

REPORT OF THE AUDITOR-GENERAL TO THE FREE STATE LEGISLATURE AND THE COUNCIL ON THE PHUMELELA LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the Phumelela Local Municipality, which comprise the statement of financial position as at 30 June 2011, and the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, a summary of significant accounting policies and other explanatory information, as set out on pages [xx] to [xx].

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these 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, 2010 (Act No. 1 of 2010) (DoRA) and for such internal controls as management determines 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. As required by section 188 of the Constitution of the Republic of South Africa, 1996 (Act No. 108 of 1996) and section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with International Standards on Auditing and General Notice 1111 of 2010 issued in *Government Gazette 33872 of 15 December 2010*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

individual debtors which are considered doubtful as required by the South African Statement of Generally Accepted Accounting Practice, IAS 39 (AC 133), Financial instruments: Recognition and measurement. The entity's records did not permit the application of alternative audit procedures to confirm the compliance with the above mentioned standard and the existence, valuation and obligations of the provision for doubtful debts.

19. The trade receivables balance of R53 380 784 (2010: R40 437 381), as disclosed in note 14 to the financial statements does not agree to the balance of R61 946 652 (2010: 40 502 468) per the debtors' age analysis. The municipality did not reconcile the difference of R8 565 868 (2010: 65 087) between the financial statements and the underlying records. I was unable to determine the effect on the other account balances or classes of transactions contained in the financial statements.
20. Suspense accounts with net debit effect of R2 558 070 (R944810 credit and R3 502 880 debit) were included in the trade and other receivables from exchange transactions. These suspense accounts were not cleared at the year end as required by section 65(2)(j) of the MFMA. I was unable to obtain sufficient appropriate evidence to support the transactions and balances included in these suspense accounts. The completeness and classification of these transactions could not be consequently confirmed.
21. The municipality could not provide sufficient appropriate audit evidence to support debtors with credit balances amounting to R122 465. The municipality also could not provide sufficient appropriate audit evidence to support other receivables from non-exchange transactions amounting to R653 249. Furthermore, I could not confirm the existence of debtors amounting to R575 516 as no payments were received from these debtors during the financial year and subsequent to year end. The entity's records did not permit the application of alternative audit procedures to confirm the existence, valuation, rights of trade and other receivables.

Property, plant and equipment

22. The Accounting policy did not indicate that the municipality has taken advantage of the Transitional Provisions for the adoption of Standards of Generally Recognized Accounting Practice (GRAP) by Medium and Low Capacity Municipalities, Directive 4 and as a result; the municipality has not applied subsequent measurement which requires that the depreciation be calculated over the depreciable amount for all assets owned by the municipality. Accordingly I could not confirm the valuation of Property, plant and equipment amounting to R185 842 677 (2010: R157 071 000).
23. Standards of Generally Recognized Accounting Practice, GRAP 17, Property, plant and equipment requires that subsequent to initial recognition at cost, an item of property, plant and equipment should be carried at cost less accumulated depreciation and accumulated impairment losses. As indicated in note 5 to the financial statements, plant and equipment were not depreciated during the financial year. The amount of depreciation not provided for and consequently the effect on accumulated surplus cannot be quantified as the fixed asset register does not indicate dates when the assets were purchased.
24. The entity did not capitalise infrastructure assets which were completed during the year in accordance with Standard of Generally Recognised Accounting Practice, GRAP 17, Property, plant and equipment. Had this capitalisation been done in line with the entity's policies and practices on capitalisation, infrastructure assets, included in note 5 to the

R35 933 438. The entity's records did not permit the application of alternative audit procedures to confirm the completeness and valuation of investment property.

31. Additionally, other investment property as per the complete fixed asset register could not be located and physically inspected. I was therefore unable to confirm the existence, valuation and allocation and rights of investment property disclosed in note 4 to the financial statements. The entity's records did not permit the application of alternative audit procedures to confirm these properties.

Non-current assets held for sale

32. The municipality has disclosed all assets that it has set aside for write-off as non-current assets held for sale. GRAP 100 – Non-current assets held for sale, requires that assets only be classified as non-current assets held for sale when their carrying amount will be recovered principally through a sale transaction. Writing-off of these assets therefore does not qualify as a sales transaction and the full amount of non-current assets held for sale reflected at R7 353 642 on the face of the statement of financial position and note 16 in the notes to the financial statements is incorrect and should still be classified under property, plant and equipment until they are written-off. Furthermore, I could not verify the existence, valuation and allocation and rights of non-current assets held for sale.
33. Although the full amount disclosed as non-current assets held for sale do not qualify for recognition as such as per GRAP 100 – Non-current assets held for sale. The Non-current assets held for sale balance of R7 353 642 (2010: Nil) as disclosed in note 16 to the financial statements, does not agree to the balance of R8 013 084 (2010: Nil) as per the listing provided for audit purposes. The entity did not reconcile the difference of R659 442 (2010: Nil) between the financial statements and the underlying accounting records. Consequently, the non-current assets held for sale balance is understated by R659 442 (2010: Nil). I was unable to determine the effect on the other account balances or classes of transactions contained in the financial statements.

Financial assets

34. I was unable to obtain sufficient appropriate audit evidence to support financial assets amounting to R708 318 (2010: 648 676) as disclosed in note 7 to the annual financial statements and as a result I could not confirm the valuation, existence and rights of financial assets. The entity's records did not permit the application of alternative audit procedures to confirm the valuation, existence and rights of financial assets.

Value added tax (VAT)

35. The municipality could not provide sufficient appropriate audit evidence to support journal entries that were processed against the VAT accounts amounting to R4 513 277. I could therefore not confirm the existence, valuation and rights relating to VAT receivable as disclosed in note 13 to the annual financial statements. The entity's records did not permit the application of alternative audit procedures to confirm the existence, valuation, rights of VAT receivable

Provisions

36. The municipality could not provide sufficient appropriate audit evidence to support provisions for rehabilitation of landfill sites amounting to R1 503 000. The engineers' report was not signed and the municipality did not use the values stated in the report. As a result it could not be established whether the report was final and complete. I was therefore unable to verify the existence, valuation and obligations of the provision for landfill sites amounting to R1 503 000 (2010: R450 000) as reflected in the statement of financial position and note 19 of the annual financial statements. The entity's records did not permit the application of alternative audit procedures to confirm the valuation, and obligations of provisions for rehabilitation of landfill sites.
37. The municipality could not provide sufficient appropriate audit evidence to support provisions for post employment benefits amounting to R 1 803 000 disclosed in note 9 to the financial statements. The actuarial report could not be relied upon as information used could not be validated. As a result, I was unable to verify the completeness, valuation and allocation and obligations of the provisions for post employment benefits of R 1 803 000 (2010: 1 582 000).

Long-term liabilities

38. The municipality could not provide sufficient appropriate audit evidence to support year-end journal entries to the amount of R2 129 711. I was therefore unable to confirm the existence, valuation and allocation and obligations of long-term liabilities reflected as R3 067 213 (2010: R1 565 858) in the statement of financial position and note 17 to the annual financial statements. The entity's records did not permit the application of alternative audit procedures to confirm the existence, valuation, and obligations of long-term liabilities.

Inventory

39. I was unable to obtain sufficient appropriate evidence to confirm the existence, valuation and rights of inventory amounting to R6 756 720 (2010: 6 397 496) as disclosed in note 10 to the financial statements. The entity's records did not permit the application of alternative audit procedures.
40. I was unable to obtain sufficient appropriate evidence to confirm the existence, valuation, rights and completeness of vacant land and farms amounting to R5 944 065. Furthermore, these items have been disclosed in the annual financial statements as inventory instead of investment property as prescribed by SA statement of GRAP 16; investment property. The entity's records did not permit the application of alternative audit procedures.

Leases

41. Standards of Generally Recognized Accounting Practice (GRAP), GRAP 13, Leases, requires a lease to be classified as a finance lease if the lease term is for a major part of the economic life of the asset even if title is not transferred. The municipality is party to a number of lease agreements that constitute finance leases, but have been accounted for as operating leases. As the relevant information was not available; I was not able to quantify the extent by which the property, plant and equipment, long-term liabilities, the current portion of long-term liabilities and accumulated surplus were misstated if GRAP 13 had been applied correctly.

Expenditure

42. A difference of R60 640 was identified between the trial balance and the amount disclosed as expenditure in the statement of financial performance. Based on this difference, the trial balance and general ledger supporting the amount disclosed could not be relied upon and expenditure as disclosed is not considered to be fairly stated. I could not determine the effect on the other account balances or classes of transactions contained in the financial statement.
43. The municipality could not provide sufficient appropriate audit evidence to support expenditure transactions amounting to R1 866 732. As a result of this limitation, I was unable to satisfy myself concerning the accuracy, occurrence, classification, completeness and cut-off of expenditure as disclosed in the statement of financial performance. The entity's records did not permit the application of alternative audit procedures.
44. The municipality did not record expenditure amounting to R1 226 495 in the general ledger owing to the weak financial controls surrounding capturing of expenditure and recording of creditors. I was unable to satisfy myself concerning the completeness and accuracy of expenditure as disclosed in the statement of financial performance.
45. The amount disclosed as debt impairment of R11 719 645 (2010: R9 173 807) in the statement of financial performance and note 50 to the annual financial statements did not agree to the movement on the bad debt provision. The movement exceeded the disclosed amount by R121 580. Additionally, the debt impairment disclosed did not account for any bad debts written-off by council during the year. This actual write-off is estimated at R22 397 797. The debt impairment disclosed is therefore incomplete and inaccurately disclosed in the annual financial statements.
46. Withdrawals amounting to R12 427 691 as per the listing of conditional grants could not be traced to the general ledger. As a result I was unable to satisfy myself concerning the completeness and accuracy of expenditure as disclosed in the statement of financial performance. There were no alternative procedures available for me to satisfy myself concerning these amounts.
47. The finance charge as per the loan register does not agree with the total as per the general ledger. The municipality did not reconcile the difference of R317 287 between the general ledger and the underlying records.

Employee costs

48. The current year comparatives for employee costs for the year ended 30 June 2010 were not correctly recorded in the financial statements. The prior year amounts exceed the current year comparative disclosure by R1 480 706. Based on this difference, employee cost as disclosed in the current year comparatives is not considered to be accurate. I was unable to perform alternative procedures as the primary source of audit evidence could not be relied upon and as a result I could not confirm the accuracy of employee cost.

Revenue

49. The municipality could not provide sufficient appropriate audit evidence to support revenue from exchange transactions amounting to R5 783 366. I was therefore unable to verify the occurrence, accuracy, classification, completeness and cut-off of revenue from exchange transactions of R20 261 124 (2010: 17 635 424) as disclosed in note 24 to the financial

statements. The entity's records did not permit the application of alternative audit procedures to confirm the occurrence, accuracy, classification, completeness and cut-off of revenue from exchange transactions.

50. The municipality could not provide sufficient appropriate audit evidence to support revenue journal entries amounting to R12 474 208. Material entries related primarily to water revenue and I could therefore not verify the accuracy, occurrence, cut-off, classification and completeness of water revenue as disclosed in note 24 of the financial statements. The entity's records did not permit the application of alternative audit procedures to confirm these transactions processed against water revenue.
51. There was no system of control over prepaid electricity on which I could rely for the purpose of my audit, and there were no satisfactory audit procedures that I could perform to obtain reasonable assurance that prepaid electricity was accurately recorded using the tariffs approved by the National Energy Regulator of South Africa (NERSA). Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the accuracy, completeness, cut-off and classification of revenue from sale of electricity of R4 923 999 (2010: R4 743 489) disclosed in note 24 to the financial statements.
52. The municipality did not update the financial system with property values as per the valuation roll. Mater values relating to property rates were not captured onto the system and I could therefore not verify the accuracy, occurrence, cut-off and classification of revenue from property rates as disclosed in note 23 to the financial statements.
53. The municipality could not provide sufficient appropriate audit evidence to support revenue from grants totalling R71 366 284. I could not verify the accuracy and occurrence of grant revenue as disclosed in note 25 to the annual financial statements. The entity's records did not permit the application of alternative audit procedures to confirm the accuracy and occurrence of revenue from grants.
54. The municipality could not provide sufficient appropriate audit evidence for journals processed against revenue amounting to R18 404 888. The entity's records did not permit the application of alternative audit procedures regarding the accuracy, occurrence, cut-off and classification of revenue.
55. The municipality charged interest on credit balances where the entity actually owes the consumers. This is as a result of the lack of knowledge on the formulae used in the financial system to calculate interest on arrear accounts. Furthermore, the municipality was still billing customers for buckets even though bucket system is no longer in use. I was not able to quantify the extent by which revenue, receivables and accumulated surplus were misstated if the formulae on the financial system had been applied correctly.

Comparative figures

56. My report on the prior year's financial statements was a disclaimer of opinion. There were numerous balances and transactions that were qualified in the prior years that have not been corrected in the current year. As the municipality have not provided the required information or made the required changes to the opening balances in respect of these balances, I could not determine the effect on the other account balances or classes of

transactions contained in the financial statement.

Statement of cash flows

57. The Cash Flow Statement has not been prepared according to Standards of Generally Recognised Accounting Practice (GRAP), GRAP 2, *Cash flow statements*. The cash flows arising from operating activities was incorrectly reported on a net basis that is not in line with paragraph 16 of GRAP 2. The entity did not disclose the method adopted for reporting cash flows.

Financial disclosures

58. The annual financial statements are misleading as the following items affecting the disclosure notes in the financial statements were identified:

- There were no estimated useful lives given for Community Assets or Other Property, Plant and Equipment per accounting policy 2.6 for Property, Plant and Equipment.
- The last section of accounting policy 2.6 related to the valuation model and is not deemed to be appropriate.
- There was no valuation method disclosed for investment property under accounting policy number 2.7.
- There is no reference made to use of Directive 4 under the notes to the annual financial statements or the progress made to full compliance with the GRAP standards;
- Note 14 includes property rates which should be excluded as they are revenue from non-exchange transactions;
- The non-current and current liabilities as per note 17 should all be considered to be valued at amortised cost (not fair value through surplus or deficit).

Other Statutory disclosures

59. Particulars of non-compliance with the MFMA were not disclosed in the notes to the annual financial statements, as required by section 125 (2) (e) of the MFMA. As included in the compliance with laws and regulations section of this report, several material deviations from the MFMA were identified during the audit; however, no particulars of any of these matters were disclosed in the notes to the annual financial statements.

Unauthorised expenditure

60. The municipality incurred unauthorised expenditure amounting to R19 945 202 mainly as a result of overspending of certain votes that was not appropriated in an adjustment budget. This unauthorised expenditure was not disclosed in the notes to the financial statements as required by section 125(2)(d)(ii) of the MFMA. Unauthorised expenditure is thus understated by a similar amount.

61. The listing detailing all unauthorised expenditure condoned during the year did not correspond with the amount disclosed in note 45 of the financial statements as R33 863 487 (2010: Nil). The listing exceeded the financial statement disclosure by R9 459 130. I was therefore unable to satisfy myself regarding the completeness and valuation of all condoned unauthorised expenditure disclosures.

Fruitless and wasteful expenditure

62. The listing detailing all fruitless and wasteful expenditure condoned during the year did not correspond with the amount disclosed in note 46 of the financial statements amounting to R1 954 187 (2010: Nil). The financial statement disclosure exceeded the listing by R954 260. I was therefore unable to satisfy myself regarding the completeness and valuation of all condoned fruitless and wasteful expenditure disclosures.

Contingent liabilities

63. The confirmation received from the municipality's legal representatives indicates that, there is a remote possibility that certain cases against the municipality will be successful. This therefore does not meet the recognition criteria for contingent liabilities in terms of the Standards of GRAP 19: *Provisions, Contingent Liabilities and Contingent Assets* as the standard indicates that a contingency should not be recognised where the possibility of an outflow of resources embodying economic benefits or service potential is remote. The contingent liabilities as disclosed in note 40 to the financial statements amounting to R 6 002 800 (2010: R Nil) are therefore overstated by R4 718 500.
64. I was unable to confirm the completeness and valuation of contingent liabilities disclosed at R6 002 800 (2010: R Nil) in note 40 to the financial statements, due to limitations placed on the scope of my work by the entity. The municipality did not disclose the possible obligation to repair assets and infrastructure affected by the heavy rainfall within the municipality's region owing to the weak financial controls surrounding the recognition of contingent liabilities.

Commitments

65. The municipality did not maintain a contract management system for the identification and recognition of contracts and there were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that all commitments were properly recorded. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness of commitments of R61 492 075 (2010: R25 140 634), as stated in note 39 to the financial statements.
66. The municipality could not provide sufficient appropriate audit evidence to support new commitments of R35 952 570 due to council approval which was not submitted to validate the amounts. In the absence of council approval, I could not verify by alternative means the completeness and valuation of the amount disclosed.

Related parties

67. The municipality did not have policies and procedures in place during the year under review with which to detect and monitor any related party relationships. As a result of the above, I was unable to verify the completeness of related parties and related party transactions as no such relationships were disclosed in the financial statements.
68. The municipality incurred expenditure during the current year amounting to R255 529 where procurement was made from a company in which the director is a related party to a key employee of the municipality and the necessary disclosure was not made in the financial statements. As a result of the above, I was unable to verify the completeness and

valuation of related party transactions which took place during financial year.

Financial instruments

69. The municipality did not discount its revenue or expenditure as required by IAS 39: *Financial instruments* or account for the time value at year-end for trade receivables and trade payables. The municipality is required to recognise the interest portion as and when the transactions occur. Revenue, expenditure, trade receivables and trade payables are therefore overstated and interest in the statement of financial performance is therefore understated. I was unable to perform alternative procedures to quantify the amount of these misstatements.

Adverse opinion

70. In my opinion, because of the significance of the matters described in the Basis for adverse opinion paragraphs, these financial statements do not present fairly the financial position of the Phumelela Local Municipality as at 30 June 2011 and its financial performance and cash flows for the year then ended, in accordance with GRAP and the requirements of the MFMA.

Emphasis of matter

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

Restatement of corresponding figures

72. As disclosed in note 41 to the financial statements, the corresponding figures for 2010 have been restated as a result of an error discovered during 2011 in the financial statements of the Phumelela Local Municipality at, and for the year ended, 30 June 2010.

Material Impairments

73. As reported in note 50 to the financial statements receivables amounting to R11 719 645 were impaired during the year.

Irregular expenditure

74. As disclosed in note 46 to the financial statements, the municipality incurred irregular expenditure amounting to R39 315 083

Additional matters

Unaudited supplementary information

75. 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

76. In accordance with the PAA and in terms of *General notice 1111 of 2010*, issued in *Government Gazette 33872 of 15 December 2010*, I include below my findings on the annual performance report as set out on pages [xx] to [xx] and material non-compliance

with laws and regulations applicable to the municipality.

Predetermined objectives

Presentation of information

77. The reported performance against predetermined objectives was deficient in respect of the following criteria.

- The performance against predetermined objectives was not reported using the National Treasury guidelines.

78. The following audit findings relate to the above criteria:

Reported targets are not consistent when compared with the planned targets

- Targets as per annual performance report differed from the IDP as certain objectives were not reported on.

Reasons for major variances between planned and actual reported targets were not supported by sufficient appropriate evidence

- Measures taken to improve performance were not explained in the report on predetermined objective.

Usefulness of information

79. The following criteria were used to assess the usefulness of the planned and reported performance:

- Consistency: The reported objectives, indicators and targets are not consistent with the approved integrated development plan.
- Relevance: Is there a clear and logical link between the objectives, outcomes, outputs, indicators and performance targets?
- Measurability: The indicators are not well defined and verifiable, and targets are not specific, measurable and time bound.

The following audit findings relate to the above criteria:

Planned and reported targets are not specific, measurable and time bound

- For the selected programmes, 84% of the planned and reported targets were not:
 - specific in clearly identifying the nature and the required level of performance;
 - measurable in identifying the required performance;
 - time-bound in specifying the time period or deadline for delivery.

Planned and reported indicators are not well defined

- 82% of selected programmes; valid performance management processes and systems that produce actual performance against the planned indicators do not exist for certain of these measures.

Reported performance against indicators is not complete when compared to source information

- The municipality did not report on planned measures to improve on reported information where targets were not achieved.

Reported objectives are not consistent and complete when compared with the planned objectives

- Reported development priorities/objectives were not consistent or not complete when compared with planned development priorities/objectives.
- Reported indicators were not consistent or not complete when compared with planned indicators.
- Reported targets were not consistent or not complete when compared with planned targets.

Reliability of information

80. The reported performance information was deficient in respect of the following criteria:

- **Validity:** The reported performance did not occur and does not pertain to the entity.
- **Accuracy:** Amounts, numbers and other data relating to reported actual performance has been recorded and reported appropriately.
- **Completeness:** All actual results and events that should have been recorded have not been included in the reported performance information.

The following audit findings relate to the above criteria:

The validity, accuracy and completeness of reported performance against indicators could not be confirmed as inadequate supporting source information was provided.

- For selected objectives the validity, accuracy and completeness of 82% of the reported indicators could not be established as sufficient appropriate audit evidence and relevant source documents could not be provided.

Compliance with laws and regulations

Strategic planning and performance management

81. The municipality did not implement a framework that describes and represents how the municipality's cycles and processes of performance planning, monitoring, measurement, review, reporting and improvement will be conducted, organised and managed, as required by sections 38, 39, 40 and 41 of the MSA and Municipal Planning and Performance

Management Regulations 7 and 8.

82. The accounting officer did not assess the municipality's actual service delivery performance for the first half of the financial year against the service delivery targets and performance indicators set in the service delivery and budget implementation plan, by 25 January 2011 as required by section 72(1)(a)(ii) of the MFMA
83. The accounting officer did not submit the results of the assessment on the performance of the municipality during the first half of the financial year to the mayor of the municipality, the National Treasury, and the provincial treasury, as required by section 72(1)(b) of the MFMA.
84. The accounting officer did not submit a service delivery and budget implementation plan as defined in section 1 of the MFMA for the year to the mayor as required by section 69(3) of the MFMA.

Budgets

85. The municipality incurred expenditure that was not budgeted for and/or incurred expenditure in excess of the limits of the amounts provided for in the votes in the approved budget, in contravention of section 15 of the MFMA.
86. The accounting officer did not always submit the monthly budget statements to the mayor and/or the relevant provincial treasury, as required by section 71(1) of the MFMA.
87. The accounting officer did not perform a mid-year budget and performance assessment as required by section 72 of the MFMA.

Annual financial statements, performance and annual report

88. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the Municipal Finance Management Act. Material misstatements identified by the auditors were not adequately corrected, which resulted in the financial statements receiving an adverse audit opinion.
89. Contrary to the requirements of section 126 of the Municipal Finance Management Act, the annual financial statements were not submitted to the Auditor General of South Africa for auditing within two months after the end of the financial year.
90. We could not obtain evidence that the accounting officer has submitted the annual report to the National and Provincial Treasury as required by section 72 of the Municipal Finance Management Act.
91. Contrary to the requirements of section 126 of the Municipal Finance Management Act, the municipality did not submit consolidated annual financial statements to the Auditor General of South Africa.

Audit committees

92. The municipality did not have a functioning audit committee in place, as required by section 166 of the MFMA.
93. The municipality did not appoint and budget for a performance audit committee, nor was another audit committee utilised as the performance audit committee as required by Municipal Planning and Performance Management Regulation 14.

Internal audit

94. The internal audit unit did not function as required by section 165(2) of the MFMA, in that it did not prepare a risk-based audit plan and an internal audit programme for the financial year under review;
95. The internal audit processes and procedures did not include assessments of the functionality of the municipality's performance management system and whether the system complied with the requirements of the MSA as required by Municipal Planning and Performance Management Regulation 14.
96. The internal audit processes and procedures did not include assessments of the extent to which the municipality's performance measurements were reliable in measuring the performance of the municipality on key as well as general performance indicators as required by Municipal Planning and Performance Management Regulation 14.
97. The internal auditors of the municipality did not audit the performance measurements on a continuous basis and/or did not submit quarterly reports on their audits to the municipal manager and the performance audit committee as required by Municipal Planning and Performance Management Regulation 14.
98. Internal audit did not report to the audit committee on the implementation of the internal audit plan;
99. Internal audit did not advise the accounting officer and report to the audit committee on matters relating to internal audit, internal controls, accounting procedures and risk and risk management.

Procurement and contract management

100. Goods and services with a transaction value of between R10 000 and R200 000 were procured without obtaining written price quotations from at least three different prospective providers as per the requirements of SCM regulation 17(a) and (c).
101. Final awards and/or recommendation of awards to the accounting officer were not always made by an adjudication committee which was appropriately constituted as per the requirements SCM regulation 29(2).
102. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids as per the requirements of SCM regulation 19(a) and 36(1).
103. The preference point system was not applied in all procurement of goods and services above R30 000 as required by section 2(a) of the Preferential Procurement Policy Framework Act and SCM regulation 28(1)(a).
104. Contrary to the requirements of section 41(2) of the Municipal Supply Chain Regulations I could not obtain a risk register or other documentary proof that risk assessment relating to

the SCM system were performed.

105. Contrary to the requirements of regulation 14 of the Municipal Supply Chain Regulations the accounting officer did not keep a list of accredited prospective providers of goods and services.
106. Evidence could not be obtained that the required supply chain management reports had been compiled and reviewed by management to ensure compliance with regulation 6(1),(3) and (4) of the Municipal Supply Chain Management Regulations.

Human resources management and compensation

107. The municipal manager did not ensure that the municipality has adequate human resource capacity that enables it to perform its functions and exercise its powers in an economical, efficient, effective and accountable manner in compliance with section 68 (1) of MSA.

Expenditure management

108. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained an effective system of expenditure control, including procedures for the approval, authorisation, withdrawal and payment of funds as required by section 65(2) of the MFMA.
109. The accounting officer did not take all reasonable steps to ensure that all money owing by the municipality is paid within 30 days of receiving the relevant invoice as required by section 65(2)(e) of the MFMA.
110. The accounting officer did not take all reasonable steps to prevent, identify and report unauthorised, irregular, fruitless and wasteful expenditure and other losses, as required by section 62(1)(d) and 32 of the MFMA.
111. The municipality did not recover unauthorised, irregular or fruitless and wasteful expenditure from the liable persons, as required by section 32(2) of the MFMA.

Revenue management

112. Revenue received by the municipality was not always reconciled at least on a weekly basis, as required by section 64(2) (h) of the Municipal Finance Management Act.
113. The rates property register is not compiled in the format required by the Property Rates Act number 6 of 2004.
114. The municipality's credit and debt collections policy did not provide realistic targets consistent with collection ratios as required by section 97(1)(d) of the MSA.

Asset management

115. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained a management, accounting and information system and internal controls which account for the assets of the municipality as required by section 63(2)(a) and (c) of the MFMA.
116. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained an effective system of internal control for assets (including a proper asset register) as required by section 63(2)(c) of the MFMA.

Financial misconduct

117. The municipality did not investigate all identified possible, unauthorised, irregular, fruitless and wasteful expenditure and take disciplinary action against the relevant staff members as required by section 171(4)(b) of the MFMA.

INTERNAL CONTROL

118. In accordance with the PAA and in terms of General notice 1111 of 2010, issued in *Government Gazette 33872 of 15 December 2010*, I considered internal control relevant to my audit, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters reported below are limited to the significant deficiencies that resulted in the basis for adverse opinion, the findings arising from the audit of the annual performance report and the findings arising from the audit of compliance with laws and regulations included in this report.

Leadership

119. Oversight responsibility over the preparation of financial statements, report on predetermined objectives, compliance with the laws and regulations and internal control was not exercised by the accounting officer. Leadership has not ensured that there is a process in place to ensure that reviews take place before submission. This was also evidenced by the numerous instances of non-compliance with laws and regulations, the internal control deficiencies and material misstatements in the financial statements that were noted throughout the audit process.
120. Instances have been identified where there is a lack of decisive action to mitigate emerging risks, implement timely corrective measures and address non-performance.

Financial and performance management

121. Instances have been identified where quality, reliable monthly financial statements and management information is not prepared by the municipality. Pertinent information is not identified and captured in a form and time frame to support financial and performance reporting. Numerous errors have been noted on the annual financial statements submitted which is an indication that the financial statements were not adequately reviewed by management before submitting the final version for audit.
122. The municipality does not have proper record keeping and record management processes in place to ensure that the documentation supporting the amounts and disclosures in the financial statements are properly filed and easily retrievable. Information requested for audit purposes was not readily available and significant delays were experienced throughout the audit process. In some cases, the documentation was not received at all which resulted in a limitation of scope being placed on the audit.
123. The municipality has a financial management system in place. Numerous instances have been identified where the municipality did not have manual or automated controls designed to ensure that the transactions have occurred, are authorised, and are completely and accurately processed.

Governance

124. Risk identification and management processes are not designed to identify changes in processes or risks and verify that the design of underlying controls remain effective. The municipality has not selected and developed internal controls to prevent, detect and correct material misstatements in financial reporting and reporting on predetermined objectives.
125. There is no evidence that management has taken action during the period being reviewed to address fraud risk.
126. Although an audit committee has since been established, and an internal audit department exists, these did not function adequately during the year, preventing it from discharging its duties adequately.

Auditor-General

Bloemfontein

27 January 2012



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence