

**REPORT OF THE AUDITOR-GENERAL TO THE MEMBERS OF THE  
COUNCIL ON THE FINANCIAL STATEMENTS OF BUSHBUCKRIDGE  
MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2006**

**1. AUDIT ASSIGNMENT**

The financial statements as set out on pages 4 to 30, 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). These financial statements are the responsibility of the municipal manager. 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 of material misstatement.

An audit includes:

- 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 is required to prepare financial statements in accordance with the standards determined by the Institute of Municipal Treasurers and Accountants in its Code of Accounting Practise (1997) and Report on Published Annual Financial Statements (second edition – January 1996), which constitute an entity specific basis of accounting.

**4. QUALIFICATION**

- 4.1 On 18 October 2006 I issued a report in which I stated that the financial statements of the municipality for the 2005 financial year did not fairly represent the financial position of the municipality as at 30 June 2005 and

the results of its operations and cash flow information for the year then ended. In the circumstances I was unable to satisfy myself regarding the extent to which the results for the year ended 30 June 2006 had been affected by misstatements of closing balances at 30 June 2005.

4.2. The validity, accuracy and completeness of expenses to the value of R156 886 519 could not be verified due to the following reasons:

- Supporting documentation could not be obtained for selected expenses amounting to R680 613.
- Operating lease payments amounting to R1 490 877 could not be verified against signed operating lease agreements. The validity, accuracy and completeness of these payments could not be verified.
- The completeness, accuracy and validity of salary and wage expenses totalling R47 225 422 could not be verified due to the following reasons:
  - Salary expenses as per the payroll system were not reconciled to the general ledger. Differences between the payroll and the general ledger amounted to R5 108 238 for the year under review. These differences could not be substantiated.
  - The actual salary expense for the year exceeded the budgeted amount by R5 545 961. I was unable to obtain any proof that this excess expenditure was approved by the council. Management was unable to provide me with an explanation as to why the approved budget was exceeded.
  - The monthly salary of a deceased employee was paid into the deceased's bank account for four months after the employee had passed away. The salary payments for the four months amounted to R14 276. This amount was not recovered from the deceased's estate. These payments are regarded as fruitless expenditure.
  - The employee files of six employees selected for testing could not be obtained. This placed a limitation on the scope of the audit.
  - The appointment letters or employment contracts of four employees selected for testing could not be obtained. This placed a limitation on the scope of the audit.

- I was unable to obtain the municipality's IRP 501 annual tax reconciliation for the year under review. A summary of IRP 5's issued was not compiled.

No comparison could therefore be made between IRP 5's issued and employees' tax deducted as per the payroll system. No evidence could be obtained that the IRP 5 reconciliation was submitted to the Receiver of Revenue.

- Councillors made use of municipal cellphones during the year under review. No evidence could be obtained that amounts exceeding the approved limits were deducted from councillors' salaries. Excess expenditure of R7 698 was identified in the audit sample selected for testing. The excess expenditure was not included in the councillors' taxable income and no PAYE was deducted on these amounts.
- Salary deductions amounting to R68 751 could not be traced to payment documentation. I was therefore unable to determine whether any liabilities in respect of payroll deductions existed at year-end.

4.3 The completeness, accuracy and validity of income to the value of R175 982 920 could not be verified due to the following reasons:

- The completeness and accuracy of grants received to the value of R141 614 091 could not be verified as the equitable share recorded for the year under review was R1 959 956 less than the amount published in the relevant Government Gazette in terms of the Division of Revenue Act, 2005 (Act No. 1 of 2005). This difference could not be substantiated.
- Grants amounting to R12 146 258 could not be verified against grant letters. I was unable to determine whether these grants were subject to certain conditions and therefore I could not determine whether the grants received should be disclosed as trust funds or conditional grants.
- District Council grants amounting to R19 206 434 could not be verified against supporting documents.
- The completeness, accuracy and validity of assessment rates amounting to R15 085 203 could not be verified due to the following reasons:

- The municipality did not reconcile the valuation roll with the assessment rates charged to consumers. I was therefore unable to verify the completeness and accuracy of assessment rates charged during the year.
  - I was unable to obtain proof that the valuer who compiled the valuation roll was a registered professional valuer or professional associated valuer as required by the Property Valuer's Profession Act, 2000 (Act No. 47 of 2000).
  - Revenue from assessment rates was adjusted by R47 386 850 during the year under review. This adjustment was due to excessive assessment rates levied on properties. I was unable to determine whether the valuation roll contained any other inaccurate valuations. The impact of possible incorrect valuations could therefore not be determined.
  - Assessment rates charged from July 2005 to February 2006 were processed as a single entry of R57 993 500 in the general ledger. I was unable to verify this amount against billing reports.
  - I was unable to obtain proof that the council approved the assessment rates that were levied during the year under review. Assessment rates were levied at a rate of 5 cents per rand and residential properties received a rebate of 3 cents per rand.
  - Five of the valuation rolls selected for testing were not signed by the valuer. The validity of these valuation rolls could not be verified.
  - Property values of a sample of properties were incorrectly captured on the billing system. The value of these properties on the billing system was R202 000 less than the valuations reflected on the valuation roll.
  - Properties valued at R382 500 were not captured on the billing system.
- The completeness and accuracy of revenue from the sale of water amounting to R8 399 059 could not be verified as the municipality did not have sufficient controls in place to ensure that all water meter readings were recorded and that all meter readings were accurately captured on the billing system.
  - No register of new or re-connections was kept. I was therefore unable to determine the completeness and accuracy of connection fees amounting to R125 178.

- The completeness, accuracy and validity of traffic income amounting to R2 623 294 could not be verified due to the following reasons:
  - None of the receipts and deposit books prior to November 2005 were submitted for audit purposes. This placed a limitation on the scope of the audit.
  - I was unable to obtain the daily transaction reports from the municipality's computerised vehicle licensing system. I was therefore unable to verify the completeness and accuracy of income from the issuing or renewal of vehicle licences. The amount that should have been recorded as licensing revenue could not be determined.
  - The municipality should pay 80% of the income from driver's licence bookings and vehicle registrations to the Department of Transport. A total of R257 796 was paid to the Department of Transport during the year under review. I could not verify the completeness and accuracy of the amount paid to the Department of Transport as I was unable to obtain the daily transaction reports from the municipality's computerised vehicle licensing system. The amount that should have been paid to the Department of Transport could not be determined.
- The completeness and accuracy of house and site rental income amounting to R35 326 could not be determined as there was no register detailing the tenants or amounts to be paid. No rental agreements existed between the municipality and the tenants who leased houses or sites from the municipality. The monthly rent payable and the terms of the leases could not be determined.
- An amount of R116 451 was received with regard to the sale of tender documents. I was unable to verify the validity, accuracy and completeness of this amount as no register for the sale of tender documents existed and no reconciliation was done between the number of tender documents sold and amounts received.
- Income from the sale of stands was not recognised in the accounting records of the municipality when the sale took place. This income was recorded on a cash basis as and when the purchaser paid a deposit or instalments to the municipality. An amount of R99 257 was recorded in the financial records of the municipality for the year under review. I was therefore unable to verify the completeness, accuracy and validity of income from the sale of stands.

- According to statement 4.5 of the Code of Accounting Practice for Local Authorities in South Africa, transactions with respect to the development and selling of land and property must be kept in a separate set of accounts and be reported on separately.
- During the year under review the municipality operated a bank account with a commercial bank to deposit all receipts from regional offices. According to the agreement with the bank, no interest was earned on this account. This resulted in financial losses to the municipality. The amount of lost revenue could not be determined.
- The completeness and accuracy of sundry revenue amounting to R256 715 could not be verified due to a lack of supporting documents. This placed a limitation on the scope of the audit.
- Several cellphone towers were erected on the municipality's property and according to council decisions, rental was recoverable in this regard. I could not obtain information relating to the total number of towers installed on the municipality's property and details regarding the monthly rental income generated from these towers. The completeness, accuracy and validity of rental income from cellphone towers could therefore not be determined.
- The billing report for November 2005 could not be submitted for audit purposes. This placed a limitation on the scope of the audit.
- Interest charged on long-term debtor accounts was recorded on the individual manual debtor cards. The interest levied on the debtors' cards was not recorded as revenue in the general ledger of the municipality. The completeness of interest received could therefore not be verified.
- The municipality did not keep record of conditional grants received and the expenditure incurred in respect of these conditional grants. I was therefore unable to determine whether the grants were utilised for the intended purpose (i.e. schedule 4B, 6 or 7).

Furthermore, I could not determine whether any portion of these grants remained unspent at year-end. The unspent portion of these grants should be reflected as deferred revenue (liability) in the balance sheet of the municipality.

- 4.4 The accuracy and recoverability of current debtors amounting to R40 802 383 could not be verified due to the following reasons:

- The provision for doubtful debts amounting to R11 403 480 was not based on a list of long outstanding consumer accounts or a reasonable formula. The provision for doubtful debts did not seem adequate to cover the possible bad debts as consumer accounts amounting to R40 596 892 had been outstanding for 90 days or longer. I could not find any evidence that the provision for doubtful debts was approved by the council.
- The debtors balance included outstanding assessment rates amounting to R25 641 781. As reported under point 4.3 above, the municipality's valuation roll did not comply with all the legal requirements as set out in the Municipal Property Rates Act of 2004. The valuations used to calculate assessment rates might therefore be invalid and inaccurate. Outstanding assessment rates was adjusted by R47 386 850 during the year under review. This adjustment was due to excessive assessment rates levied on properties. Property values included in the valuation roll might therefore be inaccurate and might be disputed by consumers. I was therefore unable to verify the accuracy and recoverability of outstanding assessment rates amounting to R25 641 781.
- The municipality appointed a debt collection agent. The contract stipulated that the municipality would compensate the collection agent based on a percentage of the total outstanding or old debts recovered on its behalf. Although this agreement expired during April 2005 the service provider continued to deliver services to the municipality up to August 2005.

Furthermore, it came to my attention that their responsibilities expanded during the year under review to include the administration of the consumer billing system which involved invoicing, collection of payments and the issuing of receipts. The debt collection agent performed these functions up to August 2005. There were no controls in place to ensure that all consumers were correctly billed by the debt collection agent and that all receipts were remitted to the municipality.

I could not be supplied with an agreement between the service provider and the municipality authorising the agent to perform these specific functions on behalf of the municipality.

- Debtor confirmations were sent under my control to 17 selected debtors. Only 12 debtors returned their confirmations and of those returned, 10 debtors did not agree with their balance as per their consumer statement.

The debtors did not provide me with the amounts shown in their records. All these debtors indicated that they were not liable for the full balance, as they received correspondence from the municipality, requesting them to provide water to fellow community members during the dry season. The correspondence apparently stated that they would not be liable for the account.

This was a further indication that debtors' balances might not be recoverable.

4.5 The completeness, accuracy and recoverability of long-term debts amounting to R1 051 426 could not be verified due to the following reasons:

- Long-term debts amounting to R1 860 753 were written off to the appropriation account during the year under review. I was unable to obtain a list of the debtor balances that were written off and consequently I could not verify the accuracy and validity of the amount written off. I was unable to determine whether this adjustment to the appropriation account was approved by the council.
- Long-term debtors amounting to R1 051 426 have been incorrectly disclosed as current assets in the balance sheet of the municipality. These debtors balances are long term in nature as the balances relates to the sale of stands.
- No agreements between the municipality and long-term debtors could be submitted. I was therefore unable to verify the existence of long-term debtors.
- As mentioned in paragraph 3.2 above, the municipality only recorded revenue from the sale of stands on a cash basis. Long-term debtors are therefore not accurate and complete.

4.6 The completeness, accuracy and validity of the VAT receivable of R1 517 964 could not be verified due to the following reasons:

- Taxable supplies declared on the municipality's VAT returns for the year under review was R8 997 450 less than taxable supplies recorded in the municipality's income statement.



- The municipality was registered on the invoice basis for VAT purposes but accounted for VAT transactions on the cash basis.
- 4.7 The accuracy of the leave provision amounting to R3 021 671 could not be verified due to the following reasons:
- The municipality did not have a formal system in place to ensure that a leave application was completed and approved for all leave taken and that all leave application forms were recorded in the leave register. The accuracy of leave balances at year-end could therefore not be verified.
  - The leave balances used in the leave provision calculation were based on the leave balances as at October 2006, adjusted with twelve days to compensate for the fact that leave balances subsequent to year-end were used. I was unable to determine whether these leave balances actually represented the outstanding leave days as at 30 June 2006.
- 4.8 In the previous year I reported that I was unable to verify the validity and accuracy of trust funds amounting to R4 490 589. During the year under review trust funds amounting to R3 274 109 were written off to the appropriation account. The amount written off represented trust funds that could not be verified against grant agreements. I was unable to verify the validity and accuracy of the amounts written off.
- 4.9 The completeness, accuracy and existence of fixed assets amounting to R64 066 933 could not be verified due to the following reasons:
- The fixed asset register compiled by the municipality did not agree to the accounting records of the municipality. The cost price of fixed assets as per the financial statements of the municipality amounted to R64 459 094. The cost price of assets reflected in the fixed asset register only amounted to R8 841 016. No reliance could therefore be placed on the fixed asset register compiled by the municipality.
  - The existence of fixed assets could not be verified as physical assets were not numbered and no reliance could be placed on the municipality's fixed asset register.
  - The fixed asset register was not complete and accurate. A deed search indicated that twenty-nine (29) properties owned by the municipality were not accounted for in the asset register.
  - Although fixed assets (vehicles) were disposed of during the year under review, no details were disclosed in annexure C to the financial statements.

- I could not determine the selling price of fixed assets (vehicles) disposed of during the year under review. The proceeds of the fixed assets (vehicles) disposed of to the value of R40 000 were not processed correctly to the income statement.
- 4.10 The completeness and accuracy of bank and cash balances to the value of R53 229 412 could not be verified due to the following:
- No cash book was maintained on the PROMIS accounting system for the Standard Bank current account. The transactions on this account were processed from the bank statements subsequent to year-end. I was therefore unable to verify the completeness of receipts and payments in the Standard Bank current account. The balance of this account amounted to R21 654 561 at year-end.
  - In the previous year it was reported that the bank reconciliation for the Standard Bank account contained outstanding deposits amounting to R308 765. These outstanding deposits represented receipts recorded in the cash book that were not yet banked. During the year under review several journals were processed to balance the bank statement amount to the general ledger balance. I could not obtain any evidence that the outstanding deposits of R308 765 were deposited during the year under review.
  - The petty cash balance amounting to R56 430 could not be confirmed in the previous year. This amount was written off in the income statement during the year under review. I was therefore unable to verify the accuracy and validity of the amount written off to the income statement.
- 4.11 The existence, valuation, completeness and accuracy of inventory amounting to R2 685 995 could not be verified due to the following reasons:
- The stocktaking that was performed by the municipality subsequent to year-end was not attended by an independent representative of the Auditor-General. The accounting records of the municipality did not permit the application of alternative procedures in this regard. I was therefore unable to verify the existence of inventory on hand at year-end.
  - A sample of inventory items amounting to R1 902 365 was selected for testing. The cost prices of inventory items to the value of R1 861 439 could not be verified against purchase invoices.

- Inventory was not valued in terms of the municipality's accounting policy. The accounting policy of the municipality stated that inventory was valued at the lower of cost, determined on the weighted average basis, and the net realisable value. All inventory items were valued based on the purchase price of inventory items subsequent to year-end. Inventory was therefore not valued on the weighted average cost basis.
- 4.12 The completeness, accuracy and validity of unspent conditional grants amounting to R1 213 480 could not be verified. In the previous year we reported that we were unable to verify the validity and accuracy of trust funds amounting to R4 490 589. During the year under review management allocated R1 213 480 of the trust funds to unspent conditional grants and disclosed it as part of creditors at year-end. We were unable to verify this balance of R1 213 480 against grant contracts or agreements.
- 4.13 There was no movement other than interest and bank charges on the FNB PHP Project Call investment account. The balance of the account was R624 264 at year-end.

I was unable to determine whether the balance of this account represented restricted funds as the municipality could not provide me with grant documentation.

It is my understanding that additional expenditure was incurred on the PHP project during the year under review. This expenditure was however funded from the municipality's operational bank account.

I could not determine whether the PHP call account should have been disclosed as investment funds or restricted funds.

- 4.14 The Municipality was appointed as the Water Services Authority for the Bushbuckridge area as from 1 March 2006 (Gazette number 28931 - Notice 554). This appointment followed the disestablishment of the Bohlabela District Municipality. Correspondence between the Bushbuckridge Municipality and the Department of Provincial and Local Government indicates that certain assets and employees will be transferred to the Bushbuckridge Municipality as a result of the Municipality's appointment as the Water Services Authority. We were unable to obtain any formal agreement that indicates the number of staff members or the value of assets that will be transferred. We were also unable to determine the effective date from when the assets or staff will be transferred to the Municipality.

The revenue, assets and liabilities that arose due to the Municipality's appointment as the Water Services Authority are not reflected in the annual financial statements of the Municipality. The impact of the Municipality's appointment as the Water Services Authority on the financial statements could not be determined due to the lack of formal agreements or documentation in this regard.

## **5. ADVERSE AUDIT OPINION**

In my opinion, because of the significance of the matters discussed in the preceding paragraph and its effect on the financial statements, the financial statements do not present fairly, in all material respects, the financial position of Bushbuckridge Municipality at 30 June 2006 in accordance with the basis of accounting described in paragraph 3 and in the manner required by the Municipal Finance Management Act, Act No 56 of 2003.

## **6. EMPHASIS OF MATTER**

Attention is also drawn to the following matters:

- 6.1 According to statement 4.5 of the Code of Accounting Practice for Local Authorities in South Africa, the accrual basis of accounting shall be used in measuring the financial position and operating results of the municipality.

This means that all income must be recorded as it is earned, i.e. received in case of direct income such as traffic fines; or levied in case of services rendered.

The municipality recognised income from house and site rental on a cash basis during the financial year under review. Income was therefore only recognised once payment was received from lessees. The total income from house and site rentals amounted to R35 325.

The municipality used the computerised PROMIS accounting system, which was specifically designed for the use of municipalities. The municipality did not, however, make effective use of PROMIS and appointed a consultant to assist in the finalisation of the general ledger and trial balance.

- 6.2 The following is reported for the budget process:

➤ No controls were in place to monitor actual results against the budget.

- The 2005-06 budget was presented by the mayor at a council meeting held on 19 May 2005. This was 30 days before the start of the new financial year. The budget was therefore not discussed 90 days before the start of the financial year as required by section 16(1) of the MFMA.
- The National Treasury requires that a municipality should submit to them by not later than 30 June of a year, its budget for the next financial year and such other budgetary information as required, including, but not limited to, information on the nature and extent of basic services, including free basic services, to be provided by that municipality. This was not complied with as the budget for the 2006 financial year was not submitted in time.
- The National Treasury also requires a municipality to submit to them, to the national accounting officer responsible for local government, as well as to the provincial department responsible for local government, not later than 10 days after the end of each quarter, information on the implementation of the budget, including, but not limited to, information on actual revenue collected, actual total spending on water, electricity, refuse removal, municipal infrastructure and free basic services. This was not complied with.
- The following matters were noted where the municipality did not comply with the MFMA regulating the budget process:
  - Particulars relating to the municipality's investments were not presented with the 2005-06 annual budget.
  - The 2005-06 budget did not provide any information regarding the proposed cost relating to salaries, allowances and benefits for political office bearers, councillors of the municipality, the municipal manager or the chief financial officer.
  - I was unable to obtain any information regarding service delivery agreements which should accompany the tabled annual budget.
  - I was unable to obtain budget/council meeting minutes to determine whether the mayor at least 10 months before the start of the budgeted year, tabled in the municipal council a time schedule outlining key deadlines for the following:
    - The preparation, tabling and approval of the annual budget.
    - The annual review of the integrated development plan (IDP) and the budget-related policies.
  - The tabling and adoption of any amendments to the integrated development plan.

- I could not obtain the minutes of the budget meetings to determine whether there was any correspondence regarding non-compliance with the MFMA requirements pertaining to the tabling or approval of the annual budget.
  - I was unable to obtain a draft service delivery and budget implementation plan, which should have been submitted 14 days after the approval of the annual budget, by the accounting officer (MM) to the mayor.
- The following control weaknesses were noted in the municipality's budget process:
- Actual revenue and expenditure regarding the year preceding the budget year were not disclosed on the 2005-06 annual budget.
  - The budget did not include a projection of cash flow for the budget year by revenue source, broken down per month.
  - The 2005-06 budget did not include a 3-year capital budget to address backlogs in municipal infrastructure.

6.3 Section 40 of the Division of Revenue Act, 2006 (Act No. 2 of 2006) states that: "The relevant receiving officer must, in respect of an allocation transferred to a municipality, submit a report to the relevant transferring national or provincial officer."

Section 40(4) of the same act states that a monthly report should be submitted to the transferring national officer detailing "The actual expenditure incurred by the Municipality, as the case may be, for the month reported on and for the financial year up to the end of that month; The extent of compliance with the conditions of an allocation and with this Act"

The reports required by section 40 of the Division of Revenue Act were not submitted to the relevant transferring national or provincial officer.

6.4 According to Statement 33 of GAAP for Local Government, cleansing and sewerage services delivered to the community are classified as economic services. Economic services are services in respect of which the tariffs should be fixed in such a way that the full costs of providing these services may be recovered without incurring a surplus or deficit.

It is required that the various operating income and expenditure transactions relating to the various services provided by a local authority be disclosed in objective form in the income statement and in appendix E to the financial statements. This information was, however, not reflected. It was therefore not possible to determine whether the above-mentioned

services to the community yielded a surplus or loss for a specific financial year.

## 6.5 Assets

- The fixed asset register was not complete as it lacked the following details, which were required in terms of the municipality's policy:
  - Asset identification number
  - Region where asset is situated
  - The value of the asset
  - Date purchased
  - Date of disposal
- Due to the absence of a proper fixed asset register I was unable to determine whether sufficient short-term insurance existed with regard to fixed assets.
- A fixed asset count was not performed during the year under review as required by Standard Financial By-law no. 53(3).

## 6.6 Value-added tax

- No reasonable allocation (formula) existed to distinguish between taxable and non-taxable services paid for to suppliers by the municipality. This allocation formula is needed in order to determine amounts paid in respect of VAT to suppliers that can be claimed back from SARS and should be approved by SARS.
- The municipality is currently registered to submit VAT returns on a bi-monthly basis. Revenue exceeded the threshold of R30 million per annum, whereafter the municipality should submit VAT returns on a monthly basis as required by the Value-added Tax Act.
- No zero-rated items were declared on the VAT201 returns for both Output and Input VAT.
- The VAT 201 returns for the 2005-06 financial year were not submitted by the 25th of the month following the end of the VAT period as required by the VAT Act.

<b>VAT 201 month</b>	<b>Date submitted</b>
November 2005	8 March 2006
January 2006	8 March 2006
March 2006	13 October 2006
May 2006	13 October 2006

- I was unable to determine whether site rentals were recorded exclusive of VAT.

#### 6.7 Investments

- The IMFO Code of Investment Practice, *inter alia*, requires a municipality to maintain a proper record of all investments indicating the institution, fund, interest rate, interest earned etc. (section 11). There was, however, no investment register in place at the municipality.
- Investment reconciliations were not prepared on a monthly basis. The reconciliations were not reviewed by a senior municipal official.

6.8 Council policy regarding the allocation of interest earned on funds invested could not be obtained. No interest was allocated to the Capital Development Fund during the year under review.

#### 6.9 Bank reconciliations

- Bank reconciliations were only prepared at year-end for the financial year under review and were therefore not:
  - reviewed on a monthly basis by a senior official of the municipality, and
  - submitted to the council on a monthly basis as required by regulation 1536 (*Government Gazette* dated 14 November 1997).
- No register was kept of "Refer to drawer" (R/D) cheques returned by the municipality's bankers.

#### 6.10 Weaknesses in internal control

- The audit approach of the Auditor-General involves evaluating institutions against predetermined levels of financial management in terms of the financial management capability model. This will allow for assessing over time whether financial management is improving within the municipality and allow for the entity to be benchmarked against other public sector entities.

The Bushbuckridge Municipality is still considered to be at the start-up level (level 1) in terms of the financial management capability model.



The following characteristics are associated with a municipality at the start-up level:

- No proper control framework.
- Financial accounting and internal control systems are not properly developed.

From the above it is evident that I did not expect to see an elaborate system of internal controls at the municipality. I did however expect to see reasonable controls commensurate with the level of activity of the municipality. In the 2005-06 management letter as well as for the previous five financial years' management letters I reported extensively on all identified control weaknesses and the lack of adequate controls. It is of great concern to me that the municipality has made very little progress in addressing these shortcomings.

➤ The following aspects regarding consumers (water) were observed:

- No contractual agreement was entered into between the municipality and the consumer before the municipality rendered services to the end user. This was in contravention of the current credit control and debt collection policy adopted by the municipality on 3 December 2002 as well as the municipality's adopted water by-laws proclaimed on 12 August 2005. No cut-off list could be obtained for disconnections made during the 2005-06 financial year.
- No register was kept for new or re-connections.

➤ The credit control and debt collection policy of the municipality was adopted on 3 December 2002, however, the municipality did not enforce this policy. The following aspects are highlighted:

- Interest will be charged on outstanding amounts - I could not find any evidence that interest was charged on long overdue consumer debtor accounts.
- A consumer that is in arrears will not receive any services until his/her account has been paid up to date - Consumers only paid a part of their outstanding account before services were reconnected.
- Legal action should be taken against long outstanding debtor balances - No long-term debt policy existed, no legal action was taken against long overdue consumer debtors.

➤ The following shortcomings were identified in the internal control over cash at the regional offices:

- One employee was responsible for receiving the cash, issuing the receipts, recording the amounts in the manual cash book and depositing the cash.
  - Cash collected during a specific day was only banked the following day and there were no procedures in place to prevent the rolling of cash.
  - No cash counts were performed during the year.
  - No reconciliations were performed between total receipts, cashbook listing and monthly return sent to Head Office.
- There was a lack of control over income from traffic fines. I could not find any evidence that the municipality had implemented controls to ensure that:
- all fines paid at the local Magistrate's office were paid over to the municipality;
  - long outstanding fines were followed up and collected.
- The municipality had no formal expenditure-related controls in place to ensure that:
- the purchases of goods and services were approved;
  - only goods and services actually received were paid for;
  - payments were properly authorised;
  - all supporting documents were cancelled after payment, properly filed and kept for future reference;
  - three quotations were obtained for expenditure;
  - payment vouchers and orders were marked as “cancelled” or “paid”.
- The following control weaknesses with regard to the tender process were identified:
- No tender register was kept.
  - The tender adjudication process was not properly documented and kept for future reference.
  - Tender documents were not properly filed.
- Although a cellphone policy existed at the municipality I could not find any evidence that cellphone expenses were monitored during the year under review.
- It was evident that there were significant internal control shortcomings with regard to salary payments and related issues. I identified the following shortcomings during the course of the audit:

- The computerised payroll system (Pay-Day) was not utilised to its full potential due to the fact that employees were not properly trained.
  - There was no control over standing master data (e.g. adding new employees to payroll, changing employee banking details or monthly salaries etc.).
  - The human resources policies and procedures were not updated regularly (last updated in 2003).
  - A senior independent employee did not review the payroll.
  - Non-statutory deductions were not authorised.
  - All salary expenses were allocated to one account in the general ledger. The budgeted departmental salary expenses could therefore not be compared to the actual departmental salary expenses, indicating that the salary budget was not properly managed for the period under review.
  - I was unable to determine whether vacant positions were available on the organisational structure. A signed copy of the “Organogram” for the 2005-06 financial year could not be obtained.
  - In the prior year’s management letter I recommended that the municipality perform a headcount of all employees to address the risk of possible fictitious employees. I could not find any evidence that the municipality attempted to address the risk.
  - No overtime policy could be obtained.
  - Employees did not always sign the attendance registers.
  - No review of the Earnings Analysis Report was done by a senior official.
  - Access to payroll records was not restricted. It was noted that many employees entered the payroll office where the payroll records were kept. The payroll records were therefore accessible to anyone who entered the payroll office.
  - The salary system (Pay-Day) and the general ledger (PROMIS) were not integrated and journals were processed to capture payroll transactions in the general ledger. I was unable to obtain journal vouchers for these journals and there was no proof that these journals were authorised or reviewed.
  - No reconciliations were performed between the PROMIS accounting system and the Pay-Day payroll system. It was not clear whether all payroll costs were correctly transferred to the accounting system.
- No amount regarding consumer deposits was reflected in the financial statements of the municipality as required by the adopted water by-laws. I am of the opinion that a system whereby deposits for water usage are collected from end-users will be to the benefit of the municipality as it will have an effect on losses suffered by the municipality due to the non-payment of consumer accounts.

- Progress reports were not maintained for projects. The municipality did not have proper controls in place to monitor the progress on projects and to ensure that projects were completed on time within the approved budget.
- Expenditure was not always allocated to the correct budget vote in the general ledger which resulted in an under- or overspending in the individual vote accounts. I could not perform a proper review comparing budget vs actual expenditure.
- No payments were made to SETA or the Commissioner regarding a skills development levy for the financial year under review. A skills development levy was calculated on the Pay-Day payroll system but no amounts were paid to the relevant third party. The municipality might be liable for penalties and interest in the event that payments were not made on a timeous basis.

The municipality's balance sheet did not reflect a liability for skills development levies calculated but not paid.

- The EMP 201 returns for the months of July 2005 to February 2006 could not be obtained. EMP 201's were only completed and submitted to the Receiver of Revenue from March 2006.
- I could not obtain evidence that journals amounting to R107 145 425 were reviewed and approved by the CFO. I was therefore unable to verify whether these journals were properly authorised.
- The municipality did not maintain a contract register. I was unable to verify the completeness of contracts.

6.11 Paragraph 6.22.1 of the Code of Accounting Practice for Local Authorities in South Africa requires the presentation of statistical information, including the publication of water statistics such as number of users, kilolitres bought, kilolitres sold and loss in distribution.

Due to various reasons, there was no system in place at the municipality to summarise water sold to end-users in order to ensure that the loss in water distribution was monitored on a monthly basis. Abnormal water losses could therefore not be identified on an ongoing and timely basis.

6.12 Fringe benefits: Rental to employees

- Several of the employees rented houses from the municipality. I noted that the municipality did not perform any calculations to determine

whether these employees received a fringe benefit. A fringe benefit will arise when the rent paid by employees is below market-related rentals. The municipality did not have a rental register or signed rental agreements and I was therefore unable to determine the fringe benefits that might arise from these rentals.

- No formal policy regarding the leasing of these houses to employees could be obtained. No list or register of employees who rented these houses could be obtained. There was a possibility that employees who occupied these houses did not pay rent or that rent was not deducted from their monthly salaries. No lease agreements could be obtained which were entered into between the employee and municipality.

### 6.13 Employee leave

- Leave application forms were not always captured on the salary system for the financial year under review. Manual leave registers were maintained for the following:
  - Annual leave
  - Unpaid leave
  - Sick leave
  - Other leave

These manual leave registers were filed in the employee files. I also found that for two employees, their leave registers differed from their leave applications.

- Section 7(4) of the South African Local Bargaining Council (SALBC) agreement states that leave accumulated subsequent to 1 January 2004 may be accumulated to a maximum of forty-eight (48) days. The leave balances of 45 employees exceeded the maximum of 48 days.
- The Human Resource Policy had not been updated to reflect the change in annual leave entitlement. The annual leave entitlement was 24 days as prescribed by the South African Local Bargaining Council (SALBC) agreement.
- No leave application forms or medical certificates could be obtained for the two employees who took sick leave as per the leave registers.
- I was unable to obtain leave registers and leave application forms for three contract workers.
- The leave provision of R3 021 671 was disclosed as part of the total creditors balance of R53 006 047 in the financial statements. The

leave provision should be disclosed as part of provisions as a separate line item in the annual financial statements.

#### 6.14 Performance bonuses

- No new performance agreements were entered into between the municipality and the managers employed by the municipality during the 2005-06 financial year. This was contrary to the requirements of section 57 of the Municipal Systems Act.

#### 6.15 Current and long-term debtors

- No bad debts were written off during the 2005-06 financial year. An approved policy to identify and approve bad debt write-offs did not exist.
- Long outstanding debtors (9 debtors) did not make any payments after year-end. I could not find any evidence that these long outstanding accounts were actively followed up.

6.16 I was unable to obtain proof that the accounting officer delegated in writing the authorised signatories on the municipality's bank account in terms of the MFMA section 11(1).

#### 6.17 Inventories

- The purchases and issues of stock were not recorded in the general ledger during the year under review. A stock count was performed subsequent to year-end and the balance of inventory was adjusted to agree to the stock count.
- Manual issue vouchers were not properly completed. The unused portion of the inventory requested section was not crossed out.

#### 6.18 Assessment rates

- Section 3(1) of the Municipal Property Rates Act, 2004 (Act No. 6 of 2004) requires the council of the municipality to adopt a policy consistent with this act on the levying of rates on rateable property in the municipality.

A Rates Policy did exist. I was however unable to obtain any evidence that this policy had been implemented and/or approved by the council.

- Section 23 (1) of the Municipal Property Rates Act of 2004 requires a municipality to draw up and maintain a register in respect of properties situated within that municipality, consisting of a Part A and Part B.

The register kept by the municipality did not comply with section 23 of the Municipal Property Rates Act with regard to the following requirements:

- *Section 23(2) states that Part A of the register should consist of the current valuation roll of the municipality, including any supplementary valuation rolls of the municipality prepared in terms of section 78.*

The register obtained did not include the property values as per the valuation roll.

- *Section 23(3) states that Part B of the register must specify which properties on the valuation roll or any supplementary valuation rolls are subject to –*
  - *an exemption from the rate in terms of section 15;*
  - *a rebate on or a reduction in the rate in terms of section 15;*
  - *a phasing-in of the rate in terms of section 21; or*
  - *an exclusion referred to in section 17(1)(a),(e),(g),(h) and (i).*

The register submitted did not include the information required by section 23(3).

- *Section 23(5) states that the municipality should at regular intervals, but at least annually, update Part B of the register.*

The municipality did not comply with the requirements of this section as the register did not include a Part B.

6.19 The following items were not properly disclosed in the financial statements or were not disclosed at all:

- Note on assessment rates, disclosing assessment rates charged for the year as well as the value of properties included in the valuation roll. The rate at which assessment rates were charged should also be disclosed.

6.20 In addition to matters raised elsewhere in this report regarding non-compliance with laws and regulations, a number of concerns with regard to non-compliance with various legislative requirements were identified. Full details regarding these concerns were brought to the attention of the municipal manager in the management letter dated 28 November 2006.

6.21 Municipal infrastructure grants were previously administered by the Bohlabela District Municipality on behalf of Bushbuckridge Municipality. Towards the end of the current financial year the municipality received R28 533 000 from the Department of Local Government and Housing specifically for the purposes of funding municipal infrastructure development within the municipality's demarcated area.

I could not find any evidence that the municipality had developed and implemented a system of control to ensure that:

- infrastructure needs were properly assessed and that proper feasibility studies were completed;
  - all intended projects were properly approved;
  - there was proper coordination between the municipality, provincial and national government and local communities;
  - expenditure was compared to the amount allocated and that any excess expenditure was approved.
- 6.22 No report regarding unauthorised, irregular, fruitless or wasteful expenditure was submitted to the mayor, MEC for Local Government or the Auditor-General as prescribed by section 32(4) of the MFMA. No fruitless, unauthorised, irregular or wasteful expenditure was disclosed in the financial statements.

## **7. APPRECIATION**

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

A N Dzuguda  
*for Auditor-General*

Polokwane  
28 November 2006