

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

1. AUDIT ASSIGNMENT

The financial statements as set out on pages 3 to 8 and 17 to 27 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.

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's policy is to prepare the financial statements on the entity specific basis of accounting as described in note 1 of the accounting policies to the financial statements.

4. QUALIFICATION

4.1 Rates income

- a) As a result of not implementing a property register the completeness and accuracy of the valuation roll and resulting rates income could not be confirmed.
- b) Assessment rates – note 11 in the financial statements did not disclose any information with regards to valuations and tariffs.

4.2 Services income

- a) Due to the lack of monthly reconciliations, material unexplained differences were noted between the meter reconciliation report and the service charge printouts. The accuracy and completeness of services income could therefore not be confirmed. This could indicate that inadequate financial management discipline was exercised in performing the reconciliations.

4.3 Equitable share

- a) According to the Division of Revenue Act, 2005 (Act No. 1 of 2005) the municipality was allocated equitable share of R9 336 000. The accounting records only indicated R8 921 109. The difference of R414 891 could not be explained by the municipality and resulted from the lack of financial management discipline in monitoring the equitable share receipts.

4.4 Rental income

- a) Management had the obligation to put in place controls to manage rental income. During my audit only two rental agreements could be obtained for the renting of municipal properties. No council policy on rental tariffs existed. The accuracy, validity and completeness of rental income disclosed as R111 957 in the financial statements could therefore not be confirmed.

4.5 Interest income

- a) External interest received according to the bank confirmation letters amounted to R156 464. Note 14 to the financial statements only indicate external interest of R20 127. The difference of R136 336 resulted from the lack of financial management discipline in reviewing the financial statements.

4.6 Expenditure

- a) Due to the lack of financial management discipline in processing invoices timely expenditure of R86 860 relating to the prior year was recognised in the 2005/06 year. Expenditure was therefore overstated.
- b) Supporting documentation could not be obtained for payments totalling R109 149 and journals totalling R29 375. The accuracy and validity of the expenditure could therefore not be confirmed. This resulted from the lack of

financial management discipline in monitoring the internal controls relating to expenditure management.

4.7 Value added tax (VAT)

- a) The municipality's accounting system was inadequate to account for VAT. Consequently the general ledger accounts were not used for VAT calculation purposes. Separate spreadsheets were maintained for completion of the monthly VAT returns. The amount owed at 30 June 2006 according to the VAT returns was R74 156 and R154 365 according to the financial statements.
- b) The VAT output provision balance of R1 713 467 at 30 June 2006 could not be reconciled to the supporting documentation.
- c) VAT returns were not submitted on time and were not reviewed by a senior official as required for good financial management discipline, resulting in input VAT claimed on disallowed expenditure amounting to R103 344.

4.8 Debtors

- a) The provision for bad debt was disclosed as R9 200 018. According to the age analysis at 30 June 2006, debtors older than 90 days amounted to R14 239 142. The municipality did not use any basis to determine the adequacy of the provision. The provision was therefore understated resulting in debtors being overstated with approximately R5 039 124.
- b) Due to the lack of financial management discipline in performing reconciliations the debtor amount of R16 504 478 in the financial statements differed from the debtors control account amount of R16 563 779. The difference of R59 301 could not be explained by the municipality.
- c) Journals amounting to R557 335 were debited to the debtors control account. No supporting documentation could be obtained to verify the validity and accuracy thereof. This resulted from the lack of financial management discipline in monitoring the internal controls relating to debtor management.

4.9 Assets

- a) Although an asset count was performed by the municipality, it was not reconciled to the asset register. The completeness, existence and valuation of assets disclosed in the financial statements as R1 190 188 could not be confirmed due to the lack of detail in the asset register.
- b) Management did not implement a proper system to account for asset. Assets amounting to R4 566 551 were capitalised by means of journal entries. No supporting documentation could be obtained to verify the accuracy and validity of the assets.
- c) Management did not implement a proper system for project management. Consequently, the accuracy and completeness of additions to assets resulting from project expenditure could not be confirmed.

- d) Management lacked the ability to put in place controls to help it identify and implement the appropriate accounting treatment for leased assets. Assets and liabilities were understated with an unknown amount resulting from leased assets that were not capitalised and liabilities not recognised in the financial statements.
- Twelve different debit orders amounting to approximately R101 254 monthly were noted on the bank statements.
 - No leased asset accounting policy existed.
 - No evidence could be obtained that VAT was accounted for on any of the leases.
 - Not all agreements could be obtained for audit purposes.
 - Not all the leased assets could be located.
 - No evidence could be obtained that quotations were obtained or tender procedures followed in procuring the assets.
 - Section 46(2) of the MFMA was not adhered to as the municipal manager did not sign the debt agreements and the mayor did not approve them by signing the relevant council minutes as it was never laid before council.
 - Section 46(3) of the MFMA was not adhered to as the debt was not made public.

4.10 Bank and cash

- a) The accounting records were inaccurate and incomplete due to management's inability to implement controls to help it identify exceptions in the accounting records. A cheque sequence error resulted in various cheques indicated as cancelled on the accounting system although the physical cheque was drawn and various cheques recorded as valid payments on the accounting system although the physical cheque was cancelled. The cash book balance did not correspond with the cash book balance used in the bank reconciliations. This error was not identified by the officials compiling or reviewing the bank reconciliations. The list of outstanding cheques on 30 June 2006 was understated with at least R203 452.
- b) R27 332 was received on 30 June 2006 but not banked. The bank reconciliation did however not indicate any outstanding deposits.

4.11 Trust funds

- a) Supporting documentation for trust fund payments totalling R216 626 could not be obtained for audit purposes. The accuracy and validity of the expenditure could therefore not be confirmed. This resulted from the lack of financial management discipline in monitoring the internal controls relating to trust fund expenditure management.
- b) Trust fund expenditure of R4 962 855 was incurred for the year. Due to the lack of a proper system to account for trust fund expenditure, only two business plans of the 16 projects could be obtained for audit purposes. It could therefore not be confirmed if all money was utilised in line with the conditions of the funds.
- c) Due to the lack of competent and skilled officials, the municipality appointed a consulting engineering firm to perform project management on all the projects. Tender procedures were not followed in appointing the firm. A service level agreement did not exist with the firm. Evidence could not be obtained that the municipality monitored the projects. The infrastructure manager position was vacant for the entire year. This resulted in the overspending on four projects amounting to R107 203.
- d) A policy on the allocation of interest did not exist. Consequently, interest was not allocated to any of the funds indicated in annexure A to the financial statements.
- e) Trust fund expenditure was overstated with R46 426 due to a journal processed incorrectly.
- f) A clear audit trail did not exist between the income and expenditure on the trust funds and the movement in the investment accounts due to the lack of a proper system to account for trust fund expenditure.

4.12 Leave provision

- a) Due to the lack of financial management discipline in maintaining adequate leave records, the leave provision of R311 718 could not be confirmed as accurate and complete.

4.13 Creditors

A proper system to account for creditors was not implemented. This resulted in the following:

- a) No payment numbers were indicated on the creditor list submitted for audit purposes. Consequently, I could not verify the validity, accuracy and completeness of creditors.
- b) Creditors were understated with at least R26 256 due to transactions recognised in the wrong financial year.

- c) Tax was deducted incorrectly from the monthly salary payments resulting in an under recovery of tax. The creditor in respect of the South African Revenue Services was therefore understated.
- d) No calculation could be submitted for the short term portion of the long term loans disclosed as R139 135.

4.14 Commitments and capital projects

- a) Commitments were not disclosed in the financial statements. Various projects and lease agreements were however in progress at year-end. Due to the lack of a proper system to account for projects and leased assets the accuracy and completeness of commitments could not be confirmed.

4.15 Unappropriated surplus

- a) Supporting documentation could not be obtained for entries on the unappropriated surplus account amounting to R128 960. This resulted from the lack of financial management discipline in monitoring the internal controls relating to management of the general ledger.

4.16 Unauthorised expenditure

- a) Due to the lack financial management discipline in monitoring the budget, the actual expenditure for the year of R35 942 083 exceeded the budget of R33 605 543 with R2 336 540. No unauthorised expenditure was disclosed in the financial statements as required by section 125(d) of the MFMA.

4.17 Financial statements disclosure

- a) The financial statements deviated significantly on various disclosure requirements as set by IMFO and various casting and cross-referencing errors were noted. Although the cash flow statement reconciled, the supporting notes differed materially from the amounts in the cash flow statement. This resulted from the lack of competency and skill in compiling and reviewing the financial statements. Furthermore, the following instances of non-adherence to legislation was noted with regards to disclosure in the financial statements:
 - Remuneration of councillors and senior management was not disclosed in the financial statements as required by section 124(1) of the MFMA.
 - Amounts paid in audit fees, taxes, levies, duties and pension and medical aid contributions were not disclosed in the financial statements as required by section 125(1) of the MFMA.
 - Disclosure was not made in the financial statements of non-compliance with the MFMA as required by section 125(2)(e) of the MFMA.

5. DISCLAIMER OF OPINION

Because of the significance of the matters in the preceding paragraph, I do not express an opinion on the financial statements.

6. EMPHASIS OF MATTER

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

6.1 Going concern

The following conditions indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to continue as a going concern:

- a) Debtors increased with 15% from the prior year to R16 504 478 at 30 June 2006.
- b) Water and electricity distribution loss information was not disclosed in annexure F to the financial statements. Details and supporting evidence for the distribution losses incurred by the municipality could not be submitted. The amount of forfeited revenue could therefore not be calculated.
- c) Only 26% of statutory and trust funds were represented by investments, resulting in an uninvested portion of R7 942 853.
- d) The income statement indicated that the municipality realised a deficit of R7 030 943 for the 2005/06 year (2005: R820 412 profit).
- e) The Douglas holiday resort realised a deficit of R843 429 (2005: R733 213 deficit, 2004: R352 236 deficit).

6.2 Irregularities

6.2.1 Commonage land

- a) According to a council resolution the commonage land should be transferred to a trust. Management indicated that the council resolution was incorrectly minuted as it was the administration of the commonage land that should be transferred. The transfer was not done by 30 June 2006 and no agreement was signed. However the trust already issued mining permits in this regard.

6.2.2 Cash shortages

Due to the lack of segregation of duties, review and monitoring over the cash components within the municipality, the following were noted:

- a) Five surprise cash counts were conducted during October 2006 at different cash points. Unexplained differences were noted at all of them.
- b) A reconciliation of the motor licensing cash received on behalf of a government department and the depositing of the money into that bank account, indicated that R18 876 was not deposited.
- c) A reconciliation of the motor licensing cash accruing to the municipality and the depositing of the money into the municipal bank account indicated that R11 712 was not deposited.
- d) It was noted that the municipality instituted investigations into eight cases of alleged cash and equipment theft.

6.2.3 Mayor travel allowance

- a) The travel allowance of R72 000 received by the mayor was R40 600 more than the upper limit of R31 400 set in *Government Gazette* no. 28231 of 14 November 2005 in relation to the Remuneration of Public Office Bearers Act, 1998 (Act No. 20 of 1998).

6.2.4 Appointment procedures not followed

- a) Three officials were appointed on 1 December 2005 without advertising the positions, compiling shortlists or interviewing the applicants. Council approved the appointments on 13 February 2006, after the appointment date. No personnel files could be submitted for these officials.

6.2.5 Salary adjustments

- a) Two officials' salaries were adjusted upwards (over and above the 6% annual increase) with R11 752 per annum each. No authorisation could be obtained for the adjustments.

6.2.6 Wage payouts

- a) Wage payouts were made to two officials that did not appear on the wage register.

6.2.7 Subsistence and travel claims

- a) Subsistence and travel claims amounting to R84 221 was not approved by the relevant authority.
- b) Insufficient supporting documentation was attached to claims amounting to R25 415.

6.3 Fruitless and wasteful expenditure

6.3.1 *Meter reading outsourcing*

- a) The municipality outsourced the meter reading function on 1 March 2004. The 2005-06 charges amounted to R248 309 after VAT was claimed. It could cost the municipality approximately R134 700 to perform the function itself. The difference of R113 609 could be regarded as fruitless expenditure.

6.3.2 *Surveillance system*

- a) A surveillance system was procured by means of a lease agreement with a monthly premium of R3 947. The surveillance system was not in operation. No camera footage was available to assist with the cash theft incidents as referred to elsewhere in this report. The expenditure could therefore be regarded as fruitless and wasteful.

6.3.3 *Operational bank accounts*

- a) The municipality operated with two operational cheque accounts during the year. The primary bank account was in overdraft and the other bank account not. All money was not paid into the primary bank account as required by section 8(2) of the MFMA. 5.5% interest was earned on the favourable bank account balance whilst 11% interest was paid on the overdraft. The additional interest paid that could have been avoided by consolidating the bank accounts could be regarded as fruitless expenditure.

6.3.4 *Policies*

- a) R10 000 was paid to a consultant for the drafting of policies. These policies were however not approved by council. The expenditure could therefore be regarded as fruitless expenditure.

6.4 Weaknesses in internal control

Every municipality shall establish and maintain an effective system of internal control in terms of section 62(1)(c) of the MFMA. I reviewed the accounting and internal control systems and in my opinion the systems of internal control did not provide adequate assurance that assets were safeguarded and that transactions were completely and accurately recorded. Due to the lack of policies and procedures, the following weaknesses in internal control were noted:

6.4.1 *Administration and governance*

- a) Generally, the minutes of council meetings did not clearly reflect the discussion that took place on items and did not clearly indicate if the council approved the item. The minutes were not signed by the chairperson. Resolutions taken could therefore be invalid. The attendance register was not always kept therefore it could not be confirmed if a quorum existed.

- b) A risk management policy was not in place. Consequently, no risk assessment was performed and no fraud prevention plan compiled.
- c) No proof could be obtained that the municipality had mechanisms in place to identify and respond to exceptional circumstances. No business continuity plans, backup policies or retention policies existed. During June and July 2006 the municipality experienced a system crash. Consultants responsible for the electronic accounting systems of the municipality confirmed that all information was restored. No measures were put in place after the previous system crash in May 2005.

6.4.2 Debtor management

- a) The credit control policy were not implemented effectively as various instances were noted where long outstanding debtor accounts were not closed, various accounts did not show any payments received and services were not discontinued.
- b) Various approved indigent applications did not meet the requirements as set in the credit control policy.

6.4.3 Asset management

- a) Trip authorisation forms or log books did not exist for any of the 32 council vehicles.
- b) Eleven of the vehicles were not in working condition.
- c) Eight vehicles were identified that were not registered on the National Traffic Information System.
- d) Annexure C indicated that assets procured from operating income amounted to R81 155. Annexure D however indicated that no assets were procured from operating income.
- e) Annexure D did not disclose any capital charges. The auditor noted capital charges of at least R1 293 891.
- f) The insurance contract could not be obtained for audit purposes.

6.4.4 Cash and bank

- a) Due to the lack of budget monitoring the municipality expensed excessively at year-end in order to utilise the budgeted amounts. The average outstanding items on the bank reconciliations for January 2006 to May 2006 were R734 760 compared to the R2 508 076 for June 2006.
- b) Not all bank reconciliations were reviewed by a senior official.

6.4.5 Expenditure management

- a) Various instances were noted where supporting documentation was not approved by the head of the department.
- b) Various instances were noted where the required number of quotations were not obtained prior to procuring the goods or services.
- c) Invoices were not stamped to prevent re-submission for payment.

6.4.6 Employee cost

- a) The organogram used was outdated as it was approved 2 August 2004.
- b) Job descriptions did not exist for any official in the municipality.
- c) No time sheets or attendance registers existed to support the overtime hours worked. Therefore the completeness of hours worked and whether the supervisor reviewed the time sheet could not be verified. No overtime policy was in place. Overtime was still paid out after a council resolution on 6 June 2006 resolved that overtime may not be paid out.
- d) Time sheets or attendance registers did not always exist to support the wage payouts. No approved documentation could be obtained to verify the accuracy of the hourly wage tariffs. No proof of identification existed for any wage earner.
- e) Resignation related documentation were not always filed in the personnel files of officials that resigned. The accuracy of the amounts paid out could therefore not always be confirmed.
- f) Evidence could not be obtained that salary runs were reviewed by the head of the department.

6.5 Non-compliance with laws and regulations

6.5.1 The Municipal Financial Management Act, 2003 (Act No. 56 of 2003)

- a) An approved delegated authority matrix did not exist as required by section 59(1). In the absence of approved delegations the municipal manager should approve all expenditure. Various instances were noted where other officials approved expenditure.
- b) The financial statements were not submitted within two months after the end of the financial year as required by section 126(1). The financial statements were submitted on 1 September 2006.
- c) The council approval for the overdraft facility amounting to R750 000 could not be submitted for audit purposes. Therefore, it could not be confirmed that the requirements of section 45(3) was complied with. Furthermore, the municipality

did not submit their banking details to the provincial treasury and Auditor-General before the start of the financial year as required by section 9.

- d) Evidence could not be obtained that the 2005-06 budget was made public by advertising it in the local newspaper as required by section 22.
- e) Evidence could not be obtained that the mayor tabled a time schedule of key deadlines at least 10 months before the start of the financial year as required by section 21(1)(b).
- f) The mayor did not submit a report to council on the implementation of the budget and the financial state of affairs of the municipality as required by section 52(d).
- g) Evidence could not be obtained that quarterly reports were submitted to the provincial department responsible for local government in the province or the Auditor-General as required by section 11(4)(b).
- h) Three councillors' rates and services accounts amounting to R3 230 were outstanding for 90 days and longer. This was not disclosed as required by section 124(1)(b).

6.5.2 *Local Government Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA)*

- a) According to section 57 municipal managers and managers directly accountable to the municipal manager may be appointed to that position only in terms of a written employment contract and subject to a separate performance agreement. An employment contract for one manager could not be obtained. Signed performance agreements did not exist for the municipal manager or the managers directly accountable to him. Consequently, no performance reviews were performed.
- b) Councillors did not disclose their interests as required by schedule 1 section 5.
- c) The municipality did not have an approved tariff policy in place as required by section 74.

6.5.3 *Basic Conditions of Employment Act, 1997 (Act No. 75 of 1997)*

- a) An overtime agreement was not in place regulating to the approval of overtime in excess of the requirements of section 10.

6.5.4 *Local Government Transitional Act, 1993 (Act No. 209 of 1993)*

- a) Valuations of property did not take place timely as required by section 10(G)(6). The last valuations were performed in 1993.

6.6 Matters in the public interest

6.6.1 Cell phone expenditure

- b) Seven officials received the benefit of a cell phone account being paid by the municipality. No cell phone policy was in place. No council resolution was passed in this regard. The financial manager set cell phone limits on 8 May 2006. Six officials exceeded these limits. The overspending amounted to R79 763 for the financial year. No money was recouped for overspending the limits. The fringe benefit was not indicated on the IRP5s of the officials.

6.6.2 Motor allowance

- a) A motor allowance policy was approved by council during the 2004-05 financial year. Contrary to business practice, the allowance was granted to non-operational officials as well.

6.6.3 Old mayoral vehicle

- a) During the 2004-05 financial year, the mayoral vehicle became a council vehicle as the mayor received a travelling allowance. No trip authorisation forms or log book were maintained for the vehicle. Repair cost of R9 697 was incurred during the year. The vehicle, with a book value of approximately R80 000 at year-end, was seldom utilised as it was mechanically out of order for the most part of the year.

6.6.4 Douglas show grounds

- a) Uncertainty existed whether the Douglas show grounds was the property of the Siyancuma Municipality. Outstanding rates and services amounted to R118 114 at 30 June 2006. Various non-municipal activities were noted at the show grounds. No agreements were in place for any such activities and no related income was recognised in the municipal accounting records.

6.6.5 Rental fringe benefit

- a) Two senior officials rented a municipal house at the Douglas holiday resort at a 60% discounted rental amount. This taxable fringe benefit has not been taken into account in the remuneration of the officials. This also constituted non-compliance with the Income Tax Act, 1993 (Act No. 113 of 1993), paragraphs 2(d) and 9 of schedule 7. Outstanding rental from the officials at 30 June 2006 amounted to R38 234. These debtors have not been recognised in the accounting records of the municipality.

6.6.6 Financial management system

- a) The municipality paid approximately R225 000 to consultants for financial management system related expenses. No service level agreements existed with the consultants. Various training was provided by the consultants. Based on the recurring training charges it is questionable whether transfer of skills took place.

6.7 Performance management system

- a) A performance management system was not yet fully implemented and the council did not comply with all the requirements as set out in chapter 6 of the Municipal Systems Act, 2000 (Act No. 32 of 2000) and the performance measurement regulations. No performance report was submitted for audit purposes. Refer to the audit report issued "*Report of the Auditor-General to the Siyancuma council on factual findings on performance measurement at Siyancuma Municipality for the year ended 30 June 2006*" for more detail.

6.8 Late finalisation of the audit report

- a) 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 15 December 2006 where the financial statement in question were received by 31 August 2006.

7. APPRECIATION

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

A L Kimmie *for* Auditor-General

Kimberley

11 December 2006



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