

# **REPORT OF THE AUDITOR-GENERAL TO THE FREE STATE LEGISLATURE AND THE COUNCIL ON THE MAFUBE LOCAL MUNICIPALITY**

## **REPORT ON THE FINANCIAL STATEMENTS**

### **Introduction**

1. I was engaged to audit the financial statements of the Mafube Local Municipality set out on pages XX to XX, which comprise the statement of financial position as at 30 June 2014, the statements of financial performance, changes in net assets, cash flows, statement of comparison of budget and actual amounts and the appropriation statement for the year then ended, as well as the notes comprising a summary of significant accounting policies and other explanatory information.

### **Accounting officer's responsibility for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2013 (Act No. 2 of 2013) (DoRA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor-general's responsibility**

3. My responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Because of the matters described in the basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

### **Basis for disclaimer of opinion**

#### **Property, plant and equipment**

4. I was unable to obtain sufficient appropriate audit evidence regarding property, plant and equipment due to lack of an adequate asset management system and a system to maintain the cost records of the assets. The municipality did not review the residual values and useful lives of infrastructure assets at each reporting date in accordance with SA Standards of GRAP, GRAP 17, *Property, plant and equipment* (GRAP 17). I was unable to confirm the assets by alternative means. Consequently, I was unable to determine whether any adjustments to property, plant and equipment stated at R1 584 659 877 (2013: R1 681 116 741) in note 4 to the financial statements were necessary. The municipality also did not capitalise all items of property, plant and equipment in accordance with GRAP 17. Items of property, plant and equipment were incorrectly recognised as work in progress, projects were included at negative values and non-capital expenditure was included as work in progress. Work in progress with a carrying amount of R96 316 843 (2013: R72 993 379) was included in note 4 to the financial statements. I was not able to determine the correct carrying amount of work in progress as it was impracticable to do so.



### **Payables from exchange transactions**

5. I was unable to obtain sufficient appropriate audit evidence for salary control accounts, accrued leave pay, retention creditors, income received in advance and advance payables included in payables from exchange transactions due to the unavailability of reconciliations or support for these balances. I was unable to confirm the balances by alternative means. Consequently, I was unable to determine whether any adjustments to these balances stated at R23 320 029 (2013: R14 132 049) included in the amount of R171 009 712 (2013: R150 196 314) as disclosed in note 17 to the financial statements were necessary. Furthermore differences were identified between the amounts disclosed in the financial statements and external confirmations as well as differences on the credit balances included in the debtors' age analysis. Consequently, payables and expenditure were understated by R5 959 048. There was also a resultant impact on the deficit for the period and the accumulated surplus.

### **Investment property**

6. The municipality did not recognise the correction of investment property of R45 628 985 in 2012/13 as a prior period error in accordance with SA Standards of GRAP, GRAP 3, *Accounting estimates, change in accounting estimates and errors*. The correction of the error was incorrectly disclosed as a reclassification of infrastructure assets. In addition, the municipality did not value investment properties with a carrying amount of R44 487 936 (2013: R44 868 286) in note 3 to the financial statements in accordance with SA Standards of GRAP, GRAP 16, *Investment property* as a number of investment properties had been recognised at zero value; the assumptions used in the investment property register have not been accurately applied in the determination of the deemed cost; and adequate records of the assumptions used in the determination of deemed cost were not kept. I was not able to determine the full extent of the misstatement as it was impracticable to do so.

### **Consumer receivables from exchange transactions**

7. I was unable to obtain sufficient appropriate audit evidence for consumer debtors as service contracts, supporting documents for indigent debtors and applications could not be submitted to confirm the gross debtors. I was also unable to obtain sufficient appropriate audit evidence with regard to the provision for impairment of debtors because supporting documentation for the debt impairment calculation for the current year could not be provided and the provision per service category and consumer type had been apportioned pro rata in relation to the total gross provision for debt impairment for the prior year. I was unable to confirm consumer debtors by alternative means. Consequently, I was unable to determine whether any further adjustments to consumer debtors stated at R35 926 954 (2013: R35 257 255) in note 11 to the financial statements was necessary.

### **Unspent conditional grants and receipts**

8. The municipality did not accurately roll forward the balance of unspent conditional Municipal Infrastructure Grants (MIG) from the prior year financial statements in accordance with SA Standards of GRAP, GRAP 23, *Revenue from non-exchange transactions*. Where the municipality had spent its own funds before MIG allocations were received the amount receivable was not recognised in the prior year. Consequently, unspent conditional grants as disclosed in note 14 to the financial statements are understated and grant expenditure (capital or operating) is overstated by R4 352 283, respectively for the 2012/13 and 2013/14 financial years. The municipality also did not have adequate processes in place to ensure that VAT relating to unspent grants had been correctly accounted for in the prior year.



9. I was unable to obtain sufficient appropriate audit evidence for the difference in the opening balance of R2 239 000 of the Integrated National Electrification Grant due to inadequate record keeping by the municipality. I was unable to confirm the balance by alternative means. Consequently, I was unable to determine whether any adjustments to Integrated National Electrification Grant stated at R776 235 (2013: R5 002 447) as disclosed in note 14 to the financial statements was necessary.

#### **Value added tax**

10. I was unable to obtain sufficient appropriate audit evidence for value-added tax (VAT) payable due to inadequate record keeping by the municipality. I was unable to confirm the balance by alternative means. Consequently, I was unable to determine whether any adjustments to VAT payable stated at R13 388 504 (2013: R7 628 085) as disclosed in note 18 to the financial statements was necessary. In addition the municipality did not claim input VAT on all expenses as per the Value-added Tax Act of South Africa, 1991 (Act No. 89 of 1991). Consequently, VAT payable and general expenditure are overstated by R2 934 420. Additionally, there was a resultant impact on the deficit and the accumulated surplus for the period.

#### **Employee benefits**

11. The municipality did not recognise the post-retirement benefit in accordance with SA Standards of GRAP, GRAP 25, *Employee benefits* due to incorrect information being included in the calculation of the retirement benefit obligation of R11 474 814 (2013: R11 474 814) as disclosed in note 7 to the financial statements. I was not able to determine the correct amount of the post-retirement benefit obligation for the current and prior financial years as it was impracticable to do so.

#### **Receivables from exchange transactions**

12. I was unable to obtain sufficient appropriate audit evidence for receivables from exchange transactions as supporting documentation for councilor overpayment, impairment and other receivables included in note 9 to the financial statements could not be provided. I was unable to confirm these balances by alternative means. Consequently, I was unable to determine whether any adjustment to receivables from exchange transactions stated at R3 659 010 (2013: R2 070 855) in note 9 to the financial statements was necessary.

#### **Receivables from non-exchange transactions**

13. I was unable to obtain sufficient appropriate audit evidence for receivables from non-exchange transactions as supporting documentation could not be provided for the gross balance. Support could also not be provided for the process followed for the calculation of debt impairment. I was unable to confirm the balance by alternative means. Consequently, I was unable to determine whether any adjustment to receivables from non-exchange transactions stated at R1 947 305 (2013: R3 586 867) in note 10 to the financial statements was necessary.

#### **Depreciation and amortisation**

14. I was unable to obtain sufficient appropriate audit evidence for depreciation and amortisation due to the scope limitation placed on my audit of property, plant and equipment. I was unable to confirm the depreciation and amortisation by alternative means. Consequently, I was unable to determine whether any adjustments to depreciation and amortisation stated at R122 993 232 (2013: R123 676 891) as disclosed in note 33 to the financial statements were necessary.



## **Government grants and subsidies**

15. I was unable to obtain sufficient appropriate audit evidence for conditions met for government grants and subsidies transferred to the statement of financial performance due to the absence of supporting records. I was unable to confirm government grants and subsidies by alternative means. Consequently, I was unable to determine whether any further adjustments to government grants and subsidies stated at R96 174 682 as disclosed in note 24 to the financial statements were necessary. Furthermore, an amount of R2 145 866 that needed to be transferred to revenue for conditions met was not transferred to revenue. Revenue and grants are therefore understated by this amount.

## **Employee related cost**

16. I was unable to obtain sufficient appropriate audit evidence for employee related cost as no reconciliations were performed between the payroll system and general ledgers, resulting in material unexplained differences. I could not confirm employee cost by alternative means. Consequently I was unable to determine whether any adjustments to employee related cost stated at R69 615 960 as disclosed in note 28 in the financial statements were necessary. Furthermore, travel and subsistence expenditure was incorrectly included in employee related cost, resulting in the overstatement of employee related cost and understatement of general expenses by R1 437 442 (2013: R1 409 800) respectively.

## **Service charges**

17. I was unable to obtain sufficient appropriate audit evidence regarding service charges as the municipality did not have adequate systems in place to maintain records of basic charges and service charges and record accurate meter readings. I was unable to confirm the service charges by alternative means. Consequently, I was unable to determine whether any adjustments to service charges stated at R47 117 457 (2013: R43 222 421) as disclosed in note 23 to the financial statements were necessary. Furthermore, the municipality did not measure revenue at the fair value of the consideration received or receivable as required by SA Standards of GRAP, GRAP 9 *Revenue from exchange transactions* and I was not able to determine the full extent of the misstatement as it was impracticable to do so. Additionally, there was a resultant impact on the deficit for the period and the accumulated surplus.

## **General expenses**

18. I was unable to obtain sufficient appropriate audit evidence to support the amounts allocated for general expenses. I could not confirm these expenses by alternative means. Consequently, I was unable to determine whether any adjustments to general expenses stated at R24 440 709 as disclosed in the statement of financial performance in the financial statements were necessary.

## **Property rates**

19. I was unable to obtain sufficient appropriate audit evidence for property rates due to an unsubstantiated difference between the chargeable rates per the valuation roll, the accounting records and the financial statements. I was unable to confirm the property rates by alternative means. Consequently, I was unable to determine whether any adjustments to property rates stated at R19 474 278 (2013: R16 322 286) in note 22 to the financial statements were necessary.

## **Repairs and maintenance**

20. I was unable to obtain sufficient appropriate audit evidence to support the amounts allocated for repairs and maintenance. I could not confirm these expenses by alternative means. Consequently, I was unable to determine whether any adjustments to repairs and maintenance stated at R11 206 908 as disclosed in the statement of financial performance in the financial statements were necessary.



### **Remuneration of councillors**

21. I was unable to obtain sufficient appropriate audit evidence for remuneration of councillors as there were material unexplained differences between the salary system and the amounts recorded in the general ledger. I could not confirm councillors' remuneration by alternative means. Consequently I was unable to determine whether any adjustments to remuneration of councillors stated at R5 235 182 as disclosed in note 29 in the financial statements were necessary.

### **Finance costs**

22. I was unable to obtain sufficient appropriate audit evidence for finance costs due to the absence of supporting records. I was unable to confirm finance costs by alternative means. Consequently, I was unable to determine whether any further adjustment to finance costs stated at R6 566 642 (2013: R7 278 597) in note 34 in the financial statements was necessary.

### **Pension and medical aid deductions**

23. I was unable to obtain sufficient appropriate audit evidence for the opening and closing balance of pension fund and medical aid deductions as disclosed in note 49 to the financial statements as it does not agree with their financial transactions recorded in the general ledger. I was unable to confirm the amount by alternative means. Consequently, I was unable to determine whether any further adjustments to pension fund and medical aid deductions stated at R10 453 233 (2013: R1 727 039) as disclosed in note 49 in the financial statements were necessary.

### **Other income**

24. I was unable to obtain sufficient appropriate audit evidence for other income due to a lack of proper processes to ensure that registers for all other income are maintained. I was unable to confirm the other income by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to other income stated at R770 175 (2013: R2 244 696) as disclosed in note 26 to the financial statements. In addition, other income for the prior year transactions was not disclosed in accordance with SA Standards of GRAP, GRAP1, *Presentation of financial statements* (GRAP 1) due to incorrect classification and disclosures. I was not able to determine the correct carrying amount of work in progress as it was impracticable to do so.

### **Unauthorised expenditure**

25. The municipality did not include all unauthorised expenditure and did not adhere to the disclosure requirements in note 46 to the financial statements as required by section 125(2)(d) of the MFMA. The municipality incurred expenditure in excess of the approved budget which was not disclosed as unauthorised expenditure, resulting in unauthorised expenditure being understated by R168 726 113 (2013: R186 610 002).

### **Irregular expenditure**

26. The municipality did not include particulars of all the irregular expenditure incurred in the notes to the financial statements, as required by section 125(2)(d)(i) of the MFMA. I was not able to determine the full extent of the misstatement as it was impracticable to do so. The municipality made payments in contravention of the *Supply chain management regulations* which were not included in irregular expenditure, resulting in irregular expenditure being understated by R13 260 890 (2013: R90 052 312). An amount of R71 142 949 for the prior year was deducted from the balance of irregular expenditure in note 48 without proper investigations having been performed. This resulted in a further understatement of irregular expenditure by R71 142 949 (2013: R71 142 949).



## **Commitments**

27. I was unable to obtain sufficient appropriate audit evidence for capital commitments due to an inadequate contract management system and incomplete contract register as well as the restatement of the corresponding figure. Several unexplained differences/misstatements were identified in the current and prior years which could not be agreed to the financial records. I was unable to confirm the disclosure by alternative means. Consequently, I was unable to determine whether any adjustments to commitments stated at R58 207 711 (2013: R32 821 971) as disclosed in note 40 in the financial statements were necessary.

## **Fruitless and wasteful expenditure**

28. The municipality did not include particulars of all fruitless and wasteful expenditure incurred in the notes to the financial statements, as required by section 125(2)(d)(i) of the MFMA. I was not able to determine the full extent of the misstatement as it was impracticable to do so. An amount of R17 727 744 for the prior year was deducted from the balance of fruitless and wasteful expenditure in note 47 without proper investigations having been performed. This resulted in an understatement of fruitless and wasteful expenditure by R17 727 744 (2013: R17 727 744).

## **Contingencies**

29. The municipality did not disclose all contingencies in accordance with SA Standards of GRAP 19, *Provisions, contingent liabilities and contingent assets*. According to external confirmation obtained, legal proceedings amounting to R12 512 700 were instituted against the municipality and should have been disclosed as contingencies. The disclosure for contingencies in note 41 to the financial statements was therefore understated by R12 512 700.

## **Cash flow statement**

30. I was unable to obtain sufficient appropriate audit evidence as to whether the cash flow statement and related notes for the current and prior years were fairly stated due to the material effect of misstatements and scope limitations identified in the financial statements, as set out in this report. I was unable to confirm the cash flow by alternative means. Consequently, I was unable to determine whether adjustments were necessary to the amounts disclosed in the cash flow statement.

## **Comparison of budget and actual amounts**

31. I was unable to obtain sufficient appropriate audit evidence for the differences between the statement of financial performance and the actual results contained in the statement of comparison of budget and actual amounts. I was also unable to obtain sufficient appropriate evidence about the budgeted figures as disclosed. This was due to material differences between the amounts disclosed and the actual budget prepared by the municipality. I was unable to confirm these differences by alternative means. I was therefore unable to determine whether adjustments to the statement of comparison of budget and actual amounts were necessary.

## **Public private partnership**

32. The municipality did not disclose the detail of the public private partnership between the municipality and electricity service provider as required by IFRIC 12, *Service concession arrangements*.



### **Related parties**

33. The municipality incorrectly included employee benefits in related parties as disclosed in note 42 to the financial statements. The disclosure for related parties in note 42 to the financial statements was therefore overstated by R7 186 712 (2013: R6 235 258).

### **Distribution losses**

34. The municipality did not include particulars of material losses in the notes to the financial statements as required by section 125(2)(d)(i) of the MFMA. I was not able to determine the full extent of the misstatement as it was impracticable to do so.

### **Comparatives figures**

35. The municipality did not disclose the reclassification of comparative figures as required by GRAP 1. In note 43 it was disclosed that certain comparative figures had been reclassified, while the disclosures for note 4 on property plant and equipment, note 28 on employee-related cost, note 48 on irregular expenditure and note 49 on PAYE, UIF and SDL were not presented accordingly.

### **Financial Instruments**

36. The amount disclosed as financial instruments in note 20 for payables from exchange transactions is stated as R156 923 846, while in note 17 payables from exchange transactions amounted to R171 009 712. Payables from exchange transactions are therefore misstated by R14 085 866 in note 20 to the financial statements.

### **Aggregation/ Accumulation of immaterial uncorrected misstatements**

37. I was unable to obtain sufficient appropriate audit evidence regarding the following items making up the statement of financial position and the statement of financial performance, which had a cumulative effect on the financial statements:

- Recoveries as disclosed in the statement of financial performance at R1 070 688.
- Finance lease obligations in the statement financial position and note 13 at R1 235 308.

I was unable to confirm these items by alternative means. As a result, I was unable to determine whether any further adjustments to these itemss were necessary.

### **Going Concern**

38. The municipality has prepared financial statements on a going concern basis, but there are a number of indicators that its financial sustainability is under threat. These include the material increase in trade payables and consumer receivables/indigent debtors, with only 40% of the amount levied being recovered, and cash equivalents of R64 367, which include unspent conditional grants of R21 611 165 at year-end. The municipality also incurred net deficits of R133 184 980 (2013: R123 004 723) and unauthorised expenditure of R37 837 331 during the current financial period. The municipality's ability to continue to render the required services is dependent on a number of factors, the most significant being that the accounting officer can continue to procure funding for the ongoing operations of the municipality.

### **Disclaimer of opinion**

39. Because of the significance of the matters described in the basis for disclaimer of opinion paragraphs, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.



### **Emphasis of matters**

40. I draw attention to the matter below. My opinion is not modified in respect of the matter.

### **Material impairments**

41. As disclosed in note 10 to the financial statements, a provision for impairment of debtors amounting to R15 091 223 (2013: R12 246 285) has been made with regard to irrecoverable receivables from non-exchange transactions. In addition, as disclosed in note 11 to the financial statements, a provision for impairment of debtors amounting to R152 561 826 (2013: R118 325 381) has been made with regard to irrecoverable consumer debtors.

### **Additional matters**

42. I draw attention to the matters below. My opinion is not modified in respect of these matters.

### **Unaudited disclosure notes**

43. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion thereon.

### **Unaudited supplementary schedules**

44. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.

### **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

45. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report, non-compliance with legislation as well as internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express and opinion or conclusion on these matters.

### **Predetermined objectives**

46. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2014:
- KPA4: Community services (on pages x to x)
  - KPA5: Infrastructural services (on pages x to x).
47. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
48. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned development priorities. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).
49. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
50. The material findings in respect of the selected development priorities are as follows:



## **KPA 4 – Community services**

### **Usefulness of reported performance information**

51. Section 41(c) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) requires the integrated development plan to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 75% of the reported objectives, 69% of the reported indicators and 73% of the reported targets were not consistent with those in the approved integrated development plan. This was due to a lack of oversight responsibility regarding financial and performance reporting and compliance and related internal controls.
52. The FMPPI requires the following:
- Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 100% of the targets were not specific.
  - Performance targets must be measurable. I could not measure the required performance for 100% of the targets.
  - Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 100% of the indicators were not well defined.
  - Performance indicators must be verifiable, meaning it must be possible to validate the processes and systems that produced the indicator. A total of 100% of the indicators were not verifiable.

The reasons for this were failure by management to adhere to the requirements of the FMPPI and a lack of proper systems and processes and technical indicator descriptions.

53. The FMPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. The relevance of the indicators could not be assessed due to a lack of corroborative supporting evidence to verify management's explanation for why the indicators were considered important and relevant to the realisation of strategic goals and objectives.

### **Reliability of reported performance information**

54. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of the reported performance information. This was due to limitations placed on the scope of my work due to the absence of information systems, the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information and the auditee's records not permitting the application of alternative audit procedures.

## **KPA 5 – Infrastructural services**

### **Usefulness of reported performance information**

55. Section 41(c) of the MSA requires the integrated development plan to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 20% of the reported indicators and 20% of the reported targets were not consistent with those in the approved integrated development plan. This was due to a lack of oversight of financial and performance reporting and compliance and related internal controls.



56. The FMPPI requires the following:

- Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 88% of the targets were not specific.
- Performance targets must be measurable. I could not measure the required performance for 96% of the targets.
- Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 100% of the indicators were not well defined.
- Performance indicators must be verifiable, meaning that it must be possible to validate the processes and systems that produced the indicator. A total of 100% of the indicators were not verifiable.

This was because management did not adhere to the requirements of the FMPPI and a lack of proper systems and processes and technical indicator descriptions.

### **Reliability of reported performance information**

57. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of the reported performance information. This was due to limitations placed on the scope of my work due to the absence of information systems, the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information and the auditee's records not permitting the application of alternative audit procedures.

### **Additional matter**

58. I draw attention to the following matter:

### **Achievement of planned targets**

59. Refer to the annual performance report on page(s) x to x and x to x for information on the achievement of the planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information for the selected development priorities reported in paragraph(s) 51 to 57 of this report.

### **Compliance with laws and regulations**

60. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

### **Annual financial statements and annual report**

61. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements identified by the auditors in the submitted financial statements were not adequately corrected and the supporting records could not be provided subsequently, which resulted in the financial statements receiving a disclaimer audit opinion.
62. The 2012-13 annual report was not tabled in the municipal council within seven months after the end of the financial year, as required by section 127(2) of the MFMA.
63. Oversight report, containing comments on the annual report, was not adopted by council within two months from the date on which the 2012-13 annual report was tabled, as required by section 129(1) of the MFMA.



### **Audit committees**

64. A performance audit committee was not in place and the audit committee was not used to fulfil the performance audit committee function, as required by municipal planning and performance management regulation (MPPM) 14(2)(a).
65. The audit committee did not advise the council on matters relating to internal financial control, accounting policies, effective governance, performance management and performance evaluation as required by section 166(2)(a) of the MFMA.
66. The audit committee did not advise the council on matters relating to compliance with legislation, as required by section 166(2)(a)(vii) of the MFMA.

### **Internal audit**

67. The internal audit unit did not function as required by section 165(2) of the MFMA in that it did not advise the accounting officer and/or report to the audit committee on matters relating to the internal controls, accounting procedures and practices and loss control.

### **Human resource management**

68. The municipality did not develop and adopt appropriate systems (policies) and procedures to monitor measure and evaluate performance of staff, in contravention of section 67(d) of the MSA.
69. An acting chief financial officer was appointed for a period of more than six months, in contravention of section 54A(2A)(a-b) of the MSA.
70. The competencies of financial and supply chain management officials were not assessed in a timely manner in order to identify and address gaps in competency levels as required by regulation 13 of the *Municipal regulations on minimum competency levels*.
71. The municipality did not submit a report on compliance with prescribed competency levels to the National Treasury and relevant provincial treasury, as required by regulation 14(2)(a) of the *Municipal regulations on minimum competency levels*.
72. The annual report of the municipality did not reflect information on compliance with prescribed minimum competencies, as required by regulation 14(2)(b) and 14(3) of the *Municipal regulations on minimum competency levels*.

### **Expenditure management**

73. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
74. An adequate management, accounting and information system which accounted for creditors was not in place, as required by section 65(2)(b) of the MFMA.
75. Reasonable steps were not taken to prevent unauthorised, irregular and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

### **Revenue management**

76. An adequate management, accounting and information system which accounts for revenue was not in place, as required by section 64(2)(e) of the MFMA.

### **Consequence management**

77. Unauthorised, irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine whether any person was liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.
78. Authorisation of unauthorised expenditure was not done through an adjustment budget, as required by section 32(2)(a)(i) of the MFMA.



## **Procurement and contract management**

79. Goods and services with a transaction value of below R200 000 were in certain instances procured without obtaining the required price quotations and in other instances sufficient appropriate audit evidence could not be obtained that the required price quotations were obtained, as required by supply chain management (SCM) regulation 17(a) and (c).
80. Quotations were accepted from prospective providers who were not registered on the list of accredited prospective providers and did not meet the listing requirements prescribed by the SCM policy, in contravention of SCM regulations 16(b) and 17(b).
81. Sufficient appropriate audit evidence could not be obtained that goods and services of a transaction value above R200 000 were procured by inviting competitive bids, as required by SCM regulation 19(a).
82. Sufficient appropriate audit evidence could not be obtained that bid specifications for procurement of goods and services through competitive bids were drafted in an unbiased manner that allowed all potential suppliers to offer their goods or services, as required by SCM regulation 27(2)(a).
83. Sufficient appropriate audit evidence could not be obtained that bid specifications were drafted by bid specification committees which were composed of one or more officials of the municipality, as required by SCM regulation 27(3).
84. Sufficient appropriate audit evidence could not be obtained that bids were evaluated by bid evaluation committees which were composed of officials from the departments requiring the goods or services and at least one SCM practitioner of the municipality, as required by SCM regulation 28(2).
85. Awards were made to bidders other than those recommended by the bid evaluation committee without ratification by the accounting officer, as required by SCM regulation 29(5)(b).
86. Contracts were awarded to bidders that did not score the highest points in the evaluation process, as required by section 2(1)(f) of the Preferential Procurement Policy Framework Act of South Africa, 2000 (Act no. 5 of 2000).
87. Sufficient appropriate audit evidence could not be obtained that contracts were only awarded to and quotations only accepted from bidders who had submitted a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
88. Awards were made to providers who are in the service of the municipality and whose directors are in the service of the municipality, in contravention of section 112(j) of the MFMA and SCM regulation 44. Furthermore, the provider failed to declare that he/she was in the service of the municipality, as required by SCM regulation 13(c). Similar non-compliance was reported in the prior year and the municipality did not take disciplinary action against the suppliers/officials involved.
89. Awards were made to providers who are in the service of other state institutions or whose directors are in the service of other state institutions, in contravention of section 112(j) of the MFMA and SCM regulation 44. Similar awards were identified in the prior year and no effective steps were taken to prevent or combat the abuse of the SCM process in accordance with SCM regulation 38(1).
90. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM regulation 46(2)(e).
91. SCM officials/ other SCM role players who or whose close family members/ partners had a private or business interest in contracts awarded by the municipality participated in the process relating to that contract, in contravention of SCM regulation 46(2)(f).



92. Sufficient appropriate audit evidence could not be obtained that contracts were only awarded to and quotations were only accepted from providers whose tax matters had been declared by the South African Revenue Service to be in order, as required by SCM regulation 43.
93. Sufficient appropriate audit evidence could not be obtained that contracts were only extended or modified after tabling the reasons for the proposed amendment in the council of the municipality, as required by section 116(3) of the MFMA.
94. Sufficient appropriate audit evidence could not be obtained that all extension or modification to contracts were approved by a properly delegated official, as required by SCM Regulation 5.
95. The contract performance and monitoring measures and methods were insufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA.

#### **Budget**

96. Expenditure was not incurred in accordance with the approved budget and was in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of sections 15 of the MFMA.

#### **Conditional grants**

97. MIG funds were retained or rolled over to the next financial year without the approval of the National Treasury, as required by section 21(1) of DoRA.

#### **Asset management**

98. The municipality did not establish an investment policy that was adopted by council, as required by section 13(2) of the MFMA and municipal investment regulation 3(1)(a).
99. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.
100. An effective system of internal control for assets (including an asset register) was not in place, as required by section 63(2)(c) of the MFMA.

#### **Strategic and annual planning process**

101. The local community was not afforded the opportunity to comment on the final draft of the integrated development plan (IDP) before adoption, as required by section 42 of the MSA and MPPM regulations 9, 13(1), 13(4)(c) and 15(3).
102. The municipality did not give effect to its IDP and conduct its affairs in a manner which was consistent with its IDP, as required by section 36 of the MSA, section 21(2)(a) of the MFMA and MPPM regulation 6.
103. The municipality did not establish a performance management system, as required by section 38(a) of the MSA.
104. The municipality did not establish mechanisms to monitor and review its performance management system, as required by section 40 of the MSA.
105. Key performance indicators, including input, output and outcome indicators, in respect of each of the development priorities and objectives were not set out in the IDP, as required by section 41(1)(a) of the MSA and MPPM regulations 1 and 9(1)(a).
106. Measurable performance targets for the financial year with regard to each of the development priorities or objectives and key performance indicators were not set in the IDP, as required by section 41(1)(b) of the MSA and MPPM regulations 12(1) and 12(2)(e).
107. The performance of the municipality was not assessed during the first half of the financial year, as required by section 72(1)(a)(ii) of the MFMA.



108. The annual performance report for the year under review did not include a comparison with the previous financial year and measures taken to improve performance, as required by section 46(1)(b) and (c) of the MSA.
109. The annual performance agreements for the municipal manager and all senior managers are not linked to the measurable performance objectives approved with the budget and to the service delivery budget implementation plan, as required by of section 53(1)(c)(iii) of the MFMA and section 57(1)(b) of the MSA.
110. The performance management system and related controls were not in place as it did not describe and represent the processes of performance planning/ monitoring/ measurement/ review/ reporting/ improvement and how it is conducted, organised and managed, including determining the roles of the different role players, as required by sections 38 of the MSA and MPPM regulation 7.

#### **Environmental waste management**

111. The municipality operated their waste disposal sites without a waste management licence or permit, in contravention of section 20(b) of the National Environmental Management: Waste Act of South Africa, 2008 (Act No. 59 of 2008).

#### **Internal control**

112. I considered internal control relevant to my audit of the financial statements, the performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for the disclaimer of opinion and the findings on the performance report and compliance with laws and regulations included in this report.

#### **Leadership**

113. Management did not adequately respond to the AGSA's message as they did not effectively discharge their oversight responsibilities to ensure an improvement in the audit outcome.
114. The leadership did not always take timely and adequate action to address weaknesses in the finance and supply chain management directorate due to lack of monitoring and supervision, which resulted in non-compliance with applicable legislation and gave rise to irregular expenditure.
115. Leadership did not continuously implement preventive measures to address weaknesses in the control environment to promote ethical values and good governance that protects and enhance the interests of the municipality since there were no processes in place to enable effectiveness of internal controls that ensures reliability and validity of financial information. Deviations from the expected standards of conduct were not followed up to ensure that remedial or disciplinary action was taken in a timely and consistent manner. Overriding of internal controls occurred which resulted in a high number of irregular and fruitless expenditure where value for money was not always obtained which resulted in potential cases of fraud that needs to be investigated by management.
116. Consequence management was not effective as the council did not investigate instances of unauthorised, irregular, fruitless and wasteful expenditure to determine whether any person was liable for the expenditure as the council neglected to appoint a committee to investigate the expenditure.

#### **Financial and performance management**

117. Proper record keeping was not implemented in a timely manner to ensure that complete, relevant and accurate information is accessible and available to support financial and performance reporting, as management did not monitor to determine whether the controls were implemented effectively.



118. Effective performance systems, processes and procedures as well as the management thereof had not been adequately developed and implemented due to a lack of capacity.
119. Inadequate filing procedures at the municipality resulted in limitations of scope during the current and previous year's audits due to lack of monitoring. As a result, significant difficulties were experienced in respect of the availability of information.
120. The financial statements were not properly reviewed for completeness and accuracy prior to submission for auditing due to a lack of skilled staff.
121. Management also did not establish effective monitoring and evaluation components or processes within its finance and strategic planning directorates to regularly review and monitor management's compliance with laws and regulations and internally designed policies and procedures due to capacity problems. As a result, significant non-compliance issues were noted that could have been prevented.

#### **Governance**

122. Ongoing monitoring and supervision were not undertaken to enable an assessment of the effectiveness of internal control over financial and performance reporting due to the fact that the chief financial officer position was vacant for most of the financial year. Thus internal control deficiencies were not identified, communicated and corrected in a timely manner.
123. The implementation of external audit recommendations was not prioritised and also not monitored. This resulted in the prior year audit findings not being addressed.
124. As a result of the ineffective functioning of the internal audit unit, as well as inadequate support by management, the audit committee could not adequately promote accountability and service delivery by evaluating and monitoring responses to risks and providing oversight of the effectiveness of the internal control environment, including financial and performance reporting and compliance with laws and regulations.

*Auditor-General*

Bloemfontein

30 November 2014



AUDITOR - GENERAL  
SOUTH AFRICA

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