

REPORT OF THE AUDITOR-GENERAL TO THE EASTERN CAPE PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF THE SUNDAYS RIVER VALLEY MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2009

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the accompanying financial statements of the Sundays River Valley Municipality which comprise the statement of financial position as at 30 June 2009, statement of changes in net assets, cash flow statement and statement of financial performance for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages x to xx.

The accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the basis of accounting determined by the National Treasury: Statements of Generally Recognised Accounting Practice (Statements of GRAP) and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA).

The Auditor-General's responsibility

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the International Standards on Auditing and *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008*. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer of opinion

Accumulated deficit

4. I was unable to obtain supporting documentation for the restatement of the surplus of R3,16 million in the prior year financial statements to R2,57 million in the current year financial statements. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required for the restated prior year net surplus of R2,57 million.
5. The corrections for the prior year errors of R582,688 per note 21 to the financial statements differs to the actual restatement of R584,493 reflected in the net surplus for the prior year by R1,805.

Short term portion of long term liabilities

6. The scope of our audit was restricted as I was unable to obtain the supporting documentation necessary to re-perform the calculation of the short term portion of long term liabilities of R650,709 per note 3 to the financial statements.
7. The short term portion of long term liabilities of R650,709 on the face of the statement of financial position differs to the present value of the minimum lease payments of R541,043 and R941,264 reflected as current liabilities in note 3 to the financial statements. Consequently, I was unable to confirm or verify by alternative means whether the long term liabilities of R4.66 million and the short term portion of R650,709 are presented correctly.

Current and non-current provisions

8. I was unable to determine whether any adjustments were required to the provisions for landfill rehabilitation of R3,45 million, long service bonus of R110,327 and staff bonuses R787,140 per notes 4 and 6 to the financial statements as key municipal employees were not available to provide supporting documentation.
9. The provisions have not been recorded at the present value of the expenditures expected to settle the obligation, as required by GRAP 19: Provisions, contingent liabilities and contingent assets. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to the provision of R4,35 million.
10. A provision has not been recorded and as a result provisions and the related expenditure are understated by R750,000.

Trade and other payables

11. The scope of our audit was restricted as I was unable to obtain the supporting documentation necessary to recalculate the leave pay accrual of R2,35 million per note 5 to the financial statements. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to the leave pay accrual of R2,35 million.
12. The current year audit fee per note 27 to the financial statements has been understated by R1,50 million and as a result accrued expenditure is also understated by R1,50 million.
13. The scope of our audit was restricted as I was unable to obtain, the supporting documentation for payments made subsequent to year end of R12,11 million; supporting documentation for R41,20 million of trade creditors; or reasons for large and unusual movements in order to determine whether any adjustments were required to trade creditors of R43,05 million per note 5 to the financial statements.

Unspent grants and subsidies

14. Funds allocated to specific projects are transferred to other funds on a temporary basis to fulfill cash flow needs. When these transfers are made, the unspent grant and subsidies liability account for that project is debited with the withdrawal and the unspent grant and subsidies liability account of the receiving project is credited. This is not correct as the movement is not in line with the fulfillment of conditions. As a result of the inadequate record keeping in relation to the monitoring of conditional grants and subsidies movements and the errors identified in the opening balances, I was unable to perform the audit procedures deemed necessary to determine whether any adjustments were required to the debit balance in unspent grants and subsidies of R21,82 million as per note 10 to the financial statements and the unspent grants and subsidies liability of R19,19 million as per note 12 to the financial statements, as well as whether any adjustments were required to the resulting movements in the income statements (R116,16 million expenses per note 19 to the financial statements and R114,00 million revenue per note 13 to the financial statements).
15. Appendix F (schedule of conditional grants and receipts) has not been included in the annual financial statements to assist with reconciling the movements in the statement of financial position to the movements in the statement of financial performance.
16. As a result of the above limitations to the scope of my audit, I was also unable to determine the financial impact on the closing balances of the government grant reserve of R71,46 million and accumulated deficit of R25,90 million as reflected in the statement of changes in net assets.
17. Grant agreements were not provided for audit purposes and the municipality's records did not permit the application of alternative audit procedures. I was unable to confirm or verify by alternative means whether the expenditures incurred of R116,16 million per note 19 to the financial statements were in terms of the agreement.

18. As a result of the above limitations to the scope of my audit, I was unable to determine whether the agreements required separate investment accounts be maintained in respect of unspent conditional grants, however, liabilities for grants are R19,19 million per note 12 to the financial statements and investments are only R12,51 million per note 11.5 to the financial statements thus there is a shortfall of R6,68 million.

Property, plant and equipment

19. Finance lease assets of R2,26 million have been reflected as one line item on the asset register which is contravention with GRAP 17: Property, plant and equipment, which requires that each component be accounted for separately when the component assets have different useful lives or provide benefits to the entity in a different pattern.
20. I was unable to determine whether items of land and buildings of R22,78 million should be treated as investment property in accordance with GRAP 16: Investment property which requires that property (land or a building) held to earn rentals or for capital appreciation or both, be classified as investment property.
21. The rights to land of R950,070 could not be confirmed as a result of the land not being registered in the municipality's name. The municipality could not provide a list of possible names that all the land could have been registered in and thus alternative audit procedures could not be applied over the remainder population with a cost of R5,05 million. Consequently, I was unable to confirm or verify by alternative means the municipality's rights to land reflected at a total cost of R6,00 million per note 7 to the financial statements.
22. Certain assets could not be located in the register. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to property, plant and equipment with a carrying amount of R81,69 million per note 7 to the financial statements.
23. I was unable to physically inspect items of property, plant and equipment with a cost of R86,50 million and leasing assets with a cost of R2,00 million due to a lack of availability of key municipal employees. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to property, plant and equipment reflected at a carrying amount of R81,69 million.
24. Residual values have been determined based on a generalized percentage-of-cost formula (other than certain infrastructure assets) which is not appropriate as there was no consideration of what the asset could reasonably be sold for in the same condition at the end of its life in terms of GRAP 17: Property, plant and equipment. I was unable to confirm or verify by alternative means the financial impact on the closing accumulated depreciation of R32,87 million per note 7 to the financial statements and the depreciation expense of R3,12 million per the statement of financial performance.
25. The scope of our audit was restricted as I was unable to obtain the supporting documentation for additions to property, plant and equipment of R2,90 million. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to the additions for the year of R17,58 million as reflected in Appendix B to the financial statements.
26. Items claimed from insurance with a settlement value of R190,223 could not be identified on the fixed asset register to confirm that the disposal had been recorded. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to the depreciation expense of R3,12 million, profit or loss on disposals of Rnil per the statement of financial performance and the carrying amount of R81,69 million per note 7 to the financial statements.

27. The depreciation expense has been overstated by R608,192 due to the fact that management revised the residual values and did not update the formulas on the fixed asset registers appropriately to take this into account. There also appear to be assets still in use that are nearing a nil book value for which the useful lives were not reassessed and adjusted accordingly. In addition to this, assets were over depreciated to below net book values of zero by R10,129 and residual values by R86,890. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to the depreciation expense of R3,12 million per the statement of financial performance.
28. Property, plant and equipment of R588,081 were capitalised in the current year but related to purchases in the prior year. Consequently, I was unable to confirm or verify by alternative means that additions of R17,58 million per appendix B were recorded in the correct period.
29. As a result of the above findings I was unable to confirm that the fixed asset register contains adequate details to support the balances in the government grant reserve, public contributions and donations reserve and the capitalisation reserves closing balance and movements for the year per the statement of changes in net assets.

Receivables

30. Salaries, travel allowances and cell phone allowances of R687,651 included in income accrued of R3,52 million per note 10 to the financial statements were overpaid to councillors and the mayor in 2005/06. In terms of section 164(1)(c) of the MFMA, loans to councillors are forbidden and it appears that no attempt has been made to recover the expenditure as required by section 167 2(a) and (b) of the MFMA and no provision for write-off has been made against this. The scope of our audit was also restricted as I was unable to obtain supporting documentation relating to the remainder of income accrued amounting to R2,83 million. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to income accrued of R3,52 million in note 10 to the financial statements.
31. I was unable to obtain the trade receivables age-analysis that would allow selections to be made from each category of ageing. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to trade receivables of R44,04 million per note 10 to the financial statements.
32. The scope of our audit was restricted as I was unable to obtain supporting documentation for other debtors of R448,391 per note 10 of the financial statements. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to other debtors of R448,391 per note 10 to the financial statements.
33. The scope of our audit was restricted as I was unable to determine whether trade and other receivables were recorded in the correct period or obtain explanations for non-routine journals. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to trade and other receivables of R30,09 million per the statement of financial position.

Cash and cash equivalents

34. The scope of our audit was restricted as I was unable to obtain the supporting documentation for bank reconciling items of R140,642 and due to errors in the bank reconciliation general expenses and trade payables were overstated by R27,345 (as the reconciling items were reclassified from bank and cash to trade creditors at year end). Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to reconciling items of R984,091 included in trade creditors of R43,04 million per note 5 to the financial statements.

Investments

35. Investments per note 11.5 to the financial statements were overstated and unspent conditional grant liabilities per note 12 understated by R414,060 when compared to the investment certificates.

Revenue

36. The scope of our audit was restricted as I was unable to obtain explanations for comparisons to budget, ratio analysis (for example the margin on bulk purchases of electricity has decreased substantially in comparison to prior year, refer to note 10 and 18 to the financial statements), non-routine journal entries and large and unusual entries for the revenue. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to revenue of R193,62 million per the statement of financial performance.
37. The scope of our audit was restricted as I was unable to determine whether whether any adjustments were required to penalty interest of R14,986 per the statement of financial performance.
38. The scope of our audit was restricted as I was unable to reconcile the equitable share according to schedule 3 of R15,64 million, the municipal infrastructure grant of R9,23 million in terms of schedule 4, the finance management grant of R2,50 million in terms of schedule 6 and the integrated NER program grant of R665,000 in terms of schedule 7 of the DoRA as published in Government Gazette 31708 to the amount received into the main bank account and to the revenue disclosed in the note 13 of the financial statements. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to revenue of R24,90 million (total government grants received excluding housing revenue recognised of R114,00 million).
39. I was unable to inspect supporting documentation for expenditure of R116,16 million incurred on the conditional grants and R3,95 million incurred on the financial management grants and accordingly whether the conditions of the grant have been met in order for the revenue of R114,00 million and R3,95 million respectively per note 13 to the financial statements to be recognised (refer further to paragraph 51).
40. A reconciliation between the valuation roles and rates charged in support of the property rates revenue of R6,76 million per the statement of financial performance was not performed. Municipal employees were also not available to provide evidence that interim valuations were adequately and timeously effected in the accounting system. Consequently, I was unable to confirm or verify by alternative whether any adjustments were required to the property rates revenue of R6,76 million per the statement of financial performance.
41. The scope of our audit was restricted as I was unable to obtain source documentation for traffic fines income. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to traffic fines income of R1,27 million per the statement of financial performance.
42. The scope of our audit was restricted as I was unable to obtain reasons why some meter readings were reflecting nil consumptions. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to water service charges of R6,21 million disclosed in note 10 to the financial statements.
43. The scope of our audit was restricted as I was unable to obtain source documentation for licences and permits revenue. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to licences and permits revenue of R4,63 million per the statement of financial performance.
44. The scope of our audit was restricted as I was unable to obtain source documentation for other income of R4,52 million. Consequently, I was unable to confirm or verify by alternative whether any adjustments were required to other income of R4,52 million per the statement of financial performance.
45. The scope of our audit was restricted as I was unable to obtain source documentation to reconcile transaction listings to deposit slips, to bank statements and to the general ledger. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to total revenue of R193,62 million per the statement of financial performance.

Expenditure

46. Employee costs and councillor remuneration per the statement of financial performance of R24,70 million could not be reconciled to the salary reports of R20,70 million for the year and explanations could not be obtained for the comparisons of current year actual to prior year and to budgets. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to employee costs and councillor remuneration disclosed.
47. The scope of our audit was restricted as I was unable to obtain applications for registered indigent debtors to determine whether the indigents qualified for the subsidies received against rates, water, refuse and sewerage accounts of R1,79 million. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to grants and subsidies paid of R1,79 million per note 19 to the financial statements.
48. Opening accumulated surplus per the statement of changes in net assets and current year general expenditure has been overstated by R542,036 as a result of incorrect cut-off errors in the prior year.
49. Expenditure of R266,613 was posted to the wrong expense accounts in the general ledger. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to total expenditure disclosed of R192,32 million per the statement of financial performance.
50. The scope of our audit was restricted as I was unable to obtain source documentation for general expenditure incurred of R4,23 million. Consequently, I did not verify by alternative means whether any adjustments were required to general expenses of R15,25 million per the statement of financial performance.
51. The scope of our audit was restricted as I was unable to obtain source documentation or grant agreements for expenditure charged against conditional grants of R116,16 million and financial management grants of R3,95 million per note 19 to the financial statements. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to the above expenditures and the associated conditional grant revenue recognised of R117,95 million (R3,95 million and R114,00 million) per note 13 to the financial statements.
52. The scope of our audit was restricted as I was unable to obtain transaction listings, reconciliations and rejected transaction listings to identify items that are deemed large or unusual. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to total expenditure of R192,32 million in the statement of financial performance.
53. As a result of the high error rates identified during the execution of the 08/09 audit procedures, whether any adjustments were required to total expenditure incurred on repairs and maintenance, bulk purchases, contracted services, grants and subsidies paid and general expenditure of R146,61 million per the statement of financial performance could not be verified.

Value Added Taxation (VAT)

54. The scope of our audit was restricted as I was unable to obtain a reconciliation of the revenue declared per the monthly VAT201 forms to the recorded sales per the ledger. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to output VAT declared during the year.
55. A number of capturing errors and the incorrect accounting treatment of VAT on invoices has resulted in an understatement of expenditure and an overstatement of the VAT receivable of R119,352. Consequently, I was unable to confirm or verify by alternative means whether any adjustments were required to the VAT receivable of R4,67 million as disclosed in note 10 to the financial statements.

Cash flow statement

56. Based on the scope limitation on the various other components audited I do not express an opinion on the cash flow statement.

Disclosure

57. The nature of the estimation uncertainty for liabilities has not been disclosed in note 4 of the provision for rehabilitation of landfill sites as required by GRAP 1: Presentation of Financial Statements, paragraph 32(a).
58. Each item on the face of the statement of financial position, statement of financial performance, statement of changes in net assets and cash flow statement has not been cross referenced to the related information in the notes as required by GRAP 1: Presentation of Financial Statements, paragraph 12.
59. The amount of undrawn borrowing facilities that may be available for future operating activities and to settle capital commitments has not been disclosed in the notes as required by GRAP 2: Cash flow statements, paragraph 49.
60. Reasonable estimable information relevant to assessing the possible impact that application of the new GRAP statements that has been issued but are not yet effective has not been made (e.g. GRAP 18, 21, 23, 24, 26 and 103) as required by GRAP 3: Accounting Policies, Changes in Accounting Estimates and Errors, paragraph 30(a) and (b):
61. No disclosure has been made regarding the effect of the adoption of the new GRAP standards in the current year and no reference was made to the prior year accounting policies as required by GRAP 3: Accounting Policies, Changes in Accounting Estimates and Errors, paragraph 28.
62. Assets subject to operating leases have not been presented in the statement of financial position according to the nature of the asset as required by GRAP 13: Leases, paragraphs 68 to 72.
63. The future minimum lease payments split between 1 year, 2 to 5 years and later than 5 years, including a general description of the leasing arrangements, have not been made as required by GRAP 13: Leases paragraph 75 (a) to (c).
64. A reconciliation disclosing the carrying amount of property, plant and equipment at the beginning of the period has not been made as required by GRAP 17: Property Plant and Equipment, paragraph 82 (e) (i) to (ix).
65. The amount of compensation from third parties of R190,233 for items of property, plant and equipment that were impaired, lost or given up has not been included in surplus or deficit as required by GRAP 17: Property Plant and Equipment, paragraph 83(d).
66. The amount or nature of change for the revision to useful lives and residual values was not accounted for as a change in accounting estimate in accordance with the requirements of GRAP 3, as required by GRAP 17, paragraph 61.
67. The increase during the period in the discounted amount arising from the passage of time and the effect of any changes in the discount rate has not been disclosed separately from the addition to the provision in note 4 to the financial statements as required by GRAP 19: Provisions, Contingent Liabilities and Contingent Assets, paragraph 107(f).
68. A description of the nature of the obligation and the expected timing of any resulting outflows of economic benefits, an indication of the uncertainties about the amount of timing of those outflows, the major assumptions made concerning future events; and the amount of any expected reimbursement has not been made for the provision disclosed in note 4 to the financial statements as required by GRAP 19: Provisions, Contingent Liabilities and Contingent Assets, paragraph 108 (a) to (c).

69. Two councillors were identified as related to companies the municipality made payments to during the year (H Jantjies: Ebron building construction, R343,169 and ZA Lose: Newton Management 11, R405,420). The scope of our audit was restricted as I was unable to determine whether this met the definition of a related party per IAS 24: Related Party Disclosure and consequently, whether separate disclosure in a note to the financial statements was required.
70. The scope of our audit was restricted as I was unable to determine whether the remuneration of the key municipal employees as disclosed in note 15 as required by section 124 of the MFMA was accurate or complete.
71. Note 38 to the financial statements states that the acting Municipal Manager is Mrs Roji, however the previous Municipal Manager that was dismissed due to allegations of fraud has since been reinstated. The note should be updated as required by GRAP 14: Events after the Reporting Date.
72. The scope of our audit was restricted as I was unable to obtain supporting documentation to determine whether there were any events in the post balance sheet period. Consequently, I was unable to confirm or verify by alternative means the completeness of disclosures and adjustments to the financial statements in respect of non-adjusting and adjusting post balance sheet events and as required by GRAP 14: Events after the Reporting Date.

Journals

73. The scope of our audit was restricted as I was unable to obtain supporting journal vouchers or explanations for any of the journals selected for fraud tests and the journal sample did not balance by a net credit of R349,032. Consequently, I was unable to confirm or verify by alternative means the occurrence, valuation, existence, cut-off classification and accuracy of all the affected components in the financial statements.

Opinion

Disclaimer of opinion

74. Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements of Sundays River Valley Municipality. Accordingly, I do not express an opinion on these financial statements.

Emphasis of matter

I draw attention to the following matters:

Basis of accounting

75. The Municipality's policy in the current year is to prepare financial statements on the basis of Statements of Generally Recognised Accounting Practice (GRAP) which has been disclosed in note 1.2 of the financial statements. The prior year's basis of accounting was in accordance with the deviation approved by National Treasury in general notice 522 of 2007, issued in government gazette No. 30013 of 29 June 2007. This basis of accounting in the prior year has not been disclosed in note 1.2 to the financial statements.

Going concern

76. The municipality has an accumulated loss of R25,90 million per the statement of changes in net assets and trade creditors of R43,05 million as per note 5 to the financial statements, however the overdraft facility is only R1 million. Note 34 to the financial statements indicate that this condition, along with other matters, point to the existence of a material uncertainty that may cast significant doubt on the entity's ability to continue as a going concern.

Unauthorised, irregular or fruitless and wasteful expenditure as well as material losses through criminal conduct

77. Capital expenditure incurred of R588,081 was not included in the approved capital budget in the prior year and per Appendix E(2), capital expenditures on various other assets also exceeded the approved capital budget.
78. Actual expenditure per the statement of financial performance exceeded the budget by R143,2 million which is therefore considered unauthorised expenditure.
79. Supply Chain Management Regulations 12, 16 and 17 were not complied with for expenditure of R366,199 as a result of not obtaining the minimum number of quotes due for transaction values between R10,000 and R200,000.
80. The scope of our audit was restricted as I was unable to obtain contracts for expenses of R1,2 million in order to determine whether the requirements of the Supply chain management Regulations were met.
81. The scope of our audit was restricted as I was unable determine whether the requirements the Supply chain management Regulations 21 to 25 were met.
82. The scope of our audit was restricted as I was unable to obtain a tender register in order to determine whether the requirements of section 2(1) of the Preferential Procurement Policy framework act no. 5 of 2000 were met.
83. Insufficient authorisation was received through the approval of purchase orders for expenditure of R1,30 million which therefore constitutes irregular expenditure.
84. The scope of our audit was restricted as I was unable to obtain a schedule of penalties and interest in respect of late payments or reports submitted by the accounting officer to the mayor and MEC for Local government with regards to unauthorised, irregular, fruitless and wasteful expenditure for the year. Consequently, I was unable to confirm or verify by alternative means the completeness of the disclosures per note 24 to the financial statements.
85. A forensic report costing R279,521 was not a proper forensic investigation and a payment of R6,450 was made for damages to a rental vehicle that was used by the Municipal Manager. These expenses are considered fruitless and wasteful expenditure.
86. Employees were promoted (to positions that were frozen by the council), as part of a mentorship program for which they received a monthly acting allowance. The mentorship program had not started nor were employees performing additional duties therefore the allowances of R35,165 are seen as fruitless and wasteful expenditure.
87. The Municipal Manager was paid his full salary once he was suspended which amounted to fruitless and wasteful expenditure of approximately R130,216.
88. The unauthorised, irregular and fruitless and wasteful expenditures above have not been disclosed as such in the financial statements as required in terms of section 125 (2)(d)(i) of the MFMA. Furthermore, no attempt was made to recover the unauthorised, irregular or fruitless and wasteful expenditures as required by section 32 (2) of the MFMA nor were they authorized in an adjustments budget, or certified as irrecoverable by council in terms of section 32 (2)(b).

Restatement of corresponding figures

89. As disclosed in note 21 to the financial statements, the corresponding figures for 30 June 2008 have been restated as a result of errors discovered during the current and prior financial year.

Other matters

90. I draw attention to the following matters that relate to my responsibilities in the audit of the financial statements:

Material inconsistencies in other information included in the annual report

91. The annual report has not yet been issued therefore this could not be inspected for material inconsistencies.

Unaudited supplementary schedules

92. The supplementary information set out in Appendix C, D, E(1) and E(2) do not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

Non-compliance with applicable legislation

93. Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA)

93.1 The scope of our audit was restricted as I was unable to obtain a listing of capital projects undertaken during the year to determine whether the requirements of section 19 had been met.

93.2 The scope of our audit was restricted as I was unable to inspect correspondence between municipality and Provincial Treasury showing that the Annual Budget was submitted timeously in terms of section 24(3).

93.3 The scope of our audit was restricted as I was unable to obtain explanations why capital projects' actual expenditure exceeded the budget in terms of section 31 (refer Schedule E(2) to the financial statements).

93.4 The accounting officer was dismissed due to allegations of fraud which stemmed from fruitless and wasteful expenditure of R279,521 (refer paragraph 84 above). This is a breach of his fiduciary duty in terms of section 61(1).

93.5 The following material non-compliances with section 62 have been noted regarding the effective, efficient and transparent systems of financial risk management and internal control:

- The internal audit plan of the municipality for 2008/09 did not include an evaluation of matters relating to compliance with the MFMA, DoRA and other applicable legislation, audit of loss control and an evaluation of accounting procedures and practices;
- There was no formal risk management policy at the municipality;
- Bank reconciliations have not been signed by the senior accountant during the year;
- Criminal proceedings were not instituted against the municipal manager who is alleged to have committed an act of financial misconduct by sharing insider information with a company who tendered for a municipal contract (for a forensic investigation).
- No documented policies and procedures appear to exist in respect of salaries and wages such as the telephone allowance, rules regarding when payments to employees can be made through the creditors system and the municipality does not have a skills retention plan or recruitment policy;
- Leave forms currently being used at the Municipality are not pre-numbered or carbonized nor are attendance registers being maintained; and
- Numerous instances were identified where supporting documentation was not available for inspection (section 62(1)(b) of the MFMA therefore not met), weaknesses were identified in the systems of internal control (section 62(1)(c)(i) of the MFMA therefore not met) and irregular or fruitless and wasteful expenditure (section 62(d) of the MFMA not met) was identified.

- 93.6 The following material non-compliances with section 63 of the MFMA have been noted regarding the maintenance and safeguarding of assets:
- The entity does not reconcile water that has been dispersed from reservoirs to the water that has been billed in order to ensure that the amount of water wastage is less than the expected 30%. In addition there are no policies and procedures to address reticulation losses;
 - Fixed asset additions are not recorded in a timely manner as this is only done at year end. The depreciation calculation is also only performed at year end and not monthly;
 - The reconciliation of the fixed asset register to the general ledger was only performed after the physical asset verification was performed at year end and not on a monthly basis;
 - General ledger investment accounts are not being reconciled to investment certificates from the bank on a monthly basis;
 - Certain journals had not been reviewed or authorised by the Senior Accountant nor were the journals sequentially numbered; and
 - Investment accounts are not being reconciled to the respective unspent conditional grant liability accounts on a monthly basis.
- 93.7 The following material non-compliances with section 64 of the MFMA have been noted regarding the system of internal control in respect of debtors and revenue:
- Mail is opened by one person and there is no independent review to see that these cheques/cash entered into the mail register are being timeously banked;
 - Interest rates input into the system for the purposes of calculating interest on long outstanding debtors are not being checked for accuracy, or that the rate is being input timeously; and
 - No master file amendment controls are in place for amendments made to the customer master file and there is no reconciliation of the valuation roll input into the system back to the authorised valuation roll received from the valutors.
- 93.8 The following material non-compliances with section 65 of the MFMA have been noted regarding the system of internal control in respect of creditors and payments:
- There is no subsistence and travel policy;
 - Reconciliations are not performed between supplier statement balance and the balance per the creditors control account;
 - Invoices are not stamped as paid to prevent re-submission for payment;
 - The Supply Chain Management Policy doesn't contain any provisions stating that payments should be made to suppliers within 30 days of invoice date and how this should be monitored or enforced;
 - No master file amendment controls are in place for amendments made to the payroll master file.
 - The payroll was not reconciled to the general ledger for July 2008 to January 2009.
- 93.9 Section 73 has not been met as Kirkwood residents protested against poor service delivery due to incomplete low cost housing earlier in the year.
- 93.10 Section 115 has not been complied with because the fraud prevention plan has not been implemented in the 2008/09 financial year.
- 93.11 Management did not adjust for errors noted during substantive testing therefore the financial statements may not have been presented fairly in terms of section 122.

- 93.12 The notes to the annual financial statements of a municipality must include particulars of any arrears owed by individual councilors to the municipality for rates or services and which at any time during the relevant financial year were outstanding for more than 90 days, including the names of those councilors in terms of section 124(b). This was not complied with as the councilors were in arrears (30 days and over) by R29,736 at the end of June 2009.
- 93.13 The scope of our audit was restricted as I was unable to inspect correspondence to determine whether the municipality had submitted the annual report to the provincial treasury, National Treasury and the provincial department responsible for local government containing matters in terms of section 127, 129 and 130.
- 93.14 The scope of our audit was restricted as I was unable to determine whether the municipality addressed all issues raised in the previous audit report in terms of section 131(1) (refer to disclaimers raised in the current year audit report).
- 93.15 The scope of our audit was restricted as I was unable to inspect all relevant correspondence between the municipality and provincial legislature to determine whether the accounting officer submitted reports to the provincial legislature within seven days after the municipal council has adopted the relevant oversight report in terms of section 132(1) and (2).
- 93.16 A follow up of the findings of the internal audit from 07/08 and the audit of performance management as required by section 165(2)(b) was not performed.
94. Municipal Property Rates Act No 6, 2004
- 94.1 The municipality has not prepared a property register that is divided into 2 parts (A and B) as stipulated by the Municipal property rates act paragraph 23(1).
95. Environment Conservation Act No 73 of 1989
- 95.1 The scope of our audit was restricted as I was unable to obtain a schedule of waste disposal sites used to dump refuse and inspect permits for each waste disposal site to determine whether the conditions attached to the issuance of the permits are being complied with.

Governance framework

96. The governance principles that impact the auditor's opinion on the financial statements are related to the responsibilities and practices exercised by the accounting officer and executive management and are reflected in the internal control deficiencies and key governance responsibilities addressed below:

Internal control deficiencies

97. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the Municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes that gave rise to the deficiencies in the system of internal control, which led to the disclaimer of opinion. The root causes are categorised according to the five components of an effective system of internal control. (The number listed per component can be followed with the legend below the table.) In some instances deficiencies exist in more than one internal control component.

Par. no.	Basis for disclaimer of opinion	CE	RA	CA	IC	M
4,5	Accumulated deficit	5				
6,7	Short term portion of long term liabilities	1				
8,9,10	Current and non current provisions	5				

11,12,13	Trade and other payables	5				
14	Unspent grants and subsidies			5		
15,16,17,18	Unspent grants and subsidies	5				
19,21,22,26,28	Property, plant and equipment				1	
20,25,29	Property, plant and equipment	5				
24	Property, plant and equipment	7				
27	Property, plant and equipment	7				
30,31,32,33	Receivables	5				
34	Cash and cash equivalents	5				
35	Investments	5				
36,37,38,39, 41,42,43,44,45	Revenue	5				
40	Revenue			3		
46,47,50,51, 52,53	Expenditure	5				

48,49	Expenditure			5		
54	Value Added taxation (VAT)	5				
55	Value Added taxation (VAT)			5		
56	Cash Flow Statement	5				
57,58,59,60, 61,62,63,64, 65,66,67,68, 69	Disclosure	7				
70,71,72	Disclosure	5				
73	Journal	5				

98. There is a lack of good corporate governance at the municipality as there is political interference from the councillors which leads to situations where the best interests of the municipality are not always considered. At times this affects the ability of the municipality to provide basic services. The Chief Financial Officer was not available to assist with providing source documentation or explanations as from the 24th of September therefore a number of the audit procedures could not be completed. Consequently the majority of the root causes for the qualifications are as a result of the accounting officer/accounting authority not exercising oversight responsibility over financial reporting and internal control.

Legend	
CE = Control environment	
The organisational structure does not address areas of responsibility and lines of reporting to support effective control over financial reporting.	1
Management and staff are not assigned appropriate levels of authority and responsibility to facilitate control over financial reporting.	2
Human resource policies do not facilitate effective recruitment and training, disciplining and supervision of personnel.	3
Integrity and ethical values have not been developed and are not understood to set the	4

standard for financial reporting.	
The accounting officer/accounting authority does not exercise oversight responsibility over financial reporting and internal control.	5
Management's philosophy and operating style do not promote effective control over financial reporting.	6
The entity does not have individuals competent in financial reporting and related matters.	7
RA = Risk assessment	
Management has not specified financial reporting objectives to enable the identification of risks to reliable financial reporting.	1
The entity does not identify risks to the achievement of financial reporting objectives.	2
The entity does not analyse the likelihood and impact of the risks identified.	3
The entity does not determine a risk strategy/action plan to manage identified risks.	4
The potential for material misstatement due to fraud is not considered.	5
CA = Control activities	
There is inadequate segregation of duties to prevent fraudulent data and asset misappropriation.	1
General information technology controls have not been designed to maintain the integrity of the information system and the security of the data.	2
Manual or automated controls are not designed to ensure that the transactions have occurred, are authorised, and are completely and accurately processed.	3
Actions are not taken to address risks to the achievement of financial reporting objectives.	4
Control activities are not selected and developed to mitigate risks over financial reporting.	5
Policies and procedures related to financial reporting are not established and communicated.	6
Realistic targets are not set for financial performance measures, which are in turn not linked to an effective reward system.	7
IC = Information and communication	
Pertinent information is not identified and captured in a form and time frame to support financial reporting.	1
Information required to implement internal control is not available to personnel to enable internal control responsibilities.	2
Communications do not enable and support the understanding and execution of internal control processes and responsibilities by personnel.	3
M = Monitoring	
Ongoing monitoring and supervision are not undertaken to enable an assessment of the effectiveness of internal control over financial reporting.	1
Neither reviews by internal audit or the audit committee nor self -assessments are evident.	2
Internal control deficiencies are not identified and communicated in a timely manner to allow for corrective action to be taken.	3

Key governance responsibilities

99. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of key governance responsibilities, which I have assessed as follows:

No.	Matter	Y	N
Clear trail of supporting documentation that is easily available and provided in a timely manner			
1.	No significant difficulties were experienced during the audit concerning delays or the availability of requested information.		X
Quality of financial statements and related management information			
2.	The financial statements were not subject to any material amendments resulting from the audit.	X	
3.	The annual report was submitted for consideration prior to the tabling of the auditor's report.		X
Timeliness of financial statements and management information			
4.	The annual financial statements were submitted for auditing as per the	X	

No.	Matter	Y	N
	legislated deadlines section 126 of the MFMA.		
Availability of key officials during audit			
5.	Key officials were available throughout the audit process.		X
Development and compliance with risk management, effective internal control and governance practices			
6.	Audit committee		
	<ul style="list-style-type: none"> The Municipality had an audit committee in operation throughout the financial year. 	X	
	<ul style="list-style-type: none"> The audit committee operates in accordance with approved, written terms of reference. 	X	
	<ul style="list-style-type: none"> The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA. 		X
7.	Internal audit		
	<ul style="list-style-type: none"> The Municipality had an internal audit function in operation throughout the financial year. 	X	
	<ul style="list-style-type: none"> The internal audit function operates in terms of an approved internal audit plan. 		X
	<ul style="list-style-type: none"> The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA. 		X
8.	There are no significant deficiencies in the design and implementation of internal control in respect of financial and risk management.		X
9.	There are no significant deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations.		X
10.	The information systems were appropriate to facilitate the preparation of the financial statements.		X

11.	A risk assessment was conducted on a regular basis and a risk management strategy, which includes a fraud prevention plan, is documented and used as set out in section 95(c)(i) of the MFMA.		X
12.	Delegations of responsibility are in place, as set out in section 106 of the MFMA.		X

Follow-up audit findings

13.	The prior year audit findings have been substantially addressed.		X
14.	SCOPA/Oversight resolutions have been substantially implemented.		X

Issues relating to the reporting of performance information

15.	The information systems were appropriate to facilitate the preparation of a performance report that is accurate and complete.		X
16.	Adequate control processes and procedures are designed and implemented to ensure the accuracy and completeness of reported performance information.		X
17.	A strategic plan was prepared and approved for the financial year under review for purposes of monitoring the performance in relation to the budget and delivery by the Sundays River Valley Municipality against its mandate, predetermined objectives, outputs, indicators and targets in terms of section 87 of the MFMA.		X
18.	There is a functioning performance management system and performance bonuses are only paid after proper assessment and approval by those charged with governance.		X

Investigations

100. Quotes obtained for expenses of R514,330 appear invalid as the letterhead formats for the same suppliers have been interchanged, the addresses differ, the signatures are not consistent and the quotes from the various suppliers appear to have been printed from the same greyscale printer. There is therefore a possibility that the requirements of the supply chain management policy have been deliberately circumvented (due to fraud) and I also cannot rule out the possibility that the staff members are receiving kickbacks from suppliers. Based on these findings I recommend that a forensic investigation be undertaken.
101. Irregularities have been reported regarding tender procedures that were not followed on various housing projects. In addition it appears that supply chain management procedures with regard to payments on these projects were also not followed. I cannot rule out the possibility of fraud but was unable to determine the full extent of the irregularities taking place as this is beyond the scope of a normal audit. A forensic investigation has been undertaken by KPMG, however at the time of our audit, this report has not been finalised. Payments were made during the year of R81,00 million on various housing projects.

Report on performance information

102. I was engaged to review the performance information.

The accounting officer's responsibility for the performance information for municipalities

103. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality, prepared by the municipality in terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

The Auditor-General's responsibility

104. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008* and read in conjunction with section 45 of the Municipal Systems Act, No. 32 of 2000.
105. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.
106. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

Audit findings (performance information)kjhhh

Non-compliance with regulatory requirements

No reporting on performance information

107. Performance reports on municipality performance have not been prepared for the 2008/2009 financial year and therefore have also not been included in the annual financial statements or annual report as required by section 46(1) and (2) of the Municipal Systems Act.
108. Section 45(1)(c) of the Municipal Systems Act was not complied with as no internal auditing procedures were performed during the 2008/9 financial year with regards to performance measurement.

Lack of adoption or implementation of a performance management system

109. Section 55(1) and 38 of the MSA was not complied with as no performance management system exists.

No mid-year budget and performance assessments

110. Section 72 of the MFMA was not complied with as the report did not assess the performance of the municipality during the first half of the financial year (by 25 January) taking into account the past year's annual report and progress on resolving problems identified in the annual report.

Content of strategic performance plan

111. Section 26 of the MSA was not complied with as the integrated development plan did not reflect the key performance indicators and performance targets.

Inadequate quarterly reporting on performance information

112. The SDBIP was not completed for the last two quarters of the 2008/9 year therefore section 53 (c) of the MFMA was not complied with.

Appreciation

114. The assistance rendered by the staff of the Sundays River Valley Municipality during the audit is sincerely appreciated.

Port Elizabeth

30 November 2009



AUDITOR - GENERAL
SOUTH AFRICA

