

**REPORT OF THE AUDITOR-GENERAL TO THE LIMPOPO PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF THE BLOUBERG 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 Blouberg Municipality which comprise the statement of financial position 30 June 2009, and the statement of financial performance, the statement of changes in net assets and the cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages [xx] 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, as set out in accounting policy note 1.1 to the financial statements and in the manner required by the Local Government: 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, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.
4. Paragraph 11 *et seq.* of the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of Financial Statements* requires that financial reporting by entities shall provide information on whether resources were obtained and used in accordance with the legally adopted budget. As the budget reporting standard is not effective for this financial year, I have determined that my audit of any disclosures made by the Blouberg Municipality in this respect will be limited to reporting on non-compliance with this disclosure requirement.

**Basis for disclaimer of opinion**

**Corresponding figures**

5. In my previous audit report dated 30 November 2008 I was unable to express an audit opinion on the financial statements of the municipality for the year ended 30 June 2008. The qualification matters have not been resolved while no alternative

procedures were possible and my audit report is disclaimed regarding the corresponding figures as discussed hereunder:

- Trade and other payables – R18,2 million
- Unspent conditional grants and receipts – R4,1 million
- Property, Plant and equipment – R126,3 million
- Consumer Receivables – R9,1 million
- Other Receivables – R4,1 million
- Cash and cash equivalents – R5,9 million
- Revenue – R77,1 million
- Expenditure, excluding employee related cost – R26,9 million
- Cash Flow statement: Purchase of property, plant and equipment – R24,3 million.

### **Cash and cash equivalents**

6. Sufficient appropriate audit evidence could not be provided for the reconciling items amounting to R15.1 million on the bank reconciliations at year-end. Consequently, I was unable to conclude on what impact, if any, the reconciling items should have on the accounts of the municipality. Alternative procedures were considered but the municipality's records did not permit it.
7. Differences of R896 293 and R6.1 million have been identified between two bank reconciliations amounting to R9.1 (bank overdraft) and R571 580 and the bank balances on the face of the statement of financial position amounting to R14.9 (bank overdraft) and R2 million respectively.

### **Payables**

8. I was unable to determine the correctness of leave provision amounting to R2.7 million as a detailed leave report was not provided for audit purposes. Alternative procedures could not be performed.
9. A reconciliation to substantiate suspense account transactions (unallocated direct bank deposits) amounting to R9.2 million could not be provided. Consequently I could not conclude whether the transactions do exist, that the municipality has an obligation to them and that the amounts reflected are accurate. Alternative procedures were considered but the municipality's records did not permit it.

### **Property, plant and equipment (PPE)**

10. Included in operating expenditure: repairs and maintenance is capital expenditure to the amount of R740 014. Expenditure is overstated by R740 104 and PPE is understated by the same amount.
11. Appropriate audit evidence for a journal transaction amounting to R860 343 could not be provided. Alternative procedures were considered but the municipality's records did not permit it.
12. The existence and completeness of PPE could not be verified due to the following:
  - assets in the fixed asset register were bundled together resulting in individual components not being adequately described, *inter alia* serial numbers, make model etc. were we were not able to determine whether assets amounting to R54.3 million exists

- a number of assets could not be traced from the floor to the asset register
- a detailed listing of all the property owned by the municipality were not provided
- a deed search performed confirmed 46 properties own by the municipality. The properties listed on the deed search could not be confirmed to the fixed asset register and financial statements
- not all fixed assets were bar-coded or have a unique asset number assigned to them.

### **Receivables**

13. A reconciliation to substantiate suspense account transactions amounting to R2.1 million could not be provided. Consequently I could not conclude whether the transactions do exist, that the municipality has rights to *them* and that the amounts reflected are accurate. Alternative procedures were considered but the municipality's records did not permit it.

### **Revenue**

14. Service charges as disclosed in note 12 to the financial statements include revenue amounting to R1 062 032, accrued by the municipality for the provision of water services on behalf of Capricorn District Municipality. This has been incorrectly accounted for by the municipality as their own revenue, and consequently service charges are overstated by this amount. The municipality's records did not permit the application of alternate audit procedures to determine the misstatement in consumer debtors, trade and other receivables (on account of output VAT) and the accumulated surplus. Further, I am unable to determine the impact on the prior year's accumulated surplus.
15. Appropriate audit evidence could not be provided for a revenue transaction (donation) amounting to R1.1 million. Consequently I could not conclude whether the transactions did occur, do affect the municipality and at what amounts they should be recorded. Alternative procedures were considered but the municipality's records did not permit it.

### **Presentation and disclosure**

16. The ageing of accounts receivable balances amounting to R3,8 million are not disclosed as prescribed by International Accounting Standard 39 (Financial Instruments: Recognition and Measurement).
17. Comparative amounts for property rates and valuations have not been disclosed in note 11 to the financial statements.

### **Disclaimer of opinion**

18. Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have been unable 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**

### **Unauthorised expenditure**

19. As disclosed in note 23 to the financial statements, unauthorised expenditure to the amount of R735 318 was incurred, as the budget was exceeded.

### Other matters

Without qualifying my audit opinion, I draw attention to the following matters that relate to my responsibilities in the audit of the financial statements:

### Unaudited supplementary schedules

20. The supplementary information set out on pages [xx] to [xx] 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

#### Local Government: Municipal Finance Management Act, 2003 (Act no. 56 of 2003)(MFMA)

21. Section 17(1) of the MFMA requires the municipality to prepare an annual budget setting out realistic anticipated revenue for the budget year from each revenue source.

The municipality budgeted for a VAT refund amounting to R2 751 837 in the income budget. Although this will create cash flow during the year, this is not considered part the municipality's revenue stream.

#### Local Government: Municipal Systems Act, 2000 (Act no. 32 of 2000) (MSA)

22. Councilors did not declare their interest, as required by the Municipal Systems Act, 2000 (Act No. 32 of 2000) (schedule (1), section (5) – disclosure of interest).

### Governance framework

23. 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

24. 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
5	Qualifying matters on corresponding figures not resolved during the year under review	1-7	1-5	1-7	1-3	1-3
6, 7	Cash and cash equivalents	1-7	1-5	1-7	1-3	1-3
8, 9	Payables	1-7	1-5	1-7	1-3	1-3
10 – 12	Property, plant and equipment	1-7	1-5	1-7	1-3	1-3
13	Receivables	5-7	4	3		1
14, 15	Revenue	1-7	1-5	1-7	1-3	1-3
16, 17	Presentation and disclosure	5,6		5		1

25. The general financial management functions is the responsibility of the accounting officer, assisted by top management in managing and co-ordinating the financial administration of the municipality and exercising financial management responsibilities within their respective areas of responsibility. Reasonable steps were not taken to ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control over the whole spectrum of municipal activities. This impacted negatively on all five root causes in the table below.

<b>Legend</b>	
<b>CE = Control environment</b>	
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 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
<b>RA = Risk assessment</b>	
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
<b>CA = Control activities</b>	
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
<b>IC = Information and communication</b>	
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
<b>M = Monitoring</b>	
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

26. 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
<b>Clear trail of supporting documentation that is easily available and provided in a timely manner</b>			
1.	No significant difficulties were experienced during the audit concerning delays or the availability of requested information.		✓
<b>Quality of financial statements and related management information</b>			
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.		✓
<b>Timeliness of financial statements and management information</b>			
4.	The annual financial statements were submitted for auditing as per the legislated deadlines (section 126 of the MFMA).	✓	
<b>Availability of key officials during audit</b>			
5.	Key officials were available throughout the audit process.	✓	
<b>Development and compliance with risk management, effective internal control and governance practices</b>			
6.	Audit committee		
	<ul style="list-style-type: none"> <li>• The municipality had an audit committee in operation throughout the financial year.</li> </ul>	✓	
	<ul style="list-style-type: none"> <li>• The audit committee operates in accordance with approved, written terms of reference.</li> </ul>	✓	
	<ul style="list-style-type: none"> <li>• The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA.</li> </ul>		✓
7.	Internal audit		
	<ul style="list-style-type: none"> <li>• The municipality had an internal audit function in operation throughout the financial year.</li> </ul>	✓	
	<ul style="list-style-type: none"> <li>• The internal audit function operates in terms of an approved internal audit plan.</li> </ul>	✓	
	<ul style="list-style-type: none"> <li>• The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA.</li> </ul>	✓	
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(1)(c)(i) of the MFMA.		✓
12.	Delegations of responsibility are in place, as set out in section 79 of the MFMA.	✓	
<b>Follow-up of audit findings</b>			
13.	The prior year audit findings have been substantially addressed.	✓	
<b>Issues relating to the reporting of performance information</b>			
14.	The information systems were appropriate to facilitate the preparation of a performance report that is accurate and complete.		✓
15.	Adequate control processes and procedures are designed and implemented to ensure the accuracy and completeness of reported performance information.		✓
16.	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 Blouberg Municipality against its mandate, predetermined objectives, outputs, indicators and targets (section 68 of the MFMA).	✓	

No.	Matter	Y	N
17.	There is a functioning performance management system and performance bonuses are only paid after proper assessment and approval by those charged with governance.		✓

27. A consultant was appointed to prepare the financial statements as the CFO did not have the necessary capacity. The financial statements were subjected to material amendments resulting from the audit. In addition, some changes were not affected to the financial statements.
28. The appropriate system report for leave provision was not generated by the applicable department at year-end, limiting my ability to perform pre-determined audit procedures.
29. The turn around time to respond to our audit findings as well as the quality of the responses impacted negatively on our audit. In a number of instances supporting documentation was not provided for audit purposes or provided at a very late stage of the audit.
30. The accounting officer and chief financial did not always design and implemented internal control in respect of financial and risk management. No risk assessment was conducted and implemented for the year under review to mitigate the risk of incorrect disclosure of financial information in the financial statements. In addition, a number of non-compliance with applicable laws and regulations were detected during the cause of the audit.
31. Adequate monitoring and supervision were not always undertaken by the accounting officer, chief financial officer, internal audit and audit committee to ensure effective internal control over financial reporting, including financial risk management as is evident in paragraphs 6 to 17 of this audit report.

## **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

### **Report on performance information**

32. I was engaged to review the performance information.

### **The accounting officer's responsibility for the performance information**

33. 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**

34. 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.
35. 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.
36. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

## **Findings on performance information**

### **Non-compliance with regularity requirements**

#### **No reporting of performance information**

37. The municipality did not provide me with the annual performance report in terms of section 46 of the MFMA as it was not yet finalised and approved at the time of the audit.

#### **Existence and functioning of a performance audit committee**

38. Although the existing audit committee was utilized as a performance audit committee as provided for in regulation 14(2) of the Municipal Planning and Performance Management Regulations, 2001, the audit committee charter did not explicitly identify performance management and evaluation as an item in their responsibilities.

39. The audit committee did not:

- review the Blouberg municipality's performance management system and make recommendations in this regard to the council of the Blouberg municipality.
- submit an auditor's report to the Blouberg council regarding the performance management system at least twice during the financial year.
- the municipality did not develop and implement mechanisms, systems and processes for auditing the results of performance measurements as part of its internal auditing processes.

#### **Lack of adoption of a performance management system**

40. The Blouberg municipality did not adopt and implement a proper framework that describes and represent how the municipality's cycle and processes 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 regulation 7 and 8 of the Municipal Planning and Performance Management Regulations, 2001.

#### **No mid-year budget and performance assessment**

41. The accounting officer of the Blouberg municipality did not (by 25 January each year) assess the performance of the municipality during the first half of the financial year, taking into account 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 and budget implementation plan, as required by section 72 of the MFMA.

#### **Performance indicators and performance targets**

42. The Blouberg municipality did not make known, both internally and to the general public, the key performance indicators and performance targets set by it for purposes of its performance management system as required by section 44 of the MSA.

#### **Community Involvement**

43. Appropriate and sufficient evidence that the Blouberg municipality adhered to the following legislative requirements could not be provided:



- afforded the local community at least 21 days to comment on the final draft of its integrated development plan before it is submitted to council for adoption, as required by regulation 15(3) of the Municipal Planning and Performance Management Regulations, 2001.
- gave notice to the public of the adoption of the IDP within 14 days by council, as required by section 25(4) of the MSA.

#### **APPRECIATION**

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

Polokwane

18 February 2010



**A U D I T O R - G E N E R A L**  
**S O U T H A F R I C A**

*Auditing to build public confidence*

DRAFT