

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

## **REPORT ON THE FINANCIAL STATEMENTS**

### **Introduction**

1. I have audited the financial statements of the Tswelopele Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2014, the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget information with actual information for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

### **The 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 the 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 my audit. I conducted my 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. 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.
4. 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.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

### **Opinion**

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Tswelopele Local Municipality as at 30 June 2014 and its financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of the MFMA and DoRA.

### **Emphasis of matters**

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

### **Restatement of corresponding figures**

8. As disclosed in note 46 to the financial statements, the corresponding figures for 30 June 2013 have been restated as a result of an error discovered during 2014 in the financial statements of the Tswelopele Local Municipality at, and for the year ended, 30 June 2013.

### **Material losses and impairments**

9. As disclosed in note 4 to the financial statements, a provision for impairment of debtors amounting to R41 275 500 (2013: R24 887 512) has been made with regard to consumer debts amounting to R43 021 424 (2013: R32 502 177).
10. As disclosed in note 4 to the financial statements, material losses to the amount of R13 528 (2013: R4 503 471) were incurred as a result of bad debts written off.

### **Irregular expenditure**

11. As disclosed in note 42 to the financial statements, the municipality incurred irregular expenditure of R1 520 952 (2013: R1 743 720) during the year under review due to non-compliance with supply chain management (SCM) processes.

### **Additional matters**

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

### **Unaudited disclosure notes**

13. 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.

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

14. 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 objectives 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 an opinion or conclusion on these matters.

### **Predetermined objectives**

15. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development objectives presented in the annual performance report of the municipality for the year ended 30 June 2014:
  - Development objective 1: Water provision on pages x to x
  - Development objective 2: Sanitation provision on pages x to x
  - Development objective 3: Electricity provision on pages x to x
  - Development objective 4: Roads and storm water provision on pages x to x
  - Development objective 5: Waste management on pages x to x
  - Development objective 6: Housing on pages x to x
16. I evaluated the reported performance information against the overall criteria of usefulness and reliability.

17. 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 objectives. 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).
18. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
19. The material findings in respect of the selected development objectives are as follows:

#### **Development objective 2: Sanitation provision**

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

20. The FMPPI requires the following:

- 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 50% 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 50% of the indicators were not verifiable.

This was because management did not adhere to the requirements of the FMPPI during the formulation of key performance indicators.

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

21. The FMPPI requires municipalities 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. Adequate and reliable corroborating evidence could not be provided for 50% of the targets to assess the reliability of the reported performance information. This was due to limitations placed on the scope of my work by the municipality as key performance indicators were not well defined and consequently not measurable. The auditee's records did not permit the application of alternative audit procedures.

#### **Development objective 5: Waste Management**

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

22. The FMPPI requires the following:

- 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 20% 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 20% of the indicators were not verifiable.

This was because management did not adhere to the requirements of the FMPPI during the formulation of key performance indicators.

## **Reliability of reported performance information**

23. The FMPPPI requires municipalities 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. Adequate and reliable corroborating evidence could not be provided for 20% of the targets to assess the reliability of the reported performance information. This was due to limitations placed on the scope of my work by the auditee as key performance indicators were not well defined and consequently not measurable. The auditee's records did not permit the application of alternative audit procedures.

## **Additional matters**

24. I draw attention to the following matters:

### **Achievement of planned targets**

25. Refer to the annual performance report on pages 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 objectives reported in paragraphs 20 to 23 of this report.

### **Adjustment of material misstatements**

26. I identified material misstatements in the annual performance report submitted for auditing on the reported performance information for development objectives for Water provision, Sanitation provision, Electricity provision, Road and Storm water provision, Waste management and Housing. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information.

### **Compliance with legislation**

27. 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:

### **Strategic planning and performance management**

28. The municipality did not establish a performance management system, as required by section 38(a) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA).
29. The municipality did not provide for steps for improvement where performance targets were not met, as required by section 41(1)(d) of the MSA due lack of a performance management system.

### **Budget**

30. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA.

### **Annual financial statements**

31. 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 of non-current assets, current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided, resulting in the financial statements receiving an unqualified opinion.

### **Audit committee**

32. The audit committee which also performs the duties of performance audit committee did not advise the accounting officer on matters relating to risk management, performance management and performance evaluation as required by section 166(2)(a) of the MFMA.
33. The audit committee did not advise the accounting officer on matters relating to compliance with legislation, as required by section 166(2)(a)(vii) of the MFMA.
34. The audit committee did not respond to the council on the issues raised in the audit reports of the Auditor-General, as required by section 166(2)(c) of the MFMA.
35. The audit committee which also performs the responsibilities of performance audit committee did not review the municipality's performance management system and or make recommendations to the council, as required by Municipal planning and performance management (MPPM) regulation 14(4)(a)(ii).
36. The audit committee which also performs the responsibilities of the performance audit committee did not submit, at least twice during the financial year, an audit report on the review of the performance management system to the council, as required by MPPM regulation 14(4)(a)(iii).
37. The audit committee which also performs the responsibilities of the performance audit committee did not review all the quarterly internal audit reports on performance measurement, as required by MPPM regulation 14(4)(a)(i).

### **Internal audit**

38. 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 report to the audit committee on matters relating to internal controls and risk management.
39. The internal audit unit did not advise the accounting officer or report to the audit committee on matters relating to compliance with the MFMA, the DoRA and other applicable legislation, as required by section 165(2)(b)(vii) of the MFMA.

### **Procurement and contract management**

40. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulation 17(a) & (c).
41. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).
42. Construction projects were not always registered with the Construction Industry Development Board (CIDB), as required by section 22 of the Construction Industry Development Board Act of South Africa, 2000 (Act No. 38 of 2000) and CIDB regulation 18

### **Human resource management**

43. 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 the Municipal Regulations on Minimum Competency Levels regulation 13.
44. 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 Regulations on Minimum Competency Levels.

### **Expenditure management**

45. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
46. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred and accounted for creditors, as required by section 65(2)(b) of the MFMA.
47. 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**

48. A credit control and debt collection policy was not maintained, as required by section 96(b) of the MSA and section 62(1)(f)(iii) of MFMA.
49. An adequate management, accounting and information system which accounts for revenue and debtors was not in place, as required by section 64(2)(e) of the MFMA.
50. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.
51. Revenue due to the municipality was not calculated on a monthly basis, as required by section 64(2)(b) of the MFMA.
52. Interest was not charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.

### **Asset management**

53. 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.
54. 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.

### **Liability management**

55. An adequate management, accounting and information system which accounts for liabilities was not in place, as required by section 63(2)(a) of the MFMA.
56. An effective system of internal control for liabilities (including a liability register) was not in place, as required by section 63(2)(c) of the MFMA.

## **Consequence management**

57. Unauthorised, irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.
58. Unauthorised, irregular and fruitless and wasteful expenditure was not always recovered from the liable person, as required by section 32(2) of the MFMA.

## **Environmental management**

59. The municipality operated one 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**

60. I considered internal control relevant to my audit of the financial statements, the performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on the performance report and the findings on non-compliance with legislation included in this report.

## **Leadership**

61. The municipal council and senior management did not ensure that the municipality has an approved performance management system that monitors performance and holds officials to account for poor performance and transgressions. This was mainly due to slow response by political leadership in approving a performance management system.
62. The accounting officer did not take adequate steps to ensure that the municipality produces accurate and complete performance reports and complies with legislation which resulted in repeat material findings on predetermined objectives and non-compliance with legislation. This was due to lack of consequences for poor performance and transgression as the municipality has not implemented a performance management system.
63. The accounting officer did not prioritise oversight over information technology (IT) governance as processes to address IT related findings reported on in the previous years were only initiated in the later part of the year under review. Repeat findings were therefore reported in the current year. This was mainly due to slow response by management as an IT officer was neither appointed in time nor allocated adequate budgetary resources.

## **Financial and performance management**

64. Ongoing monitoring and supervisory reviews over financial, performance and compliance reporting were not adequate. Internal controls weaknesses were thus not identified and corrected in time to ensure accurate and complete reporting. This was due to lack of consequences for poor performance and transgression as the municipality has not implemented a performance management system.

## **Governance**

65. Work performed by the internal audit function was not based on a risk assessment and thus had limited impact on addressing key weakness in financial reporting, performance management and compliance with legislation. This was due to slow response by management as risk assessment was not prioritised and implemented.

Bloemfontein

30 November 2014



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*