

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

1. AUDIT ASSIGNMENT

The financial statements as set out on pages ... to ..., 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 (Act No. 108 of 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 municipal manager. My responsibility is to express an opinion on these financial statements, based on the audit.

2. NATURE AND 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, and
- evaluating the overall financial statement presentation.

Furthermore, an audit includes an examination, on a test basis, of evidence supporting compliance in all material respects with the relevant laws and regulations, which came to my attention and are applicable to financial matters.

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 paragraph 1.1 of the accounting policies to the financial statements.

4. QUALIFICATION

4.1 Opening balances

4.1.1 As reported in the prior year, a disclaimer of audit opinion was issued. During the year under review no corrective measures were implemented by management on qualifications reported. As a result I am unable to verify the opening balances other than agreeing them to the prior year financial statements.

4.1.2 An adjustment of R6 955 598 consisting of unallocated credits was incorrectly credited against the prior year adjustment (Appropriations) of R13 320 789 as reflected in note 18 to the financial statements.

4.2 Accounting presentation of financial statements

The entity-specific basis of accounting is inadequately disclosed in the financial statements in respect of the accounting policies for the following material transactions, balances, events or conditions:

The treatment of the proceeds realised on the disposal of fixed assets.

4.3 Fixed assets

Following the altered jurisdiction area of the municipality in terms of Provincial Notice 322 of 2000 (Provincial Gazette 5574 dated 29 September 2000), assets and liabilities to be transferred to the Bophirima District Municipality were removed from the accounting records of the Southern District Municipality. Since the MEC responsible for local government in the province has not yet made a determination regarding the transfer of these assets and the corresponding liabilities as required by section 7 of the aforementioned proclamation, assets are understated by R28 672 401, whilst long-term liabilities, which include arrear instalments and interest, are understated by R42 535 580.

4.4 Debtors

4.4.1 In the absence of supporting evidence by management to establish an appropriate provision for bad debts and using alternative audit procedures based on our estimates applying the existing accounting policy and identifying long outstanding doubtful debtors, the provision for bad debt as disclosed in note 12 to the financial statements appear to be understated by R1 620 675.

4.4.2 An unreconciled difference of R489 588 was identified between the debtors listing of R8 035 344 and the current debtors (levies) amounting to R7 545 756 as disclosed in note 10 to the financial statements.

4.4.3 No supporting documentation or reconciliations could be provided for VAT suspense accounts of R898 428, classified as debtors and disclosed as part of suspense accounts under note 10 to the financial statements.

4.5 Creditors

4.5.1 Unallocated credits of R1 544 323 was found to be understated by R886 857. Furthermore, appropriate audit evidence to support transactions of R234 968 (debit) included in suspense account creditors of R5 068 569 as per note 13 to the financial statements, could not be provided for audit.

4.5.2 Retention monies of R4 382 470 as per note 13 to the financial statements are understated with VAT of R613 546.

4.6 Provision for leave

In the absence of proper leave records, I am unable to express an opinion on the adequacy of the leave provision of R571 780 as disclosed in note 12 to the financial statements.

4.7 Revenue

4.7.1 No revenue reconciliations for bulk levies could be provided for audit, whilst all monthly bulk levy charges for Maquassi Hills, Ventersdorp and Potchefstroom municipalities were not accounted for. Bulk supply levy revenue of R1 953 978 as disclosed in Annexure D to the financial statements is therefore materially understated.

4.7.2 Regional services levies of R18 747 762 as disclosed in Annexure D is understated by R5 833 773, being unallocated receipts incorrectly allocated to the appropriation account.

4.8 Salaries and wages

Unreconciled differences of R1 842 439 between the payroll and the general ledger were found during the audit.

4.9 Expenditure

Supporting evidence to evaluate legal expenses of R965 189 incurred by the council on behalf of the previous Executive Mayor could not be provided for audit. Furthermore, supporting documentation for expenditure of R200 000 could not be submitted for audit purposes.

4.10 Unauthorised expenditure

4.10.1 Expenditure not budgeted for of R10 643 887 incurred during the year under review, was allocated to the general ledger account unauthorised expenditure. This expenditure was however not dealt with as required by section 32 of the MFMA nor was it disclosed as unauthorised expenditure in the financial statements.

5. DISCLAIMER OF AUDIT 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 Financial statements: Presentation and disclosure

6.1.1 The interest rate payable on long-term liabilities as disclosed in note 4 to the financial statements is incorrectly stated as 10% for all liabilities, whilst a variety of individual rates apply to the various loans.

6.1.2 The notes to the financial statements do not disclose each bank account held by the municipality during the financial year and the required information regarding these bank accounts.

6.1.3 Allowances and benefits of section 57 employees have not been disclosed, as required.

6.1.4 A summary of all investments of the municipality as at year-end is not disclosed as required.

6.1.5 Credit card debt of R89 624 owed by councillors is not disclosed as required.

6.1.6 Details explaining the reasons for significant prior year adjustments of R13 320 789 against appropriations, are not explained in note 18 to the financial statements.

6.2 Fruitless and wasteful expenditure

Notwithstanding having reported on serious irregularities regarding entertainment expenses of councillors and officials over the past 3 financial years, the matters have still not been addressed and the following discrepancies were again found in entertainment expenses of R210 565 (R67 974 in 2005) incurred for the year under review:

- (a) Council did not have a formal policy regulating entertainment expenses and credit cards.
- (b) No supporting documentation was submitted by the users of these cards. Expenditure was paid without ensuring that expenses were actual, reasonable and incurred for official purposes.
- (c) Various purchases were made at grocery shops, liquor stores and on Saturdays and Sundays and as no supporting documentation was attached, the validity of this expenditure could not be satisfactorily tested.

6.3 Weaknesses in internal control

The following are some of the more material weaknesses found during the audit:

- (a) The supply chain management policy of the council was not complied with in the appointment of PEM Developers as proper tender procedures were not followed.
- (b) Not all policies and procedures are in place.
- (c) Key positions in the finance department are vacant. No proper segregation of duties is therefore in place, resulting in an inadequate internal control environment.
- (d) Contrary to the council's policy and procedures, overtime in excess of 30% of monthly salaries have been paid to certain officials.

6.4 Non-compliance with laws and regulations

6.4.1 Income Tax Act, 1962 (Act No. 58 of 1962) and Value-added Tax Act, 1991 (Act No. 89 of 1991):

- PAYE was incorrectly deducted from travel claims reimbursed to employees.
- Contrary to section 17(2)(c) of the VAT Act, input VAT on motor vehicles amounting to R132 607 was incorrectly claimed.

6.4.2 Municipal Systems Act, 2000 (Act No. 32 of 2000):

- Section 57(1)(b) - An annual performance evaluation of the municipal manager and all senior managers was not done for the year under review.
- Section 67 - The HR policies and procedures, particularly the monitoring, measuring and evaluating of performance of staff, were not implemented in accordance with applicable laws.

6.4.3 Municipal Finance Management Act, 2003 (Act No. 56 of 2003):

- Contrary to section 28, the Mayor did not table an adjustments budget. Significant changes to the budget were authorised during the year.
- Contrary to section 30, the municipality does not have a risk management plan, internal audit plan and no risk assessment was done.
- Contrary to section 52(d), the mayor did not submit a report to the council on the implementation of the budget and the financial state of affairs of the municipality.
- Contrary to section 66, the accounting officer did not report to the council on all expenditure incurred by the municipality on staff salaries, wages, allowances and benefits, in a manner which disclose such expenditure by type of expenditure.
- Contrary to section 69(1), the accounting officer in demonstrating responsibility for implementing the municipality's budget, had not taken all reasonable steps to ensure that the spending of funds had been in accordance with the budget and that expenditure had been properly monitored.
- Contrary to section 127(2), council did not table the annual report for the 2004/2005 financial year within seven months after year-end.
- Contrary to section 129, council has to date of this report not yet adopted an oversight report containing the council's comments on the annual report.
- Contrary to section 131, council has to date of this report not yet addressed the issues raised in the Auditor-General Report for the 2004/05 financial year.
- Contrary to section 133(1)(a), the Executive Mayor did not submit to the council a written explanation setting out the reasons for the delay in submitting to the council of the municipality the 2004/2005 annual report within 7 months after the end of the previous financial year.

6.4.4 Supply Chain Regulations:

- Regulation 2(1) - the maximum 20 points were not awarded for specific goals for contracts with a rand value below the prescribed amount (R1 Million), provided that the lowest acceptable tender scores 80 points for price.
- Regulation 6 - a report by the accounting officer on the implementation of the supply chain management policy for the year under review, has not been submitted to the council.
- Regulation 7 - the municipality has not yet established a supply chain management unit to implement a supply chain management policy.
- Regulations 21-25 - the bidding processes followed were not in terms of the supply chain management policies.
- Regulation 26-29 - evidence that the council provided for a committee system, could not be submitted for audit.

6.5 Computer information systems review

Based on my review, proper Information Technology (IT) governance structures which include policies, procedures, defined IT processes, proper IT strategic plan and staffing to support and properly monitor the IT functions are not in place.

7. APPRECIATION

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

ND Maphiri *for* Auditor-General

Rustenburg

30/11/2006



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