 In your opinion, does the auditing of/other form of assurance regarding the annual financial statements add any value to sectional title schemes?

Yes
No
Unsure

- Motivate your answer briefly

26 In your opinion, what are the two (2) greatest risks attached to being the trustee chairperson of a sectional title scheme?

i)

ii)

27 In your opinion, what are the two (2) greatest risks attached to being a member of the board of trustees (other than the chairperson) of a sectional title scheme?

i)

ii)

28 What are the three (3) greatest problems experienced during the budgeting process of your sectional title scheme?

i)

ii)

iii)

29 What are the most significant problems that you experience with the local authority (municipality)/service providers, with regard to:

- Water?

- Rates?

- Electricity?

- Clearance certificates for levies?

30 Are there any specific problems that your sectional title scheme has experienced with regard to banks or other financial institutions?

31 Does your sectional title scheme have a fixed policy regarding reserve funds and surplus accounts?

Yes
No

- If yes, specify:

32 In your opinion, what are the two (2) greatest misperceptions amongst the following parties with regard to your duties and responsibilities as trustee chairperson:

- Residents of the sectional title scheme?

i)

ii)

- The board of trustees?

i)

ii)

- The management agent, if any?

i)

ii)

33 Any further comments?

ANNEXURE B

Vraelys aan trustee-voorsitters

1 Wat is die drie (3) grootste probleme wat u as voorsitter van die raad van trustees ervaar?

i)

ii)

iii)

2 Is u op die hoogte van die nuutste bepalings rakende die Wet op Deeltitels?

Ja

Nee

3 Bestaan daar volgens u 'n behoefte aan spesiale kursusse of opleiding vir trustees en trustee-voorsitters?

- Opleiding vir trustees?

Ja

Nee

- Indien wel, spesifiseer:
-

- Opleiding vir trustee-voorsitters?

Ja

Nee

- Indien wel, spesifiseer:
-

4 Hoeveel trustees is na u mening die optimale getal vir 'n raad van trustees wat goed funksioneer?

--

5 Uit hoeveel persone bestaan die raad van trustees van die deeltitelskema waarvan u die voorsitter is?

--

6 Word die trustees van die raad waarvan u die voorsitter is vir hul dienste vergoed?

Ja
Nee

- Indien wel, wat is die gemiddelde jaarlikse vergoeding per trustee?

7 Word u as voorsitter van die raad van trustees vir u dienste vergoed, bo en behalwe die vergoeding in 6 hierbo gemeld?

Ja
Nee

- Indien wel, wat is die bedrag van u jaarlikse vergoeding/honorarium?

8 Word daar van die dienste van 'n bestuursagent in u deeltitelskema gebruik gemaak?

Ja
Nee

Indien wel, watter dienste word gelewer?

- Dag-tot-dag-bestuur van kompleks
- Administratiewe take
- Opstel van finansiële state
- Opstel van begrotings
- Invordering van heffings, bedrae ontvangbaar, ens.
- Ander (spesifiseer)

9 Indien u kompleks deur 'n bestuursagent bestuur word, weet u hoe die bestuursfooie bereken word?

Ja
Nee

10 Indien u kompleks deur 'n bestuursagent bestuur word, wat is u vlak van tevredenheid (kies net een opsie) ten opsigte van die dienste van die bestuursagent?

- Baie tevrede
- Tevrede
- Ontevrede
- Baie ontevrede

11 Indien u kompleks deur 'n bestuursagent bestuur word, hoe lank is die bestuursagent reeds vir die bestuur van u deeltitelskema verantwoordelik?

--

12 Watter twee (2) faktore speel volgens u die belangrikste rol by die besluit oor die aanstelling van 'n bestuursagent?

i)

ii)

13 Wat is u opinie rakende ontwikkelaars wat by deeltitelskemas betrokke is?

14 Is daar enige spesifieke probleme wat ondervind word wanneer ontwikkelaars by 'n deeltitelskema betrokke is?

15 Word die algemene jaarvergadering (AJV) van u deeltitelskema oor die algemeen goed bygewoon?

Ja
Nee

16 Wat is die drie (3) algemeenste probleme wat ten opsigte van die algemene jaarvergadering ondervind word ?

i)

ii)

iii)

17 Word daar enige ander vergaderings, bo en behalwe die algemene jaarvergadering, vir die **raad** van trustees gehou?

Ja
Nee

- Indien wel, spesifiseer die tipe vergaderings:

- Hoe gereeld word hierdie vergaderings gehou?

18 Word daar enige ander vergaderings, bo en behalwe die algemene jaarvergadering, vir die **inwoners** van die deeltitelskema gehou?

Ja
Nee

- Indien wel, spesifiseer die tipe vergaderings:

- Hoe gereeld word hierdie vergaderings gehou?

19 Word daar enige ander vergaderings, bo en behalwe die algemene jaarvergadering, vir die **eienaars** van eenhede van die deeltitelskema belê?

Ja
Nee

- Indien wel, spesifiseer die tipe vergaderings:

- Hoe gereeld word hierdie vergaderings gehou?

20 Word die finansiële jaarstate van u deeltitelskema deur 'n geëkspertiseerde/professionele rekenmeester/firma opgestel?

Ja
Nee
Soms

- Indien wel, spesifiseer die tipe firma wat die werk doen:

CA(SA)
SAIPA
Ander

- Indien ander, spesifiseer:

21 Word die finansiële jaarstate van u deeltitelskema deur 'n geoktrooieerde/professionele rekenmeester/firma geoudit?

Ja
Nee
Soms

- Indien wel, spesifiseer die tipe firma wat die werk doen:

CA(SA)
SAIPA
Ander

- Indien ander, spesifiseer:

- Indien die finansiële state nie geoudit word nie, watter vorm van gerusstelling word verkry?

22 Deur wie word die ouditeure van u deeltitelskema aangestel?

- Die trustee-voorsitter
- Die trustees
- Die lede van die beheerliggaam tydens die AJV
- Die bestuursagent

23 Watter twee (2) faktore speel volgens u die belangrikste rol by die besluit oor die aanstelling van die rekenmeester/ouditeur?

i)

ii)

24 Ondervind u dat tydsdruk wat deur die ouditeure/rekenmeesters van komplekse ervaar word, bottelnek-situasies versoorzaak?

Ja
Nee
Onseker

- Indien wel, kan u 'n moontlike oplossing(s) vir die probleem voorstel?

25 Voeg die ouditering van of ander vorm van gerusstelling oor die finansiële jaarstate na u mening enige waarde toe tot deeltitelskemas?

Ja
Nee
Onseker

- Motiveer u antwoord kortliks

26 Wat is volgens u die twee (2) grootste risiko's daaraan verbonde om die **trusteevoorsitter** van 'n deeltitelskema te wees?

i)

ii)

27 Wat is volgens u die twee (2) grootste risiko's daaraan verbonde om 'n **lid** van die raad van trustees (anders as die voorsitter) van 'n deeltitelskema te wees?

i)

ii)

28 Wat is die drie (3) grootste probleme wat tydens die begrotingsposes van u deeltitelskema ervaar word?

i)

ii)

iii)

29 Wat is die beduidendste probleme wat u ten opsigte van die plaaslike owerheid (munisipaliteit)/diensverskaffers ervaar met betrekking tot:

- Water?

- Erfbelasting?

- Elektrisiteit?

- Klaringsertifikate vir heffings?

30 Is daar spesifieke probleme wat u deeltitelskema met betrekking tot banke en ander finansiële instellings ondervind?

31 Het u deeltitelskema 'n vaste beleid rakende reserwefondse en surplusrekeninge?

Ja

Nee

- Indien wel, spesifiseer:

32 Wat is volgens u die twee (2) grootste wanpersepsies wat onder die volgende partye bestaan met betrekking tot u pligte en verantwoordelikhede as trusteevoorsitter:

- Inwoners van die deeltitelskema?

i)

ii)

- Die raad van trustees?

i)

ii)

- Die bestuursagent, indien enige?

i)

ii)

ANNEXURE C

Questionnaire for managing agents

1 How many sectional title schemes are currently being managed by your managing agency?

--

2 What are the three (3) biggest problems that you experience regarding the management of sectional title property?

i) _____

ii) _____

iii) _____

3 What percentage of your clients have:

- Actively involved trustees?
- Trustees who are relatively involved (1-2 meetings per year)?
- Trustees who are not involved at all?
- No board of trustees?

4 Are you aware of the latest stipulations of the Sectional Titles Act?

Yes
No

5 What percentage of your clients make use of the following services that you provide?

- Day-to-day management of the complex
- Administrative tasks
- Compiling of financial statements
- Compiling of budgets
- Collection of levies, amounts receivable etc.
- Other (specify)

6 Do you present sectional title-specific training for your new staff?

Yes
No

7 Are sectional title-specific updating courses presented to your current staff?

Yes
No

8 In your organisation, is there a need for special courses or training, such as legal aspects, insurance, accounting, etc., regarding sectional titles?

Yes
No

- If yes, specify
-
-

9 In your opinion, how many trustees would be the optimal number for a well-functioning board of trustees?

10 What is the average number of persons making up the boards of trustees of your clients at the present moment?

11 In your opinion, does the average trustee chairperson have the necessary knowledge and skills to be a chairperson?

Yes
No
Unsure

12 Are trustees of your clients generally remunerated for their services?

Yes
No
Unsure

- If yes, in what percentage of the complexes is this the case?
- What is the average annual remuneration per trustee?

13 Are the trustee chairpersons of your clients (over and above those in 12 above) remunerated for their services?

Yes
Sometimes
No
Unsure

- If yes, in what percentage of the complexes is this the case?
- What is the average annual remuneration per trustee?

14 What factors/criteria are taken into account in the calculation of your management fees?

15 What is your opinion regarding developers in terms of sectional title property?

16 Are there any specific problems that are experienced when developers are involved in a sectional title scheme?

17 Are the annual general meetings of your clients generally well attended?

Yes
No

18 What are the two (2) most common problems that you experience regarding the annual general meetings of your clients?

i) _____

ii) _____

19 Are the annual financial statements of your clients drawn up by a chartered/professional accountant/firm? Indicate the percentage.

%

	Yes
	No
	Sometimes

- If yes, specify the type of firm that does the work.

CA(SA)
SAIPA
Other

- If other, specify:

20 Are the annual financial statements of your clients audited by a chartered/professional accountant/firm?

Yes
No

- If yes, specify the type of firm that does the work.

CA(SA)
SAIPA
Other

- If other, specify:

- If the financial statements are not audited, what kind of assurance is obtained?

21 Who appoints the auditors of your clients? Indicate the percentage.

%

- The trustee chairperson
- The trustees
- The members of the board of control during the AGM
- We as the managing agent

22 In your opinion, what two (2) factors play the most important role in the decision about the appointment of the accountant/auditor?

i)

ii)

23 Do you find that the time pressure experienced by the auditors/accountants of complexes causes bottleneck situations?

Yes
No

- If yes, are there certain times in the year when the problem is worse?

- Can you suggest a possible solution(s) to the problem?

25 In your opinion, does the auditing of and/or any other sort of assurance about the financial statements add any value to sectional title schemes?

Yes
No
Unsure

- Motivate your answer briefly.

26 In your opinion, what are the two (2) greatest risks in being a managing agent for sectional title schemes?

i)

ii)

27 What are the three (3) greatest problems experienced during the budget process of your clients?

i)

ii)

iii)

28 What are the most significant problems that you experience with the local authority (municipality)/service providers, with regard to:

- Water?

- Rates?

- Electricity?

- Clearance certificates for levies?

29 Are there specific problems that are experienced with regard to banks and other financial institutions of your sectional title clients?

Yes
No

- If yes, specify:

30 Are there specific problems experienced from SARS regarding your sectional title clients?

Yes
No

- If yes, specify:

31 Do your clients have a fixed policy regarding the reserve funds and surplus accounts of their sectional title schemes?

Yes
No

- If yes, specify:

ANNEXURE D

Vraelys aan bestuursagente

- 1 Hoeveel deeltitelskemas word tans deur u bestuursagentskap bestuur?
- 2 Wat is die drie (3) grootste probleme wat u ervaar met betrekking tot die bestuur van deeltiteleiendom?
- i) _____
- ii) _____
- iii) _____
- 3 Watter persentasie van u kliënte het:
- Trustees wat aktief betrokke is?
 - Trustees wat relatief betrokke is (1-2 vergadering per jaar)?
 - Trustees wat glad nie betrokke is nie?
 - Geen raad van trustees nie?
- 4 Is u op die hoogte van die nuutste bepalings rakende die Wet op Deeltitels?
- | |
|-----|
| Ja |
| Nee |
- 5 Watter persentasie van u kliënte maak van die volgende dienste gebruik wat deur u gelewer word?
- Dag-tot-dag-bestuur van kompleks
 - Administratiewe take
 - Opstel van finansiële state
 - Opstel van begrotings
 - Invordering van heffings, bedrae ontvangbaar, ens.
 - Ander (spesifiseer)
- _____
- _____
- 6 Word daar deeltitelspesifieke opleiding vir u **nuwe** personeel aangebied?
- | |
|-----|
| Ja |
| Nee |

7 Word daar deeltitelspesifieke opdateringskursusse vir u **huidige** personeel aangebied?

Ja
Nee

8 Bestaan daar 'n behoefte in u onderneming aan spesiale kursusse of opleiding, bv. regsaspekte, versekering, rekeningkunde, ens. aangaande deeltitels?

Ja
Nee

- Indien wel, spesifiseer
-
-

9 Hoeveel trustees is na u mening die optimale getal vir 'n raad van trustees wat goed funksioneer?

10 Wat is die gemiddelde aantal persone waaruit die rade van trustees van u kliënte op die oomblik bestaan?

11 Beskik die gemiddelde trustee-voorsitter na u mening oor die nodige kennis en vaardighede om as voorsitter op te tree?

Ja
Nee
Onseker

12 Word trustees van u kliënte oor die algemeen vir hul dienste vergoed?

Ja
Nee
Onseker

- Indien wel, vir watter persentasie van komplekse is dit die geval?
- Wat is die gemiddelde jaarlikse vergoeding per trustee?

<input type="text"/>
<input type="text"/>

13 Word u kliënte se trustee-voorsitters (bo en behalwe vir 12 hierbo) vir hul dienste vergoed?

Ja
Soms
Nee
Onseker

- Indien wel, vir watter persentasie van komplekse is dit die geval?
- Wat is die gemiddelde jaarlikse vergoeding per trustee?

14 Watter faktore/kriteria word in ag geneem by die berekening van u bestuursfooie?

15 Wat is u siening rakende ontwikkelaars met betrekking tot deeltiteleindom?

16 Is daar enige spesifieke probleme wat ondervind word wanneer ontwikkelaars by 'n deeltitelskema betrokke is?

17 Word die algemene jaarvergaderings (AJV's) van u kliënte oor die algemeen goed bygewoon?

Ja
Nee

18 Wat is die twee (2) algemeenste probleme wat u ten opsigte van die algemene jaarvergaderings van u kliënte ondervind?

i) _____

ii) _____

19 Word die finansiëlejaarstate van u kliënte deur 'n geoktrooieerde/professionele rekenmeester/firma opgestel? Dui ook die persentasie aan.

%

	Ja
	Nee
	Soms

- Indien wel, spesifeer die tipe firma wat die werk doen:

CA(SA)
SAIPA
Ander

- Indien ander, spesifiseer:

20 Word die finansiële jaarstate van u kliënte deur 'n geoktrooieerde/professionele rekenmeester/firma geoudit?

Ja
Nee

- Indien wel, spesifeer die tipe firma wat die werk doen:

CA(SA)
SAIPA
Ander

- Indien ander, spesifiseer:

- Indien die finansiële state nie geoudit word nie, watter vorm van gerusstelling word verkry?

21 Deur wie word die ouditeure van u kliënte aangestel? Dui ook die persentasie aan.

%

- Die trustee-voorsitter
- Die trustees
- Die lede van die beheerliggaam tydens die AJV
- Ons as die bestuursagent

22 Watter twee (2) faktore speel volgens u die belangrikste rol by die besluit oor die aanstelling van die rekenmeester/ouditeur?

i)

ii)

23 Ondervind u dat tydsdruk wat deur die ouditeure/rekenmeesters van komplekse ervaar word bottelnek-situasies versoorzaak?

Ja
Nee

- Indien wel, is daar sekere tye van die jaar wat die probleem vererger?

- Kan u 'n moontlike oplossing(s) vir die probleem voorstel?
-
-

25 Voeg die ouditering van en/of ander vorm van gerusstelling oor die finansiële state, na u mening, enige waarde toe tot deeltitelskemas?

Ja
Nee
Onseker

- Motiveer u antwoord kortliks.
-
-

26 Wat is volgens u die twee (2) grootste risiko's daaraan verbonde om 'n bestuursagent vir deeltitelskemas te wees?

i)

ii)

27 Wat is die drie (3) grootste probleme wat tydens die begrotingsposes van u kliënte ervaar word?

i)

ii)

iii)

28 Wat is die grootste probleme wat u ten opsigte van die plaaslike owerhede (munisipaliteite)/diensverskaffers ervaar met betrekking tot:

- Water?

- Erfbelasting?

- Elektrisiteit?

- Klaringsertifikate vir heffings?

29 Is daar spesifieke probleme wat ondervind word met betrekking tot banke en ander finansiële instellings van u deeltitelkliënte?

Ja

Nee

- Indien wel, spesifiseer:

30 Is daar spesifieke probleme wat ondervind word met die Suid-Afrikaanse Inkomstediens (SAID) met betrekking tot u deeltitelkliënte?

Ja

Nee

- Indien wel, spesifiseer:

31 Het u kliënte 'n vaste beleid rakende die reserwefondse en surplusrekening van hul deeltitelskemas?

Ja

Nee

- Indien wel, spesifiseer:

ANNEXURE E

Questionnaire for accounting and auditing practitioners

1 How many sectional title schemes are currently clients of yours?

2 What are the three (3) biggest problems that you experience in your firm with regard to the accounting and auditing work of sectional title schemes?

i) _____

ii) _____

iii) _____

3 In your opinion, what is the level of risk (tick **one** option) associated with the auditing of sectional title schemes, in comparison with the auditing of clients in other industries:

- The risk in sectional title auditing is very low
- The risk in sectional title auditing is quite low
- The risk in sectional title auditing is average
- The risk in sectional title auditing is high
- The risk in sectional title auditing is very high

4 Are you up to date regarding the latest stipulations of the Sectional Title Act?

	Yes
	No

5 What percentage of your clients makes use of the following services that are rendered by you?

- Only drawing up of financial statements
- Only auditing of financial statements
- Drawing up and auditing of financial statements
- Drawing up of budgets
- Management advice
- Other (specify)

6 Is sectional title-specific training presented for your **new** staff members?

- To accounting staff?

Yes
No

- To audit staff?

Yes
No

7 Are sectional title-specific updating courses presented for **current** staff who do accounting work or audits of sectional title schemes?

- To accounting staff?

Yes
No

- To auditing staff?

Yes
No

8 Is there a need in your firm for special courses or training on sectional title schemes for **junior** staff?

- For administrative staff?

Yes
No

- If so, specify:

-
- For accounting staff?

Yes
No

- If yes, specify:

-
- For audit staff?

Yes
No

- If yes, specify:
-

9 Is there a need in your firm for special courses or training on sectional title schemes for **senior** staff?

- For administrative staff?

Yes
No

- If so, specify:
-

- For accounting staff?

Yes
No

- If so, specify:
-

- For auditing staff?

Yes
No

- If so, specify:
-

10 Is there a need in your firm for special courses or training on sectional title schemes for **partners/directors**:

Yes
No

- If yes, specify:
-

11 In your opinion, how many trustees is the optimal number for a well-functioning board of trustees?

--

12 In your opinion, does the average trustee chairperson have the necessary knowledge and skills to be a chairperson?

Yes
No
Unsure

13 In your opinion, does the average managing agent have the necessary knowledge and skills to be a managing agent?

Yes
No
Unsure

- 14 How long (hours) does it take on average to:
- draw up the financial statements of a sectional title scheme?

--
 - audit the financial statements of a sectional title scheme?

--

- 15 What is the average post level/qualification of staff who are responsible for:
- drawing up the financial statements of a sectional title scheme?

--
 - auditing the financial statements of a sectional title scheme?

--

- 16 What factors are taken into account in the calculating of fees for a sectional title scheme?
-
-
-

- 17 Do you or any of your staff as auditors attend the annual general meetings of your sectional title clients?
- | |
|-----|
| Yes |
| No |

- 18 Do you find that the time pressure in your firm regarding the audit of sectional title clients regularly causes bottleneck situations?
- | |
|-----|
| Yes |
| No |
- If so, are there certain times of the year when the problem is worse?
-
- Can you suggest possible solution(s) to the problem?
-
-

- 19 In your opinion, does the auditing of the financial statements add any value to the sectional title scheme?
- | |
|--------|
| Yes |
| No |
| Unsure |
- Briefly motivate your answer
-
-

20 In your opinion, what are the two (2) greatest risks attached to the auditing of sectional title schemes?

i)

ii)

21 Which two (2) problems are experienced most with SARS regarding sectional title schemes?

i)

ii)

22 In your opinion, which of the following standards is the most applicable in the drawing up of the financial statements of sectional title schemes?

- IFRS
- IFRS for SMEs
- A standard must be developed specifically for sectional title schemes
- Other (specify)

23 In your opinion, what is the most applicable manner to provide assurance regarding the financial statements of a sectional title scheme?

- A complete audit
- Agreed upon procedures
- An independent review
- Other (specify)

24 What are the most significant problems that you experience with the following organisations/service providers, with regard to the audits of sectional title units?

- Local authorities (municipalities)?

- Other government institutions?

- Banks and other financial institutions?

- Management agencies?

- Other?

25 In your opinion, what are the two (2) greatest misperceptions that exist amongst the following parties with regard to services rendered by you:

- Management agents?

i)

ii)

- Board of trustees?

i)

ii)

26 Any further comments?

ANNEXURE F

Vraelys aan rekenmeesters en ouditpraktisyns

1 Hoeveel deeltitelskemas is tans kliënte van u firma?

--

2 Wat is die drie (3) grootste probleme wat u in u firma ervaar met betrekking tot die rekeningkundige en ouditwerk van deeltitelskemas?

i)

ii)

iii)

3 Wat is na u mening die vlak van risiko geassosieer met die oudit van deeltitelskemas (merk net een opsie), in vergelyking met die oudit van kliënte in ander industrieë:

- Die risiko van deeltitel-oudit is baie laag
- Die risiko van deeltitel-oudit is redelik laag
- Die risiko van deeltitel-oudit is gemiddeld
- Die risiko van deeltitel-oudit is hoog
- Die risiko van deeltitel-oudit is baie hoog

4 Is u op die hoogte van die nuutste bepalings rakende die Wet op Deeltitels?

Ja
Nee

5 Watter persentasie van u kliënte maak van die volgende dienste gebruik wat deur u gelewer word?

- Slegs opstel van finansiële state
- Slegs oudit van finansiële state
- Opstel en oudit van finansiële state
- Opstel van begrotings
- Bestuursadvies
- Ander (spesifiseer)

--

6 Word daar deeltitelspesifieke opleiding vir u **nuwe** personeel aangebied?

- Aan rekeningkundige personeel?

Ja
Nee

- Aan ouditpersoneel?

Ja
Nee

7 Word daar deeltitelspesifieke opdatingskursusse aangebied vir **huidige** personeel wat rekeningkundige werk of oudits van deeltitelskemas doen?

- Vir rekeningkundige personeel?

Ja
Nee

- Vir ouditpersoneel?

Ja
Nee

8 Bestaan daar 'n behoefte in u firma vir spesiale kursusse of opleiding met betrekking tot deeltitelskemas vir **junior** personeel?

- Vir administratiewe personeel?

Ja
Nee

- Indien wel, spesifiseer:

-
- Vir rekeningkundige personeel?

Ja
Nee

- Indien wel, spesifiseer:

-
- Vir ouditpersoneel?

Ja
Nee

- Indien wel, spesifiseer:
-

9 Bestaan daar 'n behoefte in u firma aan spesiale kursusse of opleiding met betrekking tot deeltitelskemas vir **senior** personeel?

- Vir administratiewe personeel?

Ja
Nee

- Indien wel, spesifiseer:
-

- Vir rekeningkundige personeel?

Ja
Nee

- Indien wel, spesifiseer:
-

- Vir ouditpersoneel?

Ja
Nee

- Indien wel, spesifiseer:
-

10 Bestaan daar 'n behoefte in u firma aan spesiale kursusse of opleiding met betrekking tot deeltitelskemas vir **vennote/direkteure**:

Ja
Nee

- Indien wel, spesifiseer:
-

11 Hoeveel trustees is na u mening die optimale getal vir 'n raad van trustees wat goed funksioneer?

--

12 Beskik die gemiddelde trustee-voorsitter na u mening oor die nodige kennis en vaardighede om as voorsitter op te tree?

Ja
Nee
Onseker

13 Beskik die gemiddelde bestuursagent na u mening oor die nodige kennis en vaardighede om as bestuursagent op te tree?

Ja
Nee
Onseker

14 Hoe lank (ure) neem dit gemiddeld om:

- 'n Deeltitelskema se finansiële state op te stel?
- 'n Deeltitelskema se finansiële state te oudit?

15 Wat is die gemiddelde posvlak/kwalifikasie van personeel wat daarvoor verantwoordelik is om:

- 'n Deeltitelskema se finansiële state op te stel?
- 'n Deeltitelskema se finansiële state te oudit?

16 Watter faktore word in ag geneem by die berekening van u fooie vir 'n deeltitelskema?

17 Woon u of van u personeel as ouditeure die algemene jaarvergaderings van u deeltitelkliënte by?

Ja
Nee

18 Ondervind u dat tydsdruk in u firma rakende die oudit van deeltitelklënte gereeld bottelnek-situasies versoorzaak?

Ja
Nee

- Indien wel, is daar sekere tye van die jaar wat die probleem vererger?

-
- Kan u moontlike oplossing(s) vir die probleem voorstel?
-
-

19 Voeg die ouditering van die finansiële state na u mening enige waarde toe tot deeltitelskemas?

Ja
Nee
Onseker

- Motiveer u antwoord kortliks.
-
-

20 Wat is volgens u die twee (2) grootste risiko's daaraan verbonde om deeltitelskemas te oudit?

i)

ii)

21 Watter twee (2) probleme word die meeste met die Suid-Afrikaanse Inkomstediens (SAID) ten opsigte van deeltitelskemas ervaar?

i)

ii)

22 Watter van die volgende standarde is volgens u die toepaslikste om te gebruik by die opstel van finansiële state van deeltitelskemas?

- IFRS
- IFRS for SMEs
- 'n Standaard moet spesifiek vir deeltitelskemas ontwikkel word
- Ander (spesifiser)

23 Wat is volgens u die toepaslikste manier om gerusstelling oor die finansiële state van 'n deeltitelskema uit te spreek?

- 'n Volledige oudit
- Ooreengekome prosedures
- 'n Onafhanklike oorsig
- Ander (spesifiser)

24 Wat is die grootste probleme wat u met die volgende instansies/diensverskaffers, met betrekking tot die oudits van deeltitelskemas ervaar:

- Plaaslike owerhede (munisipaliteite)?

- Ander regeringsinstellings?

- Banke en ander finansiële instellings?

- Bestuursagentskappe?

- Ander?

25 Wat is volgens u die twee (2) grootste wanpersepsies wat onder die volgende partye bestaan met betrekking tot die dienste deur u gelewer:

- Bestuursagente?

i)

ii)

- Rade van trustees?

i)

ii)

ANNEXURE G

Cover letter for interviews

28 February 2012

TO WHOM IT MAY CONCERN

**Interviews for research project for the obtainment of the degree MAcc (Auditing) –
Ms L Lubbe – BAcc (Hons), CTA, CA(SA), CISA, CIA**

For many years, sectional titles has been a well-known concept in the South African property industry and in legislation. There are also many citizens in this country who are living in property registered in terms of legislation of sectional titles. In a country where sufficient housing for citizens still remains a dream, sectional title property will play an ever greater role to assist in satisfying the huge need for housing.

Notwithstanding the fact that sectional titles is a well-known concept, there are still many problems associated with the practice, and relatively little or no academic research has been undertaken on the subject. Managing sectional title complexes, especially, often produces problems because sectional title owners are apathetic towards the management of the complex. Furthermore, the trustees of such complexes are often not well informed about the relevant legislation or the risks attached to sectional title property. This can lead to a situation where a substantial number of complexes are not able to find persons who are prepared to make themselves available to be elected as trustees. In such cases the “management” of the complex is often left to management agents without any, or very few, inputs from the owners of the properties concerned.

Problems such as those mentioned above often widen out to affect members of the boards of trustees of sectional title complexes, and especially the chairpersons of these boards. It may then happen that misperceptions about the roles and functions of the management bodies of sectional title complexes occur. It also appears that there are certain misunderstandings amongst auditors of sectional title complexes and other professional persons who perform “assurance activities” for complexes.

Against this background, an academic research project has been undertaken (in the form of a thesis for the obtaining of the degree MAcc) in order to collect information by means of interviews and incorporating the use of properly structured questionnaires. The interviews will be held with the following three groups of stakeholders:

- Chairpersons of the boards of trustees of sectional title complexes
- Senior management members of bodies corporate of sectional title complexes
- Auditors of sectional title complexes

The three groups of respondents involved have been chosen from persons residing in Bloemfontein. It would be appreciated if you could make available about 45 minutes of your valuable time for an interview, in order to answer the questions posed. Because the respondents represent only a sample of a greater population, your responses are important for the collection of data that is representative of the people that you represent. Any information and answers that you provide will be treated as strictly confidential and there will be no reference made in the study to the respondents in the research project (either to you as individual or to the organisation that you operate/where you work).

The answers that you provide will be processed together with the answers of other respondents in order to determine tendencies, problems, solutions, perceptions etc. By this means the study will provide a valuable contribution towards the finding of solution to the problems as mentioned. Such solutions could be of great value to trustees of sectional title complexes, residents of sectional title complexes, the auditing profession, other professionals who undertake assurance work for sectional title complexes, management bodies of sectional title complexes, property agents and the legal profession.

Thank you very much for being prepared to sacrifice your valuable time to provide answers to these questions – it is highly appreciated.

Yours sincerely

Prof Dave Lubbe

BProc, MCompt, MCom, DCom, CA(SA)

(Study leader)

ANNEXURE H

Dekbrief vir onderhoude

28 Februarie 2012

HDL

Onderhoude vir 'n navorsingsprojek ter verwerwing van die graad MRek (Ouditkunde) – Me L Lubbe - BRek (Hons), STR, CA(SA), CISA, CIA

Deeltitels is reeds vir etlike jare 'n bekende konsep in die Suid-Afrikaanse eiendomsindustrie en wetgewing. Daar is ook talle inwoners van die land wat in eiendom woon wat ingevolge wetgewing op deeltitel geregistreer is. In 'n land waar voldoende behuising vir die inwoners steeds 'n droom bly, gaan deeltiteleiendom in die toekoms 'n steeds groter rol speel om die groot behoeftes aan huisvesting te help bevredig.

Nieteenstaande die feit dat deeltitels 'n bekende konsep is, is daar steeds baie probleme in die praktyk en is daar relatief min, indien enige, akademiese navorsing daarvoor onderneem. Veral die bestuur van deeltitelkomplekse lewer dikwels probleme op deurdat deeltiteleienaars apaties staan teenoor die bestuur van die kompleks. Verder is trustees van sulke komplekse dikwels nie op die hoogte van die betrokke wetgewing en die risiko's verbonde aan deeltiteleiendom nie. Voorafgaande lei selfs daartoe dat 'n wesenlike aantal komplekse soms nie daarin slaag om persone te kry wat bereid is om hulself as trustees verkiesbaar te stel nie. In sulke gevalle word die “bestuur” van komplekse dan dikwels aan bestuursagente oorgelaat sonder enige, of baie min insette vanaf die eienaars van die betrokke eiendom.

Probleme soos hierbo genoem kring dan ook dikwels uit na lede van die trustees van deeltitelkomplekse, en veral die voorsitters van rade van trustees. Daar kom ook gevalle voor waar daar wanpersepsies by inwoners en selfs eienaars van deeltiteleiendom bestaan rakende die rol en funksies van bestuursagente van deeltitelkomplekse. Dit blyk ook dat daar sekere misverstande by ouditeure van deeltitelkomplekse en ander professionele persone mag voorkom wat ander “gerusstellingsaktiwiteite” vir komplekse uitvoer.

Teen bogenoemde agtergrond is daar 'n akademiese navorsingsprojek (’n verhandeling ter verwerwing van die graad MRek) onderneem om inligting deur middel van behoorlik gestruktureerde vraelyste tydens onderhoude in te win. Die onderhoude word onder die volgende drie groepe belanghebbendes uitgevoer:

- Voorsitters van die trustees van deeltitelkomplekse
- Senior bestuurslede van bestuursliggame van deeltitelkomplekse
- Ouditeure van deeltitelkomplekse

Die drie groepe respondente hierbo is gekies uit persone woonagtig in Bloemfontein. Ons sal dit waardeer indien u bereid sou wees om ongeveer 45 minute van u kosbare tyd af te staan om antwoorde op die vrae gestel tydens die onderhoud te verskaf. Aangesien die respondente slegs 'n steekproef uit 'n groter populasie is, is u antwoorde belangrik om data te bekom wat verteenwoordigend is van die populasie van persone wat u verteenwoordig. Antwoorde deur u verskaf en inligting bekom sal as uiters vertroulik hanteer word en daar sal op geen wyse in die studie na respondente wat aan die navorsingsprojek deelgeneem het (u as individu of die onderneming wat u bedryf/waar u werksaam is), verwys word nie.

Die antwoorde wat u verskaf, sal saam met die antwoorde van die ander respondente verwerk word ten einde neigings, tendense, probleme, oplossings, persepsies, ens. te bepaal. Hierdeur sal die studie 'n uiters waardevolle bydrae lewer om oplossings te probeer vind vir genoemde probleme. Sulke oplossings kan van groot waarde wees vir trustees van deeltitelkomplekse, inwoners van deeltitelkomplekse, die ouditeursprofessie, ander professies wat

gerusstellingswerk vir deeltitelkomplekse onderneem, bestuursliggame van deeltitelkomplekse, eiendomsagente en die regsprofessie.

Weer eens dankie dat u bereid is om u kosbare tyd af te staan om antwoorde op hierdie vrae te verskaf. Ons waardeer die opoffering opreg.

Die uwe

Prof Dave Lubbe

BProc, MCompt, MCom, DCom, CA(SA)

(Studieleier)

ANNEXURE I

Summary of list of all sectional title schemes in Bloemfontein

AKTEX - DEEDS REGISTRATION SYSTEM

LIST OF ALL SECTIONAL TITLE SCHEMES IN-BLOEMFONTEIN

DATE : 04APRIL 2012

ISSUED BY DEPARTMENT OF LAND AFFAIRS

PRIVATE BAG X183, PRETORIA, 0001

ENQUIRIES : (012) 338-7059 (TEL)
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SCHEME NAME	SCHEME NUMBER	PROVINCE	SITUATED	ERF NUMBER	NUMBER OF UNITS
SS ZONHEIN	123/1994	FREESTATE	BLOEMFONTEIN	2982,1	
SS ZONNEBLOEM	44/1991	FREESTATE	BLOEMFONTEIN EXT 60	10294,3	
SS ZORBA	225/2009	FREESTATE	LANGENHOVENPARK EXT	1339,0	
SS ZUMA	255/2008	FREESTATE	BLOEMFONTEIN EXT 22	4397,0	
SS ZUNLOU	88/1997	FREESTATE	HILLSBORO	37	
SS ZUNLOU	95/1999	FREESTATE	HILLSBORO	37	
SS 15 ROODDAM	214/2008	FREESTATE	BLOEMFONTEIN RD	2354,15	
SS 23 MOODWATER	42/2008	FREESTATE	BLOEMFONTEIN RD	23,0	
SS 23 MOODWATER	15/2011	FREESTATE	BLOEMFONTEIN RD	23,0	
SS 26650 BEN TINDALL	205/2004	FREESTATE	BLOEMFONTEIN EXT 106	26650,0	
SS 26650 BEN TINDALL	209/2005	FREESTATE	BLOEMFONTEIN EXT 55	8130,0	
SS 27 GENERAAL HERTZOGSTRAAT	238/2009	FREESTATE	BLOEMFONTEIN EXT 109	15936,0	
SS 28 SPITSKOP	365/2008	FREESTATE	BLOEMFONTEIN EXT 109	28,1	
SS 29 KENILWORTH	99/2009	FREESTATE	BLOEMFONTEIN RD	2734,29	
SS 32 NEVILLE HOLMES	30/2010	FREESTATE	BLOEMFONTEIN EXT 111	16819,0	
SS 39 GROENVLEI	19/2007	FREESTATE	BLOEMFONTEIN RD	2844,39	
SS 39 GROENVLEI	249/2009	FREESTATE	BLOEMFONTEIN RD	2844,39	
SS 54 REID	33/1993	FREESTATE	BLOEMFONTEIN	245,RE	
SS 8 MILLE	17/2009	FREESTATE	BLOEMFONTEIN	464,4	

TOTAL OF SECTIONAL TITLE SCHEMES FOR THIS LOCAL AUTHORITY :

3383

2175

CLEARANCE : MANTSOPA LOCAL MUNICIPALITY

SS AT HOME	149/2008	FREESTATE	LADYBRAND	107,2	
SS BEETONPARK	88/1984	FREESTATE	LADYBRAND	284,R/E	
SS BEZMAR	68/2007	FREESTATE	LADYBRAND	248,2	
SS BOTHASTRAAT 7	242/2008	FREESTATE	LADYBRAND	15,3	
SS CASA MIA I	41/1993	FREESTATE	LADYBRAND	224	
SS CASA MIA II	37/1993	FREESTATE	LADYBRAND	226,1	
SS CLOETE VILLAS	172/2006	FREESTATE	LADYBRAND	406,0	
SS CLOETE VILLAS	64/2010	FREESTATE	LADYBRAND	406,0	
SS COSMOS	49/2001	FREESTATE	LADYBRAND	149,0	
SS COSMOS	124/2002	FREESTATE	LADYBRAND	149,0	
SS DA GAMA VILLAS	26/1987	FREESTATE	LADYBRAND	620	
SS DON BOSKO	39/1996	FREESTATE	LADYBRAND	267,3	
SS GROVE	215/2007	FREESTATE	LADYBRAND EXT 1	550,23	
SS HOPOLANG VILLA	188/2006	FREESTATE	LADYBRAND	144,2	
SS LADYBRAND VILLAS	184/2005	FREESTATE	LADYBRAND	626,1	
SS LADYBRAND VILLAS	203/2009	FREESTATE	LADYBRAND	626,1	
SS LELIEHOEK PLACE 1549	214/2009	FREESTATE	LADYBRAND EXT 18	1549,0	
SS LELIEHOEK PLACE 1597	215/2009	FREESTATE	LADYBRAND EXT 18	1597,0	
SS MARIZ VILLAS	29/2012	FREESTATE	LADYBRAND	127,0	
SS MOUNTAIN VIEW VILLAS	86/2008	FREESTATE	LADYBRAND	626,8	
SS NALEDI	305/2008	FREESTATE	LADYBRAND	618,0	
SS QUADRADO VILLAS	32/2002	FREESTATE	LADYBRAND	112,3	
SS SANDSTONE COVE	372/2008	FREESTATE	LADYBRAND EXT 17	1494,0	
SS ST ANNA'S VILLAS	152/2008	FREESTATE	LADYBRAND	282,3	
SS THE VILLAS	27/2010	FREESTATE	LADYBRAND	172,0	
SS VAN RIEBEECK 12	8/2012	FREESTATE	LADYBRAND	14,3	
SS VILLA MONALIZE	21/1998	FREESTATE	LADYBRAND	56,4	

CASH SALE RECEIPT NO : 711344

REF INVOICE NO : 2767430

ACC NO : 888 CASH SERVICES

DATE : 2012/04/05

CLIENT NAME: LLUBBE

PICKING SLIP 272584 150.00

TOTAL R 150.00

PAYMENT TYPE : CASH

*** END OF RECEIPT ***

