

REPORT OF THE AUDITOR-GENERAL TO THE PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF NXUBA 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 Nxuba Municipality which comprise the balance sheet as at 30 June 2009, the income statement, and the cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, and the accounting officer's report, as set out on pages ... to

The accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation of these financial statements in accordance with the entity specific basis of accounting as determined by National Treasury as set out in Accounting Policy note 1 and in the manner required by the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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) and Section 126 (3) of the MFMA, 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, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer of opinion

Change in operating system

4. The municipality changed operating systems from Promun to Venus during the year under review. During this process journals to the value of R7.1 million were passed in order to reconcile and balance the two respective systems. Adequate and relevant supporting documentation for these journals could not be produced for audit purposes and thus the validity of the transactions could not be verified. Due to the lack of sufficient and appropriate audit evidence as well as the pervasive nature of these journals, the overall effect on the financial statements could not be determined and the misstatement is unknown.

Journals

5. The municipality contracted consultants to prepare the financial statements for the period under review. During the compilation process journal entries to the value of R71.8 million (debit) and R76.1 million (credit) were recommended by the consultants for processing by the municipality in order to balance the trial balance to the financial statements. Sufficient and appropriate audit evidence could not be obtained to substantiate the journals. In addition, the actual journals processed by the municipality amounted to R83 million and not the recommended amounts of R76.1 million 71.8 million respectively. The reason for this difference could not be explained and the overall effect of the misstatement of the financial statements is unknown as adequate supporting documentation was not available.

Suspense accounts

6. Although accounting records reflects suspense accounts to the value of R11.2 million (debit) and R11 million (credit), these balances are not reflected in the financial statements. In addition, the information recorded in the general ledger was not sufficient to identify the nature of the transactions and accounts. As alternative procedures could not be performed to verify these balances, significant uncertainty exists around the reasonableness of creditors, debtors, revenue and expenditure.

Statutory funds

7. During the period under review, no contribution was made to the revolving fund as required by Ordinance 20 of 1974. As a result, the statutory fund disclosed in the balance sheet is understated by R242 193, whilst the expenditure for the year disclosed in the income statement and accumulated deficit is understated by R242 193.

Consumer deposits

8. Consumer deposits to the amount of R322 787 represent less than one percent of the amount due to the municipality for services rendered. It is evident that municipal officials did not ensure that adequate consumer deposits were obtained before services were supplied to consumers thus increasing the recovery risk of the municipality. In addition, no alternative procedures could be performed to verify this balance. As a result it was not possible to obtain sufficient appropriate evidence to conclude on consumer deposits and the related debtors.

Revenue

9. During procedures executed on the revenue component it came to light that sundry receipts of R3.9 million, received in the subsequent financial year, were included in the income statement for the period under review. As a result revenue is overstated by R3.9 million.
10. The municipality collects monies for traffic fines on behalf of the Department of Roads and Transport and in return retains a portion for commission. For the year under review, traffic income of R90 927 is included in total revenue in the income statement. However, the report from the National Transportation Information System (NATIS) reflects a balance of R956 329 that represents the commission that the municipality is entitled to recognize. The variance of R865 402 could not be explained and due to the incompleteness of the fines issued register, no alternative procedures could be performed. In addition, unpaid traffic fines are not reflected as a receivable on the annual financial statements at year end, leading to an understatement of receivables. The overall effect of the misstatement is not known as adequate supporting documentation was not available and thus leading to significant uncertainty of the completeness and disclosure of traffic related income, expenditure and accounts receivable.

11. The amount of revenue generated from the rental of one municipal facility is understated by R104 091 as the rental is not market related, escalation clauses are not included and no updated lease agreement exists. Five municipal facilities are leased, of which rental is only charged on one facility. The overall effect of the misstatement is unknown as adequate supporting documentation was not available.
12. The municipality has used a standard rate of 13.5% to calculate interest on outstanding debts and the said interest is disclosed as R1 million in the income statement. However, by using an average official interest rate for the year, as disclosed in the Government Gazette 30614, 31190, 31893, 32212 and 32253, calculated interest on outstanding debt amounts to R1.2 million. The variance of R271 059 could not be explained. As a result, interest on outstanding debt is understated by this amount.
13. The rates valuation roll has not been updated since 2004. As a result the rates revenue of R3.5 million, which is included in the revenue of R21.1 million disclosed in the income statement, did not reconcile to the revenue calculated based on the valuation roll. The overall effect of the misstatement is not known as adequate supporting documentation was not available.

Receivables

14. The municipality does not have an accounting policy for doubtful debts. In addition, a debtors age analysis at 30 June 2009 was not available to substantiate the material account balance of R30.1 million. Although a post year end age analysis, dated 17/09/09, was obtained, the lack of supporting documentation prevented alternative procedures to obtain assurance on year end balance of R30.1 million used in the municipality's provision for bad debts computation, or determine whether the outstanding balances of indigent debtor accounts were included in the provision.

Audit work revealed that the provision for doubtful debts of R21.8 million, as disclosed in note 7, is understated by an amount of R1.3 million whilst expenditure is also understated by the same amount. In addition to this, the movement in the provision for bad debts of R3.1 million as disclosed in note 7 to the financial statements and the income statement does not agree to the nil value reflected in the general ledger.

15. Other debtors to the value of R3.1 million were incorrectly processed to fixed assets. This transaction could not be explained and was not supported by appropriate documentation.
16. Due to the lack of adequate supporting documentation, I am unable to determine whether all debtors who received free basic services are indigent and whether the person applying for indigence is the registered owner of the home. Equitable share has not been allocated against the indigent debtors' accounts as these debtors receive a certain amount of free electricity tokens. Furthermore I am unable to determine whether the outstanding balances of indigent debtors were included in the provision for bad debts computation. I was unable to verify the completeness of revenue for service charges of R9.1 million as disclosed in the income statement and Appendix D to the financial statements.
17. The general ledger reflected monthly debtors billing integration for 5 months, namely August 2008 – December 2008. The billing integration for July 2008 and January 2009 – June 2009 was not included in the general ledger. This creates significant, material uncertainty over the completeness of revenue and receivables.

18. The electricity tariffs approved by the National Electricity Regulator of South Africa were not correctly applied by the municipality. As a result electricity revenue and accounts receivable are overstated by R434 901. In addition, the following is highlighted:

- By using the kilowatts purchased (after taking distribution losses into account) at an average tariff of 0.56 per kilowatt, electricity revenue amounts to R11.1 million and does not agree to R7.3 million reflected in the income statement and Appendix D to the financial statements. The variance of R3.8 million could not be explained. Furthermore, electricity charges of R6.3 million are included in the general ledger and do not agree to R7.3 million in the income statement and Appendix D to the financial statements. The variance of R1 million could not be explained.
- An incorrect tariff of R2.28 per 20 amp meter was levied instead of R2.42 per 20 amp meter. The overall effect of the misstatement is unknown as adequate supporting documentation was not available.
- No records are kept of estimated electricity consumption. As a result, sufficient appropriate evidence could not be obtained relating to the existence, valuation, classification, accuracy, cut off, rights and completeness of the consumer receivables and completeness, classification, cut off accuracy and occurrence of revenue. The un-metered consumption at year end (for the period between the last meter reading and year end) together with the additional revenue of the previous year into account, indicates that metered electricity revenue is understated by R143 701.
- By using the number of households billed per month at a tariff of R31.19 per house hold, refuse revenue amounts to R2 million and does not agree to the value of R882 217 per the income statement and Appendix D to the financial. The variance of R1.1 million could not be explained. As a result refuse revenue and accounts receivable are understated by R1.1 million.

19. Due to the lack of adequate supporting documentation, I am unable to determine whether all debtors who received free basic services are indigent and whether the person applying for indigence is the registered owner of the home. Equitable share has not been allocated against the indigent debtors' accounts as these debtors receive a certain amount of free electricity tokens. Furthermore I am unable to determine whether the outstanding balances of indigent debtors were included in the provision for bad debts computation as stated in paragraph 14. I was unable to verify the completeness of revenue for service charges of R9.1 million as disclosed in the income statement and Appendix D to the financial statements.

Grant funding

20. No record is maintained of the expenditure incurred whilst using grant funds. As a result it was not possible to determine whether the funds were spent in accordance with the grant's terms and conditions and whether the funds were valid, accurate and complete. It was not possible to perform alternative procedures.

21. Grant income reflected in the analysis of operating income and expenditure (Appendix D) is R15.1 million whereas the actual value of grant income received is R18.7 million. The variance of R3.6 million could not be explained. As a result, grant income is understated by R3.6 million.

22. Actual grant income received for Municipal Infrastructure Grant (MIG), Equitable Share and Primary Health of R17.5 million does not agree to that reflected in DoRA of R16.6 million. The variance of R875 014 could not be explained. As a result, grant income relating to MIG, Equitable Share and Primary Health is overstated by R875 014.

23. Grant income relating to Equitable Share is R10 million whereas the general ledger reflects only R2.9 million. The variance of R7.1 million could not be explained. As a result, Equitable Share is understated by R7.1 million.
24. Equitable share of R251 645 relating to an indigent subsidy was incorrectly disclosed as other income in the income statement instead of receivables. As a result, other income is overstated and receivables are understated by R251 645.

Cash and cash equivalents

25. Bank reconciliation statements were not processed on Venus for the entire financial year i.e. July 2008 – June 2009. The corresponding entries were not processed from the bank control account to the relevant general ledger accounts, resulting in an incomplete general ledger and trial balance. This creates significant, material uncertainty over the completeness of the general ledger and trial balance.
26. The cash book balances of R2.3 million (overdraft) per the general ledger and note 11 of the financial statements does not agree to the cash book balance of R148 653 per the bank reconciliation statements. The variance of R2.5 million (overdraft) could not be explained.
27. Invalid reconciling items to the value of R1.6 million were included on the bank reconciliation. These reconciling items related to outstanding cheques that were paid prior to year end and stale cheques and could not be adequately explained.
28. In addition to this, the municipality does not have an overdraft facility available, nor was disclosure made of the overdraft facility in note 11 of the financial statements. As a result it was not possible to obtain sufficient appropriate evidence to determine the reasonableness of the cash and cash equivalents recorded on the balance sheet and the reasonableness of income and expenditure disclosed in the income statement.

Provisions

29. The municipality does not have permits or a restoration plan for its landfill sites and is in breach of Sections 20 and 28 of the National Environmental Management Act 1998 (Act No. 106 of 1998). No provision or contingent liability in respect of the obligation for restoring/rehabilitating these landfill sites or for any penalties that may be imposed by regulatory authorities in terms of Section 29 of this Act is disclosed in the financial statements.

Due to the specialist nature of the calculations required and the lack of available information it was not possible to determine the effect of this non-compliance on the provisions, expenditure and contingent liabilities disclosed in the financial statements.

30. The accounting policy relating to provisions is not in accordance with the IMFO standards and has been disclosed under Funds and Reserves. The accounting policy is also inconsistent with the prior year's annual financial statements.
31. Although attendance and leave registers were used to ensure that all leave taken was recorded, the leave records of employees are generally inaccurate. Leave records per the attendance register do not reconcile to that per the leave register. The forfeiture of leave was also not correctly applied. The leave pay provision was incorrectly computed as the municipality used the incorrect number of days due to the employees and the incorrect cost which included bonuses. Based on the audit testing performed, employee costs and the

leave pay provision disclosed in note 9 to the annual financial statements are overstated by R93 763. Although the full extent of the misstatement is not known, it is likely to be material.

The leave provision of R1.1 million is not sufficiently cash backed due to the matters identified in paragraph 52.

Employee costs

32. The employee tax forms (EMP201) for the current financial year were only submitted to the South African Revenue Services (SARS) on the 30/07/09. The municipality did not provide for any penalties and interest thereon. As a result, employee costs and payables are understated by R122 810 (penalties) and R91 846 (interest). In addition to this, the penalties and interest have not been disclosed as fruitless and wasteful expenditure in the notes to the financial statements.
33. Employees' tax of R4 685 was not deducted for five casual employees. In addition to this, the 2007/2008 tax rates were used to compute employees' tax as the operating system was not updated to reflect the 2008/2009 tax rates. As a result, employee costs and payables are overstated by R20 993.
34. The Mayor's and Councilor's allowances together with comparative figures for certain Section 57 manager's remuneration are not disclosed in note 13 to the financial statements. The accounting officer did not provide a statement to indicate that salaries, allowances and benefits of political office-bearers and councilors are within the upper limits set in the Government Gazette. The employer contributions percentage towards the various pensions, provident and retirement funds for councilors and employees were not disclosed in note 24 to the financial statements.
35. The contributions to and outstanding amounts in respect of taxes, levies, duties and pension and medical aid are not disclosed in the financial statements as required by Section 125(1)(c) and (e) of the MFMA.

Expenditure and payables

36. The municipality did not pay or accrue for any water expenditure during the current financial year. Due to the fact that no supporting documentation was available, the full extent of the misstatement is not known, but it is likely to be material.
37. Telephone expenditure of R247 883 is included in general expenditure of R4 million as disclosed in the income statement and Appendix D to the financial statements. Due to the lack of supporting documentation it was not possible to verify the validity, accuracy and completeness of the telephone expenditure. It was also not possible to determine whether this expenditure was paid or accrued for at the end of the financial year.
38. Unrecorded liabilities to the value of R674 146 were not included in the payables of R3.2 million reflected in the balance sheet and note 10 of the financial statements.
39. As a result of non submission of information it was not possible to conclude on the completeness, accuracy, occurrence, classification, cut off and compliance with the relevant legislation that governs the supply chain management process. Irregular expenditure per paragraphs 53 and 54 has not been disclosed in a note to the financial statements.

VAT

40. The value added tax (VAT) 201 forms for July 2008 – November 2008 were only submitted to the South African Revenue Services (SARS) on the 06/03/2009, whilst the VAT 201 forms for January 2009 – June 2009 were submitted to SARS on 07/09/2009. The municipality did not accrue for any penalties and interest thereon. As a result, expenditure and payables are understated by R51 403 (penalties) and R48 124 (interest). In addition to this, the penalties and interest have not been disclosed as fruitless and wasteful expenditure in the notes to the financial statements.
41. A VAT receivable of R630 234 is disclosed in the balance sheet, note 7 to the annual financial statements and the VAT 201 forms. This amount does not reconcile to the general ledger control account of R133 278. An unreconciled difference of R496 956 could not be explained. Receivables and revenue are overstated by this amount.
42. As a result of the VAT assessment performed by SARS, certain items to the value of R371 810 were disallowed. The municipality has not taken this into account and as a result, revenue and receivables are overstated by this amount.

Leases

43. The municipality has incorrectly classified photocopying machines as operating leases instead of finance leases. Only one lease payment of R44 104 has been expensed in the general ledger and income statement of the financial statements. As a result the lease liability of R419 915, assets of R482 181 and interest expenditure of R46 723 have been understated, whilst lease payments were overstated by R44 104.

Cash flow statement

44. The cash flow statement does not cast and was not prepared on the direct method as prescribed by the IMFO standards. Furthermore, references were made to incorrect notes in the financial statements.
45. Cash generated from operations of R7.9 million as disclosed in note 17 to the financial statements does not agree to the recalculated amount of R4.1 million. The variance of R3.8 million could not be explained.
46. Net cash from operating activities of R3.1 million as disclosed in note 17 to the financial statements does not agree to the recalculated amount of R4.1 million, which was based on the information contained in the financial statements. The variance of R1 million could not be explained.
47. Net cash flows from investing activities of R6.3 million and net cash flows from financing activities of R250 380 were not disclosed in the cash flow statement. The variances of R6.3 million and R250 380 could not be explained.
48. The total movement in cash for the year of R2.4 million was not disclosed in the cash flow statement.
49. The increase in cash on hand disclosed in the cash flow statements of R2.7 million does not reconcile to the movement in the cash resources per the balance sheet of R2.3 million. The variance of R405 588 could not be explained.

Disclaimer of opinion

50. 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. Accordingly, I do not express an opinion on the financial statements.

Emphasis of matter(s)

I draw attention to the following matters on which I do not express a disclaimer of opinion:

(Highlighting critically important matters presented or disclosed in the financial statements)

Basis of accounting

51. The municipality's policy is to prepare financial statements on the standards prescribed by IMFO in the Code of Practice (1997) and the Report of Financial Statements (2nd edition, January 1996) as set out in accounting policy note 1.

Going concern

52. The municipality reflects an accumulated deficit of R2.5 million in their financial statements for the year ended 30 June 2009 and as at that date, the municipality's total assets exceeded its total liabilities by R1.3 million. Although the municipality appears to be liquid, total debtors of R30.1 million, are included in total assets and could not be validated. The provision for bad debts of R21.8 million is insufficient and does not take debtors in excess of 90 days into account. By excluding the debtors from total assets, the municipality's total liabilities exceed its total assets by R6.6 million. These conditions, along with other matters, point to the existence of a material uncertainty that may cast significant doubt on the municipality's ability to sustain their operations and effect service delivery.

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

53. Management did not monitor the implementation of the requirements of the Municipal Supply Chain Management Regulations issued in terms of Chapter 4 of the MFMA. As a result from tests performed during the audit, expenditure transactions to the value of R11.8 million were not procured in accordance with these regulations and are irregular. R7.7 million of this amount relates to a lack of supporting documentation, whilst R4 million relates to unpaid invoices in excess of 30 days. This irregular expenditure is not disclosed in the financial statements.

54. Irregular expenditure to the value of R85 496 relating to employee costs was not disclosed in the financial statements.

- Overtime to the value of R14 814 was not authorised or supported by overtime sheets. R10 736 of this value relates to claims that were authorised by the employees themselves and not senior management.
- R5 315 was paid to an employee one month after resignation. This payment could not be validated or adequately explained.

- New employees received R27 192 more than the minimum scale which could not be adequately explained.
- No supporting documentation was available to substantiate travel and subsistence claims to the value of R38 175.

Other matters

Internal audit

55. Nxuba Municipality and Amatole District Municipality have a shared internal audit service. Only one draft audit report was received from the internal auditors during the year under review. The audit was not scheduled for the current financial year or approved by the Audit Committee. The shared internal audit function is assessed as ineffective for the period under review.

Material inconsistencies in information included in the annual report

56. The draft annual report was not received and it was therefore not possible to determine whether there were any material inconsistencies in the report.

Material inconsistencies between the financial statements and general ledger

57. The following un-reconcilable variances were noted between the financial statements and general ledger:

Item	Per AFS (R)	Per GL (R)	Difference (R)
Grants and Subsidies	15,088,109	11,359,041	3,729,068
Other Income	516,460	710,490	(194,030)
Income from Tariffs, Service Charges etc	1,041,721	937,661	104,060
Salaries, wages and allowances	15,047,480	15,989,168	(941,688)
Electricity Bulk Purchases	4,122,324	(2,667,859)	6,790,183
General expenses	4,034,126	3,776,823	257,303
Repairs and Maintenance	409,027	245,376	163,651
Capital Charges	18,563	-	18,563
Contribution to Fixed Assets	6,658,164	6,616,907	41,257
Appropriations for the year	3,887,055	-	3,887,055
Accumulated deficit	(2,499,488)	-	(2,499,488)
Trust funds	183,921	318,435	(134,514)
Fixed assets	-	40,088	(40,088)

Investments	39,400	-	39,400
Debtors	8,326,049	11,447,987	(3,121,938)
Intangible assets	24,435	-	24,435
Creditors	3,230,396	6,002,810	(2,772,414)
Bank overdraft	2,372,527	2,374,333	(1,806)

No explanations were available for these variances.

Un-audited supplementary schedules

58. The supplementary information set out on pages 25 to 30 does 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

59. The municipality did not comply with Section 17 of the MFMA as adequate policies and procedures over budgetary control were not implemented. The budgeted figures were unrealistic and larger than the actual results, thus creating a misleading indication of the municipality's performance. The lack of continued monitoring, supervision and review has cast significant doubt over the municipality's ability to sustain their operations and effect service delivery.

60. Signed electronic returns relating to conditional grant spending for the current financial year were not submitted to National Treasury. This is contrary to the requirements of Section 74 of the MFMA.

61. No evidence was provided to indicate that Notice number 45/2008, dated 10/07/2008, relating to tariff increases was advertised in the local newspaper or that the notice was sent to the MEC for local government. This is contrary to requirements of Section 75A of the Municipal Systems Act.

62. No evidence was provided to indicate that the Finance Management Grant (FMG) Activity Plan for the 2008/09 financial year was submitted to Provincial Treasury. This is contrary to the requirements of Section 10 of DoRA.

63. By-laws relating to law enforcement and/or crime prevention and the regulation of liquor outlets' trading hours were not established. This is contrary to the requirements of the Liquor Act No. 59 of 2003.

64. The municipality is in contravention of Section 20 of the Environment Conservation Act No. 73 of 1989 and Section 28 of the National Environmental Management Act No. 107 of 1998 as two landfill sites are operated without permits and no remedial action has been taken to rehabilitate the environment. Refer to paragraph 29.

Non-compliance with accounting policy

65. The accounting policy relating to retirement benefits states that a full actuarial valuation should be performed every three years. No such valuation was performed for the current financial year. The rules of the pension/provident funds were not provided for audit purposes.

As a result, the pension/provident funds might be incorrectly classified as defined contribution plans.

Fixed assets

- 66. A deed search revealed that land and buildings to the value of R2.3 million were not registered in the name of the municipality. In addition to this, the deed search revealed that land and buildings to the value of R756 895 belonged to Cacadu District Municipality. Due to the lack of supporting documentation it was not possible to verify that land and buildings included in the fixed asset register were valid, accurately recorded and complete.
- 67. The fixed asset register does not contain adequate information relating to the fixed assets recorded therein. Assets are not marked with unique identification numbers and are not appropriately cross referenced to the asset register. The dates of acquisition are not included in the asset register. As a result, fixed assets could not be reliably verified. There were no alternative procedures that could be performed.
- 68. A settlement plan to the value of R934 185 was incorrectly capitalized as an asset. The settlement plan consisted of expenditure incurred on community projects. Due to the lack of supporting documentation it was not possible to verify the validity, accuracy and completeness of the settlement plan.

Housing development projects

- 69. An analysis of the assets and liabilities of the housing development projects, which are administered through separate trust fund accounts, was not prepared for the current financial year. Due to the lack of supporting documentation it was not possible to determine the reasonableness of the housing development projects. The full extent of any possible misstatement is not known, but it is likely to be material.

Governance framework

- 70. 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

- 71. 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	R A	CA	IC	M
4 – 5	Corresponding figures	5; 6	5			1; 3
6 -7	Journal entries	5; 6; 7	5	5; 6	3	1; 3
8	Suspense and clearing accounts	5; 6	5	5; 6		1; 3

10	Consumer deposits	5; 6				1
11 -13	Fixed assets	5; 6				1; 3
14 -31	Revenue and receivables	5; 6; 7	5	5; 6		1; 3
32 – 35	Cash and cash equivalents	5; 6; 7	5	5; 6	3	1; 3
36 – 38	Provisions	5; 6; 7				1; 3
39 – 44	Employee costs	5; 6; 7		1	3	1; 3
45 – 48	Expenditure and payables	5; 6; 7		5; 6		1; 3
49 - 51	VAT	5; 6; 7		5; 6		
52	Leases	5; 6; 7		5; 6		1; 3
53 – 58	Cash flow statement	5; 6; 7				1; 3
63 - 64	Irregular expenditure	5; 6; 7	5	5; 6		1; 3
Legend						
CE = Control environment						
	The organizational 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 standard for financial reporting.					4
	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 analyze 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 authorized, 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

72. 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.		✓
Quality of financial statements and related management information			
2	The financial statements were not subject to any material amendments resulting from the audit.		✓
3	The annual report was submitted for consideration prior to the tabling of the auditor's report.		✓
Timeliness of financial statements and management information			
4	The annual financial statements were submitted for auditing as per the legislated deadlines (Section 126 of the MFMA).	✓	
Availability of key officials during audit			
5	Key officials were available throughout the audit process.		✓
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. 	✓	
	<ul style="list-style-type: none"> • The audit committee operates in accordance with approved, written terms of reference. 		✓
	<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. 		✓
7	Internal audit		
	<ul style="list-style-type: none"> • The municipality had an internal audit function in operation throughout the financial year. 		✓
	<ul style="list-style-type: none"> • The internal audit function operates in terms of an approved internal audit plan. 		✓
	<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 		✓
8	There are no significant deficiencies in the design and implementation of internal control in respect of financial and risk management.		✓
9	There are no significant deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations.		✓
10	The information systems were appropriate to facilitate the preparation of the financial statements.		✓
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 62(c) of the MFMA.		✓

12	Delegations of responsibility are in place, as set out in Section 79 of the MFMA.		✓
Follow-up of audit findings			
13	The prior year audit findings have been substantially addressed.		✓
14	Oversight resolutions have been substantially implemented.		✓
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.		✓
16	Adequate control processes and procedures are designed and implemented to ensure the accuracy and completeness of reported performance information.		✓
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 Municipality against its mandate, predetermined objectives, outputs, indicators and targets Section 68 of the MFMA municipalities.		✓
18	There is a functioning performance management system and performance bonuses are only paid after proper assessment and approval by those charged with governance.		✓

Overall reflections/conclusion on the governance framework based on other key governance requirements

73. Monitoring of controls are not in place to ensure that all information disclosed in the annual financial statements are valid, accurate and complete. The lack of availability of key officials has contributed to the delays experienced throughout the audit.
74. The control environment within the municipality is not conducive to good governance and accountability as management have not ensured that the risk management processes and internal audit function have received the appropriate attention. The audit committee is an essential component in achieving good governance and accountability and is effective although it is hampered by the poor control environment and the ineffective internal audit function.
75. The root causes indicated in the two preceding paragraphs were compromised further by the following:
- Lack of personnel and skills in the finance section
 - The commitment of personnel in the finance section
 - Lack of funding to provide required training to finance personnel
76. Due to the matters that give rise to the limitation of scope, the extent of non compliance with relevant government prescripts, the lack of controls and risk management and fraud prevention strategies, the possibility that the financial statements are materially misstated resulting from fraud and errors, either on individual balances or the financial statements taken as a whole, cannot be excluded

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

Report on performance information

77. I was engaged to review the performance information.

The accounting officer's responsibility for the performance information

78. 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).
79. 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 section 45 of the MSA.
80. 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.
81. 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)

Performance information

Non-compliance with regulatory requirements

82. The integrated development plan of Nxuba Municipality did not include a financial plan and budget projection for the next three years as required by Section 26 of the MSA. Furthermore no evidence was available to indicate whether a summary of the plan was made available for the local community's commentary or whether the municipality implemented the IDP and conducted its affairs in a manner that was consistent with its IDP as required by Section 15 of the Municipal Planning and Performance Management Regulations and Section 26 of the MSA, respectively.
83. The IDP did not contain evidence to indicate whether Council's development strategies were aligned with any national or provincial sectoral plans as required by Section 26 of the MSA.
84. The Annual Performance Report only includes the current year's performance targets. The previous year's performance targets were not disclosed as required by Section 46 of the MSA.

Internal auditing of performance measurements

85. Nxuba Municipality did not develop and implement mechanisms, systems and processes for auditing the results of performance measurement as part of its internal audit processes, as required in terms of Section 45 of the MSA.

Lack of implementation of a performance management system

86. Nxuba Municipality did not implement a framework that describes and represents how the municipality's cycle and processing of performance planning, monitoring, measurement, review, reporting and improvement will be conducted, organised and managed, including determining the roles of the different role players, as required in terms of Regulations 7 and 8 of the Municipal Planning and Performance Management Regulations, 2001.

87. In addition to this, quarterly performance reports were not prepared as required in terms of Section 41 of the MSA.

Mid-year budget and performance assessments

88. The mid-year performance assessment budget did not contain the monthly statement required for the first half of the financial year; the municipality's service delivery performance during the first half of the financial year and the service delivery targets and performance indicators set in the Service Delivery Budget Implementation Plan (SDBIP); or the previous year's annual report and progress on resolving problems identified in the annual report, as required by Section 72 of the MFMA.

89. Furthermore, the SDBIP was incomplete as the monthly budget projections were omitted.

Usefulness and reliability of reported performance information

90. The following criteria were used to assess the usefulness and reliability of the information on the municipality's performance with respect to the objectives in its integrated development plan:

- **Consistency:** Has the municipality reported on its performance with regard to its objectives, indicators and targets in its approved integrated development plan?
- **Relevance:** Is the performance information as reflected in the indicators and targets clearly linked to the predetermined objectives and mandate. Is this specific and measurable, and is the time period or deadline for delivery specified?
- **Reliability:** Can the reported performance information be traced back to the source data or documentation and is the reported performance information accurate and complete in relation to the source data or documentation?

The following audit findings relate to the above criteria:

Reported performance information not reliable

Lack of source documentation

91. The reported actual achievement of the provision of electricity, maintenance of all internal gravel and tar roads, infrastructure development and service delivery and municipal financial viability and management could not be substantiated by adequate evidence/supporting documentation.

Lack of appropriate information systems generating performance information

92. Significant appropriate audit evidence with regard to the reported performance information of Nxuba Municipality could not be obtained as the information system used for generating performance information was not appropriate to facilitate the preparation of accurate and complete actual performance information. In addition to this, there are no key controls to monitor the accuracy, completeness and validity of the information that is input, processed and output in the form of reports.

Source information not accurate and complete

93. No source information or evidence was provided to support the accuracy and completeness of the reported performance information with regard to infrastructure development and service delivery and municipal financial viability and management.

94. The Annual Performance Report indicated a target of 300 applications for low cost housing which was actually met. Upon subsequent enquiry it was discovered that no applications for low cost housing were completed.
95. In addition to this, the Annual Performance Report indicated that the municipality met their target of being fully compliant with GRAP whereas the IMFO basis of accounting is still being applied.

APPRECIATION

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

Auditor-General

EAST LONDON

30 November 2009



**AUDITOR-GENERAL
SOUTH AFRICA**

Auditing to build public confidence