



#### 4.4 REPORT OF AUDITOR GENERAL

##### Report of the Auditor-General to the Tswelopele Municipality

for the year ended 30 June 2006

#### REPORT OF THE AUDITOR-GENERAL TO COUNCIL ON THE FINANCIAL STATEMENTS OF TSWELOPELE MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2006

##### 1. AUDIT ASSIGNMENT

The financial statements as set out on pages 60 to 90, for the year ended 30 June 2006, have been audited in terms of Section 188 of the Constitution of the Republic of South Africa, 1996, read with Sections 4 and 20 of the Public Audit Act, 2004 (Act No. 25 of 2004) and Section 126 of the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA). These financial statements are the responsibility of the accounting officer. My responsibility is to express an opinion on these financial statements, based on the audit.

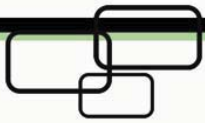
##### 2. SCOPE

The audit was conducted in accordance with the International Standards on Auditing read with *General Notice 1512 of 2006*, issued in *Government Gazette* no. 29326 of 27 October 2006. Those standards require that I plan and perform the audit to obtain reasonable assurance that the financial statements are free from material misstatement.

An audit include:

- examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements
- assessing the accounting principles used and significant estimates made by management
- evaluating the overall financial statement presentation.

I believe that the audit provides a reasonable basis for my opinion.



### 3. BASIS OF ACCOUNTING

The municipality's policy is to prepare the financial statements on the entity specific basis of accounting as described in accounting policy no. 1 in the financial statements.

### 4. QUALIFICATION

#### Accumulated surplus

As policies and procedures were not adhered to, the accumulated surplus is overstated with R383 622. The understatement relates to the following:

- Inadequate provision was made for water fees that were not paid during the 2005/06 financial year, resulting in an overstatement of R188 497.
- No provision was made for bonuses amounting to R344 486, resulting in an overstatement.
- Various shortcomings identified in the calculation of the leave provision, resulting in an understatement of R149 361.

This resulted in an understatement of creditors, provisions and debtors with R213 923, R195 125 and R25 426 respectively at 30 June 2006.

### 5. QUALIFIED AUDIT OPINION

In my opinion, except for the effect on the financial statements of the matters referred to in the preceding paragraph, the financial statements present fairly, in all material respects, the financial position of the entity at 30 June 2006 and the results of its operations and cash flows for the year then ended, in accordance with the basis of accounting determined by the National Treasury of South Africa, as described in accounting policy no. 1 to the financial statements, and in the manner required by the MFMA.



## 6. EMPHASIS OF MATTER

Without further qualifying the audit opinion, attention is drawn to the following matters:

### 6.1 Financial Management and Weaknesses in Internal Control

#### Assets

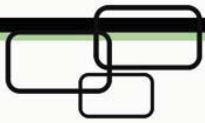
Section 63(1) of MFMA determines that an accounting officer of a municipality is responsible for the management of the assets of the municipality, including the safeguarding and the maintenance thereof. Contrary to this section:

- Proof could not be obtained that a physical asset count was performed at year-end. Subsequently surpluses and deficiencies in this regard could not be verified
- Room inventory lists were not updated for the financial year under review
- Information required for the physical identification of fixed assets for Hoopstad and Bultfontein were not included on the asset register
- Council approval for assets written off during the financial year under review amounting to R116 693 could not be submitted for audit purposes.

This is an indication that, where good financial management discipline, such as conducting regular asset counts, is not in place, management run a risk of not being able to properly account for important assets in its business.

#### Fraud Prevention and Risk Management

To enable good financial management, management of the municipality is required to properly analyse financial risk at account balance level and implement appropriate controls to minimise these risks. The municipality did not conduct a formal risk assessment during the year under review and subsequently a fraud prevention plan was not



implemented in order to combat, detect and prevent fraud, corruption, favouritism, unfair and irregular practices within the municipality.

### Supply Chain Management (SCM)

- In terms of paragraph 16 of the municipal SCM regulations, as published in the Government Gazette no. 27636 dated 30 May 2005, and paragraph 12 of the municipality's SCM policy, at least three written or verbal quotations should be obtained for purchases of R1 000 and more. Contrary to this, expenditure amounting to R548 501 was incurred where less than the required number of quotations was obtained.
- Contrary to paragraph 13 of the municipal SCM regulations evidence could not be submitted for payments amounting to R797 890 that:
  - authorisations were obtained for tax clearance certificates by the municipality and
  - natural persons, stakeholders, shareholders or managers of the suppliers are not employees of the state or have not been employees of the state in the past twelve months.
- A tender/contract register or record containing the details of the tender processes followed could not be obtained, it was thus not possible to:
  - evaluate the tender processes followed
  - verify the completeness of tender processes followed and
  - evaluate the progress of contracts awarded.
- A retention register for projects undertaken by the municipality could not be submitted for audit purposes and it was thus not possible to establish the total amount of retention money recorded in the municipality's financial records.

The above shortcomings all relate to management's inability to timeously create the right environment for good internal control and financial management.



### Computer Information Systems

Adequate general controls surrounding the information systems of the municipality to ensure the effective and continuous operation of the data-processing function were not in place. This, amongst others, includes inadequate job descriptions and duty sheets, the lack of a functioning IT steering committee, inadequate segregation of duties, antivirus definitions not being updated on a regular basis and no formal procedure regarding the installation of software on computers.

### Possible Conflict of Interest

Without negatively reflecting on the professionalism of the firm involved, a possible lack of independence and segregation of duties was noted in respect of the functions performed in respect of financial management at the municipality. A contracted audit firm was responsible for the following functions relating to the 2005/06 financial year:

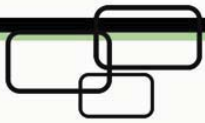
- Performance of MST work
- Preparation of the financial statements
- Internal audit function and
- A partner from the same audit firm was appointed as Chairperson of the Audit Committee of the municipality.

## 6.2 Matters in Public Interest

### Distribution Losses

- The distribution losses for water at Hoopstad and electricity at Bultfontein are considered to be exceptionally high at 10,45% and 11,8% respectively. Based on the statistical information provided in Appendix F to the financial statements, the cost of distribution losses for water at Hoopstad and electricity at Bultfontein amounted to R20 116 and R301 914 respectively.
- A difference of 619 643 kl water consumed was identified between the invoices obtained from the Department of Water Affairs and Forestry (1 461 600 kl) and the physical meter readings recorded in





the municipality's pump register (842 157 kl). This difference could not be explained by the municipality and is currently under investigation. Should the units consumed according to the Department of Water Affairs and Forestry be used, the calculated percentage loss in distribution as disclosed in Appendix F to the financial statements would increase from 9% to 47,21%.

- Accounts were not received from the Department of Water Affairs and Forestry with regard to Hoopstad's water consumption for the financial year under review. Units consumed were estimated by the municipality as 962 724 kl for the period 1 July 2005 to 30 June 2006. Consequently the correctness of calculations and the margin (mark-up) in percentage terms between bulk purchases and gross revenue could not be verified as actual units purchased were not available.

This shortcoming is directly attributable to management's inability to implement and maintain a basic control system that affects a major portion of the municipality's service delivery system.

#### **Irregular, Fruitless and Wasteful Expenditure**

The following possible irregular, fruitless and wasteful expenditure is disclosed in Note 26 to the financial statements:

- Supporting documentation to indicate compliance with tender regulations for expenditure amounting to R782 236 that was not submitted for audit purposes.
- A payment of R20 000 was made to a legal firm for the settlement of a labour dispute.

This irregular expenditure resulted from policies and procedures that were not followed.



### 6.3 Non-compliance with Laws and Regulations

The matters listed below, result from a lack of appropriately documented and approved policy and procedure frameworks to ensure compliance with all relevant laws and regulations.

#### MFMA

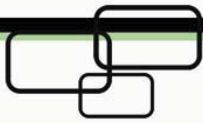
The annual report for 2004/05 financial year was not tabled timeously in council as required in terms of Section 127(2) of the MFMA. The oversight report containing Council's comments on the Annual Report as required in terms of Section 129 of the MFMA is thus not yet available.

#### Municipal Systems

- Contrary to Section 57(1) of the Local Government Municipal Systems Act, 2000 (Act No. 32 of 2000) evidence that performance agreements for both the Municipal Manager and the senior managers directly reporting to him were in place for the 2005-06 financial year, could not be submitted.
- Contrary to Section 74 of the Municipal Systems Act, (Act No. 32 of 2000) the municipality did not adopt and implement a tariff policy on the levying of fees for municipal services provided by the municipality itself or by way of service delivery agreements which complies with the provisions of this Act, the MFMA and any other applicable legislation.

#### Unemployment Insurance Contributions Act

Contrary to Section 4(1)(a) of the Unemployment Insurance Contributions Act, 2002 (Act No. 4 of 2002), UIF was not contributed for various employees working more than 24 hours a month.



### **Environmental Conservation Act**

Evidence that a permit was issued to operate the land fill site in Bultfontein as required in terms of Section 20(1) of the Environmental Conservation Act, 1989 (Act No. 73 of 1989) could not be submitted.

### **Basis Conditions of Services**

The municipality's current human resource policy stipulates that stand-by allowances should be calculated as an hour's wage for every week day and Saturday that is not a public holiday during which the employees were available on stand-by duty. This is contrary to Government Gazette dated 1 July 1994 and regulations set by the Industrial Council, which requires that stand-by allowances for stand-by duty performed on a week day and Saturday that is not a public holiday to be calculated at an hour and a half's rate.

### **Value Added Tax Act (VAT)**

Contrary to Sections 20(4) and 21(3) of the Value Added Tax Act, 1991 all VAT invoices for R3 000 and higher should indicate both the VAT numbers of the supplier and the receiver of goods and services. Although the municipality claimed input VAT, the VAT number of the municipality did not appear on the supplier invoices amounting to R391 190.





## 7. LATE FINALISATION OF THE AUDIT REPORT

In terms of Section 126(3)(b) of the MFMA, I am required to submit my report to the accounting officer within three months of the receipt of the financial statements. In the interest of improving accountability and due to the process implemented by me to ensure consistency in the manner in which material audit findings are reported, I have delayed the finalisation of my reports to no later than 22 December 2006 where the financial statements in question were received by 31 August 2006.

## 8. APPRECIATION

The assistance rendered by the staff of municipality during the audit is sincerely appreciated.

Signed by N.G. McCarthy  
for: Auditor-General

Bloemfontein  
11 December 2006



**A U D I T O R - G E N E R A L**