

REPORT OF THE AUDITOR-GENERAL TO THE WESTERN CAPE PROVINCIAL PARLIAMENT AND THE COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF THE EDEN DISTRICT MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2009

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the Eden District Municipality which comprise the statement of financial position as at 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, 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 Standards of Generally Recognised Accounting Practice (Standards of GRAP) and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2008 (Act No. 2 of 2008) (DoRA) 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)(a) of the MFMA, my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with the International Standards on Auditing read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

6. Paragraph 11 *et seq.* of the Standards 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 Eden District Municipality in this respect will be limited to reporting on non-compliance with this disclosure requirement.
7. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

8. In my opinion the financial statements present fairly, in all material respects, the financial position of the Eden District Municipality as at 30 June 2009 and its financial performance and its cash flows for the year then ended, in accordance with the Standards of GRAP and in the manner required by the MFMA and DoRA.

Emphasis of matters

Without qualifying my opinion, I draw attention to the following matters:

Amendments to the applicable basis of accounting

9. As set out in accounting policy note 1 to the municipality's financial statements, the municipality has adopted the transitional provisions as allowed by directive 4: "Transitional Provisions for the Adoption of Standards of GRAP by Medium and Low Capacity Municipalities" as issued by the Accounting Standards Board.

Unauthorised expenditure

10. As disclosed in note 37.1 to the financial statements, unauthorised expenditure to the amount of R49 972 055 was incurred as a result of over-expenditure on the approved budget, which has subsequently been approved by the council on 29 October 2009.

Fruitless and wasteful expenditure

11. As disclosed in note 37.2 to the financial statements, fruitless and wasteful expenditure to the amount of R404 515 was incurred as a result of negligence by a project manager in carrying out his duties as he behaved in a manner that was in breach of the rules and regulations of the Department of Water Affairs.

Irregular expenditure

12. As disclosed in note 37.3 to the financial statements, irregular expenditure to the amount of R66 056 was incurred as a result of fraudulent allocations by the global fund administrator and overtime claimed for work not performed of which an amount of R8 556 was recovered.

Events after the reporting date

13. As disclosed in note 43 to the financial statements:
- the Southern Cape is experiencing a severe drought, which resulted in certain areas within the Eden District Municipality being declared a disaster zone
 - the municipal manager was suspended pending the finalisation of certain investigations and the contract of the acting chief financial officer was terminated. A new acting municipal manager and acting chief financial officer were subsequently appointed

Restatement of corresponding figures

14. As disclosed in note 33 to the financial statements, the corresponding figures for 30 June 2008 have been restated as a result of errors discovered during the 2008-09 financial year in the financial statements of the Eden District Municipality at, and for the year ending, 30 June 2008.

Other matters

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

15. I have not obtained the other information included in the annual report and have not been able to identify any material inconsistencies with the financial statements.

Unaudited supplementary schedules

16. 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

17. A written contract stipulating the terms and conditions was not concluded between the municipality and the successful bidder for a tender to the value of R176 472 as required by section 116 of the MFMA.
18. The original annual budget, prepared by the municipality for the 2008-09 financial year, reflected a budgeted loss of R38 938 677, which resulted in non-compliance with the principles set out in section 18 of the MFMA. The budget was also not prepared on the same basis that the annual financial statements were prepared.

Local Government: Municipal Systems Act

19. Although the employment contracts for persons appointed in terms of section 57 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) made provision for the standards and procedures for evaluating performance and the intervals for evaluation, as required by section 57(4)(b) of the MSA, such assessments were not performed during the 2008-09 financial year.

Governance framework

20. 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 key governance responsibilities addressed below:

Key governance responsibilities

21. 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 in section 126 of the MFMA.	■	
Availability of key officials during audit			
5.	Key officials were available throughout the audit process.		■

No.	Matter	Y	N
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(1)(c)(i) of the MFMA.		■
12.	Delegations of responsibility are in place, as set out in section 79 of the MFMA.	■	

No.	Matter	Y	N
Follow-up of audit findings			
13.	The prior year audit findings have been substantially addressed.		■
14.	SCOPA resolutions have been substantially implemented.	Not applicable	
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 Eden District Municipality against its mandate, predetermined objectives, outputs, indicators and targets (section 68 of the MFMA).	■	
18.	There is a functioning performance management system and performance bonuses are only paid after proper assessment and approval by those charged with governance.		■

22. With the implementation of the Standards of GRAP, the municipality experienced difficulties in producing financial statements for audit purposes that were free from errors and omissions, although not in all instances material. This situation could have led to the qualification of the financial statements had the municipality not adjusted their financial statements during the audit, based on my findings.
23. This is indicative of a situation where:
- ongoing monitoring by the finance department is not effective enough to assess the effectiveness of internal control over financial reporting
 - policies and procedures related to financial reporting, which aim to improve the quality of reconciliations and maintenance and availability of underlying records and, therefore, the accuracy and completeness of financial reporting, are not adequately established and communicated to staff in the finance department
 - management did not adequately identify risks relevant to accurate and complete financial reporting and actions were not taken to address such

risks. These risks should be identified by way of a formal risk assessment process relating to the achievement of financial reporting objectives and/or by implementing a formal and regularly monitored financial management improvement plan, which includes actions to address not only the material findings arising from the prior year's external audit, but also the control and compliance deficiencies identified in that audit. The risk assessment process should inform the agendas of the audit committee and internal audit unit, which are essential elements in the review of the design and implementation of sound internal controls to achieve good governance and accountability over financial reporting.

24. An action plan was not implemented by management to address the findings raised by the external auditors during the prior year and consequently a number of those findings recurred.
25. As a result of the suspension of the municipal manager and the termination of the contract of the acting chief financial officer, as well as training and leave, key officials were not available throughout the audit. Significant additional audit effort was also required to obtain the audit evidence requested.
26. The next few years will pose greater challenges for the municipality with the ongoing transition to full compliance with the Standards of GRAP and the implementation of additional, approved Standards of GRAP. In order to deal with the prevalence of material misstatements in financial statements that have to be corrected during the audit, the municipality needs to:
 - develop a strategy to improve financial management controls relating to compliance with accounting standards and reconciliation and maintenance of underlying accounting records, in order to produce accurate and complete financial statements
 - produce monthly financial accounts for review by management
 - subject the financial statements to a quality review before they are submitted for auditing, while the internal audit unit and audit committee can assist with evaluating the adequacy of the design and implementation of controls around the preparation of the financial statements.
27. Although the municipality had established an outsourced internal audit unit, the absence of an audit committee resulted in no internal audit reports being issued during the 2008-09 financial year. The internal audit charter and annual audit plan was also not approved.
28. The municipality did not have a functional audit committee for the 2008-09 financial year as required by section 166 of the MFMA as the council was in the process of reviewing the composition of the audit committee. The audit committee charter was also not approved.
29. The establishment of a functional internal audit unit would, under the auspices of an active audit committee, therefore contribute in identifying deficiencies in the design and implementation of internal controls and governance practices in the municipality. Adequate capacity and stability in the finance department, especially at the position of chief financial officer, must be established to also

address the internal control and governance deficiencies and to reduce the municipality's dependency on consultants.

30. The development of a performance management system that facilitates the preparation of a performance report that is accurate and complete and available for internal and external review in a timely manner, requires urgent attention from the accounting officer with the support of internal audit and the audit committee to ensure compliance with section 40 of the MSA.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

Report on performance information

31. I was engaged to review the performance information.

The accounting officer's responsibility for the performance information

32. 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 MSA.

The Auditor-General's responsibility

33. 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.
34. In terms of the foregoing my engagement included performing procedures of a review 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.
35. 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 regulatory requirements

36. The integrated development plan did not comply with the requirements of section 26 of the MSA as:
 - it did not reflect a financial plan which includes a budget projection for at least the next three years as required by section 26(h) of the MSA; and
 - it did not reflect the key performance indicators and performance targets determined by section 41 of the MSA, as required by section 26(i) of the MSA.
37. The municipality had not developed and implemented adequate mechanisms, systems and processes for the monitoring and review of, and reporting on, performance information, as required by the sections 38 to 41 of the MSA. The municipality had developed a performance review policy as required by section 13 of the Local Government: Municipal Planning and Performance

Management Regulations, 2001 (regulations), issued in *GNR.796 of 24 August 2001*, but it had not yet been approved or implemented.

38. Audits were not performed on the results of performance measurement as required by section 45(a) of the MSA and section 14 of the regulations.

Performance information not received in time

39. An assessment could not be performed of the reliability of the reported performance information, as set out on pages xx to xx of the annual report, since the information was not received in time for audit purposes.

APPRECIATION

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

Auditor - general

Cape Town

November 2009



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

DRAFT

The Accounting Officer
Eden District Municipality
PO Box 12
GEORGE
6530

30 November 2009

Reference: 21425REG08/09

Dear Mr Hoogbaard

FINAL MANAGEMENT REPORT ON THE REGULARITY AUDIT AND THE REVIEW OF PERFORMANCE INFORMATION OF THE EDEN DISTRICT MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2009

INTRODUCTION

1. This management report is provided to the accounting officer of the Eden District Municipality to facilitate consideration and correction of the audit findings that have come to our attention to date. A final management report will be provided after the completion of the audit.
2. The report contains the following main subsections:
 - The Auditor-General's responsibilities
 - The Accounting officer's responsibilities
 - Significant findings from our audit of the financial statements
 - Financial matters
 - Governance matters
 - Significant findings from our review of the performance information
 - Summary of detailed audit findings
3. The detailed findings contained in this report were communicated during the course of the audit and include management's responses thereto.

THE AUDITOR-GENERAL'S RESPONSIBILITIES

4. Our responsibility is to express an opinion on the financial statements and to report on findings related to our review of performance information. Our engagement letter sets out our responsibilities in detail. These include the following:
 - Planning and performing the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements, whether caused by fraud or error.
 - Performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the financial statements.
 - Considering internal controls relevant to the entity's preparation and fair presentation of the financial statements.
 - Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management.
 - Evaluating the overall presentation of the financial statements.
 - Expressing an opinion on the financial statements based on the audit in accordance with the International Standards on Auditing (ISAs).
 - Evaluating non-compliance with applicable legislation relating to financial matters, financial management and other related matters.
 - Evaluating the appropriateness of controls, systems and processes to ensure the accuracy and completeness of reported performance information.
 - Reading other information in documents containing the audited financial statements.
5. Because of the test nature and other inherent limitations of an audit, we do not guarantee the completeness and accuracy of the financial statements or performance information, or compliance with all applicable legislation.
6. Having formed an opinion on the financial statements we may draw the user's attention, when in our opinion it is necessary to do so, by way of additional communication in the auditor's report to:
 - a matter, although appropriately presented or disclosed in the financial statements, that is of such importance that it is fundamental to user's understanding of the financial statements; or
 - as appropriate, any other matter that is relevant to the user's understanding of the auditor's responsibilities or the auditor's report.

These items are normally included under the headings 'emphasis of matter' and 'other matters' respectively in the auditor's report and include an indication that they do not affect the auditor's opinion.

THE ACCOUNTING OFFICER'S RESPONSIBILITIES

7. The accounting officer's responsibilities are set out in detail in the engagement letter. These include the following:
- The preparation and fair presentation of the financial statements in accordance with the Standards of Generally Recognised Accounting Practice (GRAP).
 - Designing, implementing and maintaining internal controls relevant to the preparation of the financial statements.
 - Selecting and applying appropriate accounting policies, and making accounting estimates that are appropriate in the circumstances.
 - Disclosing known instances of non-compliance or suspected non-compliance with laws and regulations, of which the effects should be considered when preparing financial statements.
 - Monitoring and reporting on performance against predetermined objectives.
 - Providing access to all information that is relevant to the preparation of the financial statements and performance information, such as records, documents and other matters.
 - Disclosing all matters concerning any risk, allegation or instances of fraud.
 - Accounting for and disclosing related party relationships and transactions.

SIGNIFICANT FINDINGS FROM OUR AUDIT OF THE FINANCIAL STATEMENTS

FINANCIAL MATTERS

Misstatements not corrected at the date of this report

8. The following represents the material misstatements that arose from a difference between the disclosures in the financial statements and the **disclosures** required by the financial reporting framework. These misstatements were identified during the audit and had **not** been corrected by management at the date of this report. These misstatements were not prevented or detected by the municipality's system of internal control. We urge management to implement improved controls over the matters reflected as the root cause for the misstatements.

Disclosure	Amount R	Root cause(s) (as per table below)
Fruitless & wasteful expenditure	R156 402	M1

Material misstatements corrected during the audit

9. The following represents the material misstatements that arose from a difference between the disclosures in the financial statements and the **disclosures** required by the financial reporting framework. These misstatements were identified during the audit and had been corrected by management at the date of this report. These misstatements were not prevented or detected by the municipality's system of internal control. We urge management to implement improved controls over the matters reflected as the root cause for the misstatements.

Disclosure	Amount R	Root cause(s) (as per table below)
Unauthorised expenditure	R49 972 055	CE5
Fruitless & wasteful expenditure	R248 113	M1

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 standard for financial reporting.	4
The accounting officer/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 security of the data.	2
Manual or automated controls are not designed to ensure that the transactions 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
Reviews by internal audit, the audit committee or self-assessment are not evident.	2
Internal control deficiencies are not identified and communicated in a timely manner to allow for corrective action to be taken.	3

Overall reflections/conclusion on the governance framework based on internal control deficiencies

10. With the implementation of the Standards of GRAP, the municipality experienced difficulties in producing financial statements for audit purposes that were free from errors and omissions, although not in all instances material.

This is indicative of a situation where:

- ongoing monitoring by the finance department is not effective enough to assess the effectiveness of internal control over financial reporting
- policies and procedures related to financial reporting, which aim to improve the quality of reconciliations and maintenance and availability of underlying records and, therefore, the accuracy and completeness of financial reporting, are not adequately established and communicated to staff in the finance department
- management did not adequately identify risks relevant to accurate and complete financial reporting and actions were not taken to address such risks. These risks should be identified by way of a formal risk assessment process relating to the achievement of financial reporting objectives and/or by implementing a formal and regularly monitored financial management improvement plan, which includes actions to address not only the material findings arising from the prior year's external audit, but also the control and compliance deficiencies identified in that audit. The risk assessment process should inform the agendas of the audit committee and internal audit unit, which are essential elements in the review of the design and implementation of sound internal controls to achieve good governance and accountability over financial reporting.

An action plan was not implemented by management to address the findings raised by the external auditors during the prior year and consequently a number of prior year audit findings reoccurred.

This situation could have led to the qualification of the financial statements had the municipality not adjusted their financial statements during the audit, based on my findings.

The next few years will pose greater challenges for the municipality with the ongoing transition to full compliance with the Standards of GRAP and the implementation of additional, approved Standards of GRAP. In order to deal with the prevalence of material misstatements in financial statements that have to be corrected during the audit, the municipality needs to:

- develop a strategy to improve financial management controls relating to compliance with accounting standards and reconciliation and maintenance of underlying accounting records, in order to produce accurate and complete financial statements
- produce monthly or, at a minimum, quarterly financial accounts for review by management
- subject the financial statements to a quality review before they are submitted for auditing, while the internal audit unit and audit committee can assist with

evaluating the adequacy of the design and implementation of controls around the preparation of the financial statements.

Funding of operations/Financial sustainability/Going concern

11. No findings

Qualitative aspects of accounting practices

12. Eden District Municipality prepared its financial statements according to Standards of GRAP in the period under review. There were no exemptions to the applicable basis of accounting granted by National Treasury. The municipality has adopted a phased-in approach in order to fully comply with the requirements of GRAP. As such, the municipality has applied the following exemptions under the Accounting Standards Board's *Directive 4 – Transitional Provisions for Medium and Low Capacity Municipalities*:

- *GRAP 12 – Inventories*: Inventories of water and land held for sale were not recognised.
- *GRAP 16 - Investment properties*: The municipality did not recognise all its investment properties.
- *GRAP 17 - Property, plant and equipment*: The municipality did not measure infrastructure and community assets and other property plant and equipment in accordance with GRAP 17.
- *GRAP 19 – Provisions, contingent liabilities and contingent assets*: The municipality did not value the provision for refuse tip-sites.
- *GRAP 100 – Non-current assets and discontinued operations*: The municipality did not recognise non-current assets held for sale and discontinued operations.
- *GRAP 102 – Intangible assets*: The municipality did not recognise or measure computer software and intangible assets.

Material losses/impairments

13. No findings.

Unauthorised/fruitless and wasteful/irregular expenditure

14. During the year under review unauthorised expenditure was incurred as a result of the municipality overspending its approved budget on the following votes:

• Executive and Council	R35 466 051
• Waste Water Management	R538 556
• Water	R306 919
• Roads	R13 660 529
TOTAL	R49 972 055

An employee of the municipality was dismissed during the year for not performing his duties in terms of the applicable rules and regulations. This resulted in the municipality incurring fruitless and wasteful expenditure of R404 515 due to the employee's negligence.

During the year the municipality incurred irregular expenditure of R57 500 as a result of fraudulent actions by one of its employees. Adequate disclosure of this amount has been included in the financial statements.

Our sample testing identified no other cases of unauthorised, fruitless and wasteful or irregular expenditure.

These matters will be included in the audit report under emphasis of matter.

Budgetary control

15. The Eden District Municipality budgeted for a loss of R38 938 677 during the current year. From a governance point of view, it would not be prudent for a municipality to budget for a loss as it would be over-committing itself, and would not be complying with the provisions of section 18 of the MFMA.

This matter will be included in the audit report under other matters.

Accounting discipline

16. No findings.

Financial indicators/ratios

17. No findings.

Financial reporting systems

18. No findings.

Revision of the previously issued financial statements

19. Amendments to the previous year's financial statements have been disclosed in note 33 to the annual financial statements.

This matter will be included in the audit report under emphasis of matter.

Accounting reforms

20. During the 2008/09 financial year, Eden District Municipality adopted the Standards of GRAP, except for the transitional provisions allowed in terms of Directive 4 of the Accounting Standards as discussed above.

It is the intention of Eden District Municipality to fully comply with the requirements of GRAP for the preparation of the 2011 financial statements.

GOVERNANCE MATTERS

Material inconsistencies in other information included in the annual report

21. The annual report has not been received at the date of submission of this draft management report. As such, the annual report could not be reviewed for material inconsistencies.

Internal audit

22. Although the municipality has an internal audit department, its work could not be considered to reduce the extent of the external audit for the following reasons:

- No internal audit reports are available for the current year.
- The internal audit charter and internal audit plan has not been authorised and approved by the audit committee.
- The internal audit charter does not stipulate that the head of internal audit should be approved by the audit committee.

This will be included in the audit report under other matters.

Audit committee

23. The municipality did not have a functional audit committee during the year under review. Consequently, the committee did not exercise any oversight role over the affairs of the municipality.

This will be included in the audit report under other matters.

Management of risk

24. The municipality has not undertaken a risk assessment to assess any risks of fraud and has consequently not developed a fraud prevention plan, as required by section 62(1)(c)(i) of the MFMA.

Prior year observations and recommendations addressed

25. A number of findings, especially those relating to matters affecting the audit report and performance information have also been reported in the prior year. The municipality did not prepare an action plan to address the external audit findings for the 2007-08 financial year and to monitor progress on resolving these matters.

Unavailability of key personnel

26. Unavailability of key personnel was a consistent issue throughout the audit. The following were the major issues:

- Key officials were either on leave or attending training interventions during the audit.
- The municipal manager was suspended during the audit
- The acting CFO was replaced during the audit

Adequacy and competence of financial reporting personnel

27. There is an urgent need to appoint a permanent Chief Financial Officer with the appropriate skills and experience. With the adoption of the GRAP accounting standards it is imperative that this person have adequate knowledge of these standards.

Currently, the municipality has to employ consultants to prepare the financial statements submitted for auditing. Mubesko Africa, in conjunction with Meyer Otto, was appointed as consultants. For the period 1 July 2008 to date an amount of approximately R603 000 was paid to the consultants, with a total contract amount of R1,5 million over two years. These consultants were responsible for certain underlying reconciliations, prior to the preparation of the AFS. In an effort to transfer knowledge, the consultants requested the municipality to prepare all underlying records in GRAP format. Regular meetings are held with municipal staff to ensure compliance with this.

Unavailability of expected information

28. As indicated in our engagement letter, we agreed that all information requested for the purposes of the audit would be submitted within two working days of the request by the auditors. Although the requests were answered in the agreed upon timeframe it still resulted in significant additional audit effort as it was expected of us to search for the requested documents.

Late submission of financial statements

29. The 2008/09 financial statements were submitted on time in accordance with section 126(1)(a) of the Municipal Finance Management Act. The performance information has not been submitted to the Auditor-General.

Related parties

30. The municipality has not implemented adequate controls to:

- identify, account for and disclose related party relationships and transactions in accordance with the Standards of Generally Recognised Accounting Practices
- authorise and approve significant transactions and arrangements with related parties.

Performance rewards

31. The municipality awarded performance bonuses to senior staff for the year ended 30 June 2009. In terms of section 57 of the Municipal Systems Act such bonuses can only be awarded to municipal manager and managers directly accountable to him after an evaluation of performance and approval by the council.

Non-compliance with applicable legislation

32. The following significant non-compliance with applicable legislation has been identified :

- The municipality has not compiled a risk management policy as required by section 62 of the MFMA.
- Non-compliance with the supply chain management guide and section 116 of the MFMA.

- Non-compliance with section 57(4)(b) of the Municipal Systems Act (MSA) relating to quarterly periodic assessments.
- Audit committee not established as required by section 166(1) of the MFMA.
- Internal audit function not operation as required by section 165(2) of the MFMA.

SCOPA / Oversight resolutions

33. During the current year the municipality established an oversight committee. The mandate of this committee is to report to council on whether to accept or reject the annual report.

Key governance responsibilities

34. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Many of these have been addressed in detail above. The table below reflects how certain of the financial and governance matters as well as other matters included under the reporting on performance information below, will be reported in the auditor's report.

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. 		■

No.	Matter	Y	N
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)(i) 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.	SCOPA resolutions have been substantially implemented.	n/a	
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 Eden District Municipality against its mandate, predetermined objectives, outputs, indicators and targets [section 68 of the MFMA].	■	
18.	There is a functioning performance management system and performance bonuses are only paid after proper assessment and approval by those charged with governance.		■

The above table will be included in the audit report under other matters.

Achievement of good practice indicators

35. The following good practices are the drivers of audit results. We have indicated our assessment of the municipality's achievement of these good practices, based on the matters included elsewhere in this report.

	Good practice	Y	N
1	Clear trail of supporting documentation that is easily available and provided timeously.		■
2	Quality of financial statements and related management information.		■
3	Timeliness of financial statements and management information.	■	
4	Availability of key officials during audits.		■
5	Development and compliance with risk management and good internal control and governance practices.		■
6	Leadership/supervision and monitoring.		■

36. While the municipality has submitted its financial statements on time, challenges still remain to ensure that they are free from material errors and omissions before submission for audit purposes. There were mostly lapses in monitoring (policies related to reliable financial reporting are not established and communicated throughout the entity, and do not have corresponding procedures that result in management directives being carried out) as indicated in more detail in paragraph 10.

Although the municipality had established an outsourced internal audit unit, the absence of an audit committee resulted in no internal audit reports being issued during the 2008-09 financial year. The internal audit charter and annual audit plan was also not approved.

The municipality did not have a functional audit committee for the 2008-09 financial year as required by section 166 of the MFMA as the council was in the process of reviewing the composition of the audit committee. The audit committee charter was also not approved.

Most findings relating to the financial statements arose as a result of non-compliance with risk management and good internal control and governance practices. The establishment of a functional internal audit unit, under the control of an active audit committee, would therefore contribute in identifying deficiencies in the design and implementation of internal controls and governance practices in the municipality. Adequate capacity and stability in the finance department, especially at the position of chief financial officer, must be established to also address the internal control and governance deficiencies and to reduce the municipality's dependency on consultants.

Other findings contained in Annexure B to this management report are also indicative of non-compliance with risk management and good internal control and governance practices and can mostly be attributed to lapses in monitoring.

The development of a performance management system that facilitates the preparation of a performance report that is accurate and complete and available for internal and external review in a timely manner, requires urgent attention from the accounting officer with the support of internal audit and the audit committee to ensure compliance with section 40 of the MSA.

SIGNIFICANT FINDINGS FROM OUR REVIEW OF THE PERFORMANCE INFORMATION

37. The following shortcomings were identified in relation to the managing of, and reporting on, performance information

- No internal audit was performed on the results of performance measurements and, consequently there are no quarterly audit reports on performance measurement compiled by the internal audit function.
- The current year Integrated Development Plan does not reflect the performance targets or the key performance indicators as prescribed by the Municipal Systems Act.
- Although the municipality does have a performance review policy in place, it has not been approved and implemented.
- Performance information was not received for audit purposes.

RATINGS OF DETAILED AUDIT FINDINGS

38. For the purposes of this report, the detailed audit findings included in annexures A to C have been classified as follows:

- Matters to be included in the auditor's report.

These matters should be addressed as a matter of urgency.

- Other important matters – deficiencies that could adversely affect the entity's ability to initiate, record, process and report financial data consistent with the assertions of management on the financial statements and in accordance with the applicable basis of accounting. Unacceptable risk that errors and irregularities may occur that will not be prevented or detected by the internal controls in good time.

These matters should be addressed within the next 12 months.

- Administrative matters – non-material non-compliance with applicable legislation, or misstatements in the financial statements that are unlikely to affect the decisions of a user and do not affect the financial statements as a whole, or opportunities for improvement, or other matters of governance interest.

These matters should be addressed at the discretion of the entity.

Failure to address matters reported in a particular category may result in the matter being rated as more significant in the next financial year.

APPRECIATION

39. We would like to express our appreciation for the courtesy extended and assistance rendered by the staff of the Eden District Municipality during the audit.

Yours sincerely

Liezl Klue-Knipe
Senior Manager

Enquiries

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CFO
Audit Committee Chairperson

SUMMARY OF AUDIT FINDINGS

Page no.	Finding	Type of finding	Control component	Impact on auditor's report			Other important matters	Administrative matters	In which years was it reported		
				Qualification	Other matters	Performance information			2007-08	2006-07	2005-06
19	A.1. Supply chain management	Non-Compliance	Control activities Monitoring		■				■	■	
21	A.2. Integrated Development Plan	Performance information	Control activities Monitoring			■			■	■	
22	A.3. Quarterly assessment of section 57 employees	Non-compliance	Control activities Monitoring		■						
23	A.4. Key performance indicators	Performance information	Control activities Monitoring			■				■	
24	A.5. Performance management system	Performance information	Control activities Monitoring						■	■	■
26	A.6. Internal audit	Control deficiency	Control activities Monitoring		■						
27	A.7. Internal audit charter and internal annual audit plan	Control deficiency	Control activities Monitoring		■						
28	A.8. Appointment and dismissal of the head of internal audit	Control deficiency	Control activities Monitoring		■						

Page no.	Finding	Type of finding	Control component	Impact on auditor's report			Other important matters	Administrative matters	In which years was it reported		
				Qualification	Other matters	Performance information			2007-08	2006-07	2005-06
29	A.9. Audit committee	Control deficiency	Control activities Monitoring		■			■			
30	A.10. Audit committee charter	Control deficiency	Control activities Monitoring		■						
31	A.11. Risk management	Control deficiency	Control activities Monitoring		■			■	■	■	
32	A.12. Fraud prevention plan	Control deficiency	Control activities Monitoring		■				■		
33	A.13. Budgeting for a loss	Non-Compliance	Control activities Monitoring		■						
35	A.14 Key performance indicators	Performance Information	Control activities Monitoring			■					
37	B.1. Irregular and fruitless and wasteful expenditure	Financial	Control activities Monitoring				■	■	■		
39	B.2. Overtime authorisation	Control deficiency	Control activities				■				
41	B.3. Leave approval	Control deficiency	Control activities				■				

Page no.	Finding	Type of finding	Control component	Impact on auditor's report			Other important matters	Administrative matters	In which years was it reported		
				Qualification	Other matters	Performance information			2007-08	2006-07	2005-06
43	B.4. Leave gratuity	Financial	Control activities Monitoring				■				
44	B.5. Classification of assets	Financial	Control activities Monitoring				■				
46	B.6. Existence of trade receivables	Control deficiency	Control activities				■				
48	B.7. Estimates	Non-Compliance Financial	Control activities Monitoring				■				
49	B.8. Authorisation for obtaining quotes	Non-Compliance	Control activities Monitoring				■				
50	B.9. Offsetting of income and expenses	Financial	Control activities Monitoring				■				
51	B.10. Inventory issues	Financial	Control activities Monitoring				■				
52	B.11. Slow moving inventory	Financial	Control activities Monitoring				■				
53	B.12. Inventory adjustment	Financial	Control activities Monitoring				■				

Page no.	Finding	Type of finding	Control component	Impact on auditor's report			Other important matters	Administrative matters	In which years was it reported		
				Qualification	Other matters	Performance information			2007-08	2006-07	2005-06
54	B.13. Current portion of long term liabilities	Financial	Control activities Monitoring				■				
55	B.14. Distribution losses	Financial	Control activities Monitoring				■				
56	B.15. Credit control policy	Control deficiency	Control activities Monitoring				■	■			
57	B.16. Bad debts write-off policy	Control deficiency	Control activities Monitoring				■		■		
58	B.17. Government departments and other public body receivables	Control deficiency	Control activities Monitoring				■				
59	B.18. Budget information	Financial	Monitoring				■				
60	B.19. Government department receivables	Control deficiency	Control activities Monitoring				■				
61	B.20. Insurance proceeds	Control deficiency	Control activities Monitoring				■				
63	B.21. Details of assets	Control deficiency	Control activities Monitoring				■				

Page no.	Finding	Type of finding	Control component	Impact on auditor's report			Other important matters	Administrative matters	In which years was it reported		
				Qualification	Other matters	Performance information			2007-08	2006-07	2005-06
65	B.22 Creditors	Control deficiency	Control activities Monitoring				■				
68	B.23. Unspent conditional grants	Non Compliance Control deficiency	Control activities Monitoring				■				
69	B.24. Prepaid electricity	Non Compliance Control deficiency	Control activities Monitoring				■				
70	B.25. Tariffs for rental property	Control deficiency	Control activities				■				
71	C.1. Unidentified receipts	Control deficiency	Control activities Monitoring					■			
72	C.2. Returned cheques	Control deficiency	Control activities Monitoring					■			

ANNEXURE A: MATTERS AFFECTING THE AUDITOR'S REPORT

A.1. Supply chain management

Audit Finding

Section 116 of the Municipal Finance Management Act, 56 of 2003 states:

- "(1) A contract or agreement procured through the supply chain management must*
- (a) be in writing*
 - (b) stipulate the terms and conditions of the contract or agreement, which must include provisions for providing for -*
 - (i) the termination of the contract or agreement in the case of non- or under-performance;*
 - (ii) dispute resolution mechanisms to settle disputes between the parties*
 - (iii) a periodic review of the contract or agreement once every three years in the case of a contract or agreement for longer than three years; and*
 - (iv) any other matters that may be prescribed."*

The above matter is also mentioned in the supply chain management guide for municipalities from National Treasury which states:

"After approval of a bid, both parties should sign a written contract or, if necessary, a service level agreement. Original/legal copies should be kept in a secure place for judicial reference."

No formal contract between the municipality and the successful bidder could be found for the following contract awarded during the current year:

Tender number	Description	Amount (R)
E/13/08/09	Installation of waterless toilets and construction of brick toilet top structures	176 472.00

Root cause

Ongoing monitoring and supervision are not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Risk

- (i) Non-compliance with section 116 of the Municipal Finance Management Act, which requires contracts or agreements in writing between the municipality and the successful bidder.
- (ii) In addition, the municipality could incur losses due to no contract in place should the successful bidder not deliver and this could lead to fruitless and wasteful expenditure.

Recommendation

Management should ensure compliance with all applicable laws and regulations.

Management response

There was no formal contract between the municipality and the contractor for the installation of waterless toilets and construction of brick toilet. The legal advisor is in the process of compiling a standardised contract to be used for all formal tenders awarded from July 2009.

A.2. Integrated Development Plan

Audit Finding

Section 26(h) of the Municipal Systems Act, No 32 of 2000 (MSA) requires that the integrated development plan (IDP) must reflect a financial plan. Such a plan must include a budget projection for at least the next three years.

The 2008/09 IDP prepared by the municipality only reflects a budget projection for the 2009/10 financial year.

Root cause

- (i) The requirements of the MSA were not fully complied with in the preparation of the IDP.
- (ii) *Reporting deficiencies* – Internal control deficiencies are not identified and communicated in a timely manner to those parties responsible for taking corrective action, and to management and the accounting officer/authority as appropriate.

Risk

The IDP is not in compliance with applicable legislation.

Recommendation

The IDP prepared for all future years must include a budget projection for at least the next three years.

Management response

The IDP prepared for all future years will include a budget projection for at least the next three years. Eden's annual budget is drafted for a three year period although the budget for the financial year of the IDP review is only included in the IDP review documents. The recommendation will be adhered to.

Name: K Nieuwoudt
Position: Acting Manager Strategic Services
Date: 30 October 2009

A.3. Quarterly assessment of section 57 employees

Audit Finding

The terms and conditions relating to the individual employment contracts include a provision that quarterly periodic assessments be performed for all MSA section 57 municipality employees for the purposes of calculating their performance bonuses. However, per enquiry and inspection of the section 57 employee files, no proof exists that such quarterly assessments were performed during the current year.

Root cause

- (i) The municipal council has adopted and approved a formula based assessment for the calculation of performance bonuses, which contravenes the method proposed and stipulated as per section 57(4)(b) of the MSA.
- (ii) *Performance measurement and reward* – Realistic targets are not set for performance measurement and this, in turn, is not linked to an effective performance reward system.

Risk

Performance bonuses are not calculated in terms of the MSA which will result in the municipality calculating and paying out performance bonuses that do not comply with applicable legislation.

Recommendation

Performance bonuses for such employees should be calculated in accordance with section 57 of the MSA. This would mean that the municipality must develop a system which would ensure that section 57 employees be subjected to a quarterly periodic assessment.

Management response

I am not in agreement with the finding, the recommendation are adhere to.

Name: K Nieuwoudt

Position: Acting Manager Strategic Services

Date: 2 November 2009

Further management response : Performance bonuses for section 57 employees will be calculated in accordance with section 57 of the MSA. The municipality will develop a system which will ensure that section 57 employees be subjected to a quarterly period assessment.

For the 2008/09 financial year an external service provider was used to draft the performance contracts of section 57 employees. Performance contracts of section 57 employees for 2009/10 was drafted in-house and in accordance with the five National key performance areas.

Auditor's response

The process for 2008-09 was therefore not in corrected dealt with.

A.4. Key performance indicators

Audit Finding

Section 26(i) of the MSA states that “*an integrated development plan must reflect the key performance indicators and performance targets determined in terms of section 41.*”

The 2008/09 IDP does not reflect the performance targets or the key performance indicators as prescribed by the MSA.

Root cause

- (i) The requirements of the MSA were not fully complied with in the preparation of the IDP.
- (ii) *Reporting deficiencies* – Internal control deficiencies are not identified and communicated in a timely manner to those parties responsible for taking corrective action, and to management and the accounting officer/authority as appropriate.

Risk

The IDP is not in compliance with applicable legislation.

Recommendation

The IDP prepared for all future years must include the key performance indicators and the municipality’s performance targets.

Management response

The recommendation will be adhered to.

Name: K Nieuwoudt

Position: Acting: Manager Strategic Services

Date: 30 October 2009

A.5. Performance management system

Audit finding

Section 38 of the Municipal Systems Act No. 32 of 2000 (MSA) states that *“a municipality must-*

- (a) establish a performance management system that is –*
 - (i) commensurate with its resources;*
 - (ii) best suited to its performance; and*
 - (iii) in line with the priorities, objectives, indicators, and targets contained in its integrated development plan.”*

In terms of section 40 of this Act *“the municipality must establish mechanisms to monitor and review its performance management system”*.

Section 41(1)(c) prescribes that the municipality must, in terms of its performance management system, monitor performance against key performance indicators and targets set and measure and review performance at least once per year.

Section 45 of this Act further provides that *“the results of performance measurements must be audited-*

- (a) as part of municipality's internal auditing processes; and*
- (b) annually by the Auditor-General”*.

In terms of Municipal Planning and Performance Management Regulations, 2001, regulation 14, audit reports on performance measurement should be prepared on a quarterly basis by internal audit.

- (i) No internal audit was performed on the results of performance measurements and, consequently there are no quarterly audit reports on performance measurement compiled by the internal audit function.
- (ii) Although the municipality does have a performance review policy in place, it has not been approved and implemented.
- (iii) Performance information was not submitted with the annual financial statements on 31 August 2009 to the Auditor-General.

Root Cause

Ongoing monitoring -Ongoing monitoring and supervision is not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Management did not comply with the Municipality Systems Act.

Risk

There is a risk that the adequacy, reliability and accuracy of performance information may not be appropriately monitored.

Recommendation

Internal audit should audit results of performance measurement to ensure compliance to applicable laws and regulations

Management response

- (1) There was no internal audit performed on the results of performance measurements.

This matter will receive the necessary attention as soon as the new internal auditor has been appointed.
- (2) The municipality does have a performance review policy but it has not been approved.

This matter is in process and will soon be finalised.
- (3) A Request for extension has been granted until the 30 October 2009. See letter attached.

Auditor's Response

Management response noted. The letter referred to merely requests extension. No evidence has been provided that approval was granted for the request.

In terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000), the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality. Section 45 of the Municipal Systems Act, 2000 furthermore states that the results of performance measurements must be audited annually by the Auditor-General. To enable the Auditor-General to annually audit the performance information that will be included in the municipality's annual report and issue an audit report, it is critical that such performance information is submitted for auditing with the annual financial statements on 31 August.

A.6. Internal audit

Audit finding

Section 165(1) of the Municipal Finance Management Act No 56 of 2003 (MFMA) states “each municipality must have an internal audit unit.

- (2) *The internal audit unit of a municipality must-*
- (a) *prepare a risk-based audit plan and an internal audit program for each financial year*
 - (b) *advise the, accounting officer and report to the audit committee on the implementation of the internal audit report...”.*

Although the municipality does have an outsourced internal audit unit, no evidence is available, including internal audit reports, to substantiate that it was operating in the manner prescribed by the MFMA during the financial year under review.

Root Cause

Ongoing monitoring of internal control should be built into the normal, recurring operating activities of an entity. It includes regular management and supervisory activities, and other actions personnel take in performing their duties.

Risk

There is a risk that the adequacy, reliability and accuracy of financial reporting and performance information may not be appropriately monitored.

Recommendation

Management should ensure that an Internal audit unit is functional and operating effectively thereby complying with all applicable laws and regulations.

Management response

There was no internal audit report for the 2008/2009 financial year. The first report was submitted on the 28th of August 2009.

A.7. Internal audit charter and internal annual audit plan

Audit finding

The internal audit charter and the internal annual audit plan have not been signed as being authorised or approved by the head of internal audit, municipal manager, audit committee chairperson or executive mayor.

Root Cause

Ongoing monitoring of internal controls should be built in terms of normal, recurring activities of an entity. It includes regular management and supervisory activities and other actions personnel take in performing their duties.

Risk

Non-compliance with the applicable laws and regulations by management of the entity.

Recommendation

The Internal Audit Charter and Internal Annual Audit Plan should be signed as being authorised and approved by the relevant personnel.

Management response

The internal audit charter is still in draft form, as soon as it has been finalised it will be authorised by the relevant authorities.

A.8. Appointment and dismissal of the head of internal audit

Audit finding

The internal audit charter does not stipulate that the appointment or dismissal of the head of internal audit should be approved by the audit committee.

Root Cause

Monitoring - Ongoing monitoring

Ongoing monitoring and supervision are not undertaken to enable management to determine whether the internal audit charter meets all the requirements as per the applicable standards.

Risk

Non-compliance with the Standards for the Professional Practice of Internal Auditing, which sets out the minimum requirements of an Internal Audit Charter.

Recommendation

The Internal Audit Charter should be amended to include the requirement that the appointment or dismissal of the Head of Internal Audit must be concurred by the audit committee.

Management response

Appointment and dismissal procedures are not stipulated in the internal audit charter. With the next review this matter will received the necessary attention.

A.9. Audit committee

Audit finding

Section 166(1) of the MFMA states “*each municipality must have an audit committee.*”

There was no audit committee appointed for the financial year under review at the municipality.

Root Cause

- (i) The management did not comply with the applicable laws and regulations.
- (ii) *Policies and procedures:* Policies related to reliable financial reporting are not established and communicated throughout the company, and do not have corresponding procedures which result in management directives being carried out.

Risk

There is a risk that the adequacy, reliability and accuracy of financial reporting information may not be appropriately monitored.

Recommendation

Management should ensure that an Audit committee is functional and operating effectively thereby complying with all applicable laws and regulations.

Management response

There is still a audit committee but it was not very active during the 2008/2009 financial year. See council resolution (5/6/2/7) dated 23 March 2009 for the continuation of the existing audit committee.

Auditor’s response

The previous audit committee’s appointment expired on 30 June 2008 and was not renewed until 23 March 2009.

A.10. Audit committee charter

Audit finding

The audit committee charter has not been signed as being authorised or approved by the head of internal audit, municipal manager, audit committee chairperson or executive mayor.

Root Cause

Ongoing monitoring -Ongoing monitoring and supervision is not undertaken to enable management to determine whether internal controls are in place to ensure that the audit committee is present and functioning effectively.

Risk

Non-compliance with the applicable laws and regulations by management of the entity. Possible risk that the audit committee may not function effectively.

Recommendation

Management should make sure that the Audit Committee Charter is signed and approved by the Head of Internal Audit, Municipal Manager, Audit committee chairperson or executive Mayor.

Management response

The audit committee charter will be properly signed and approve by the relevant authorities.

A.11. Risk management

Audit finding

The municipality does not have a risk committee or a risk management policy in place to identify risks to the municipality.

Root Cause

Control Environment – Organisational structure

The entity's organisational structure does not address areas of responsibility and establish lines of reporting in order to support effective risk management.

Risk

The absence of a Risk Management Policy may result in risks not being detected, or responded to timeously and in the most effective manner by the municipality.

Recommendation

Management should form a Risk Committee as well as develop and implement an effective Risk Management Policy.

Management response

The management committee fulfil the tasks of the risk committee. The risk management policy form part of the Risk Management Strategy which has been already submitted to the auditors. A dedicated risk assessment was done by IA Professional Placements. This assessment was work-shopped in detail by the Mancom (Ref MANCOM 16/09/09), refer the action plans which was submitted to the Audit Committee on 28/09/2009. However the lack of a Risk Management Policy was identified and corrective action plans will be put in place.

Auditor's response

We have received no evidence to support the fact that the management committee fulfils the tasks of the risk committee. The risk assessment was also completed after year-end and therefore not applicable to the 2008-09 financial year.

A.12. Fraud prevention plan

Audit finding

A fraud prevention plan has neither been developed nor implemented to prevent and detect fraud during the 2008/09 financial year. This finding was also raised during the 2007/2008 audit.

Root Cause

Fraud risk – The potential for material misstatement due to fraud is not explicitly considered in assessing risks to the achievement of the financial reporting objectives.

Risk

The absence of a fraud prevention plan could result in the late or non detection of fraud, which could lead to financial loss to the municipality.

Recommendation

A fraud prevention plan must be developed by the municipality to prevent and detect fraud.

Management response

A Fraud prevention plan has been finalised during August 2009. The plan has been submitted electronically.

Auditor's response

Fraud prevention plan was not available or implemented during financial year under review. Therefore, audit finding not resolved.

A.13. Budgeting for a loss

Audit Finding

Section 18 of the MFMA states:

- “(1) *An annual budget may only be funded from*
- (a) realistically anticipated revenues to be collected;*
 - (b) cash-backed accumulated funds from previous years’ surpluses not committed for other purposes; and*
 - (c) borrowed funds, but only for the capital budget referred to in section 17(2).*
- (2) *Revenue projections in the budget must be realistic, taking into account*
- (a) projected revenue for the current year based on collection levels to date; and*
 - (b) actual revenue collected in previous financial years.”*

The current year budget included in Annexure E(1) reflects a net deficit for the year for the municipality.

Although nothing in the MFMA specifically addresses budgeting for a loss. From a governance point of view, it would not be prudent for a municipality to budget for a loss as it would be over-committing itself, and would not be complying with the provisions of section 18 above.

Furthermore, the budget was not prepared on the same basis on which the transactions are accounted for and the on which the annual financial statements are prepared.

Root cause

- (i) The budget was not prepared in the same format as the annual financial statements i.e. not in accordance with Generally Recognised Accounting Practice (GRAP).
- (ii) *Financial reporting information* – Pertinent information is not identified, captured, used at all levels of the company and distributed in a form and time frame that support the achievement of financial reporting objectives.

Risk

The prepared budget is not realistic or achievable and can not be used to monitor actual revenues and expenditures to budgeted figures.

Recommendation

The budget must be prepared in terms of GRAP so that it could be prepared in such a way that a deficit would not be budgeted for.

Management response

The budget reflected in the financial statements, are the first revised budget. At year end, transactions were processed to ensure GRAP compliancy. The first revised budget did not include all the GRAP transactions. A second revised budget was therefore prepared to align the budget with the financial statements. This revised budget was approved by council on the 29th of October 2009. This will be disclosed in the resubmitted financial statements. Refer to Appendix B for the council meeting minutes held on the 29th of October 2009.

Name: Louise Hoek
Position: Chief Accountant
Date: 5 November 2009

Auditor's response

The original budget for the 2008-09 financial year was, however, prepared with a net loss bottom line. This practice is not regarded as prudent. Therefore, audit finding not resolved.

Management response

Please note however that the budget was in fact cash funded as per MFMA requirements. If non-cash items (e.g. depreciation) are added back, the loss on the budget is in fact reversed.

A.14. Key performance indicators

Audit Finding

- a) Key performance indicators was only included in the SDBIP and was not included in the IDP.
- b) The following general key performance indicators have to be included in the IDP, according to Municipal Planning and Performance Management Regulations, regulation 10:

	General key performance indicators	
1	The percentage of households with access to basic level of water, sanitation, electricity and solid waste removal.	
2	The percentage of households earning less than R1100 per month with access to free basic services.	
3	The percentage of a municipality's capital budget actually spent on capital projects identified for a particular financial year in terms of the municipality's IDP.	
4	The number of jobs created through the municipality's local economic development initiatives including capital projects.	
5	The number of people from employment equity target groups employed in the three highest levels of management in compliance with a municipality's approved employment equity plan.	
6	The percentage of a municipality's budget actually spent on implementing its workplace skills plan.	
7	Financial viability as expressed by ratios	
	Debt coverage, where-	
	"A" represents debt coverage	
	"B" represents total operating revenue received	
	"C" represents operating grants	
	"D" represents debt service payments (i.e. interest + redemption) due within the financial year	
	Outstanding service debtors to revenue, where-	
	"A" represents outstanding service debtors to revenue	
	"B" represents total outstanding service debtors	
	"C" represents annual revenue actually received for services	
	Cost coverage, where-	
	"A" represents cost coverage	
	"B" represents all available cash at a particular time	
	"C" represents investments	
	"D" represents monthly fixed operating expenditure	

- c) In addition, the only reporting to the council relates to financial information i.e. income and expenditure.
- d) To date, request for information 19 was not submitted to the Auditor-General:

The following information is still outstanding in relation to the 2008/09 IDP:

- (i) Whether the local community given 21 days to comment on the draft IDP?
- (ii) Whether the municipality within 14 days of adoption of the IDP gave notice to the public that the IDP was adopted.
- (iii) Whether the municipal manager within 10 days of adoption of the IDP submitted a copy of the IDP to the MEC for local government in the province.
- (iv) Whether the community was involved in the setting up of the Key performance indicators.

Root cause

- a) Emphasis is placed on the reporting of the financial matters, as legislation regarding spending and overspending is strictly enforced.
- b) Information supplied by management to the auditors, in respect of RFI 19, was in respect of the 2009/2010 IDP.
- c) Policies related to reliable financial reporting are not established and communicated throughout the entity, and do not have corresponding procedures that result in management directives being carried out.

Risk

Non compliance with the Municipal Systems Act, which would result in service delivery achievements not being comparable between entities.

Recommendation

Proper reporting processes should be implemented to ensure that the municipality is able to comply with applicable regulations.

Management response

No management response was received.

ANNEXURE B: OTHER IMPORTANT MATTERS

B.1. Fruitless and wasteful expenditure

Audit Finding

During the year a project manager employed by the municipality was dismissed for being negligent in carrying out his duties as he behaved in a manner that was in breach of the rules and regulations of the Department of Water Affairs. Whilst inspecting the report of his disciplinary hearing it was noted that the following amounts could be considered as fruitless and wasteful expenditure:

Incident	R (excl. VAT)
Gross negligence in not complying with administrative procedure	87 505.50
PM did not comply with admin processes – no requisition or order issued prior to work being done. Risk to Council if DWAF refuse to allow payment	68 896.61
TOTAL	156 402.11

Root cause

- (i) Management might not be aware of what constitutes irregular expenditure.
- (ii) *Ongoing monitoring* - Ongoing monitoring and supervision are not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Risk

Fruitless and wasteful expenditure is possibly understated by R156 402.11.

Recommendation

Management should implement a process to identify irregular expenditure and develop a method to account for such expenditure in the annual financial statements.

Management response

- i) Fruitless Expenditure DWAF

The R87 505.50 was claimed from and paid by DWA.

The R183 113.36 remains a liability as the issue has not been addressed yet.

The incident has been reported to Dept. of Finance, John Samery, for insurance purposes.

- The R 68 896.61 has been claimed from and paid by DWA.
- The 65 000.00 was expended to rectify the damage caused

The final financial statements will be adjusted to ensure the R183 113.36 as well as the R65 000 are correctly disclosed as irregular fruitless and wasteful expenditure.

ii) The calculation error will be corrected in the final financial statements.

Irregular expenditure will be decreased with the said R32.500 relating to the ACVV expenses.

Auditor's response

The full amount of R404 515 is considered to be fruitless and wasteful expenditure and should have been disclosed as at year-end there was no clarity yet on the recoverability of the full amount. Only R248 113 was disclosed in the financial statements.

B.2. Overtime authorisation

Audit Finding

The municipality's overtime policy provides that overtime may only be worked subject to prior written approval by a competent authority.

However, no evidence of written approval for overtime was available on the files of the following employees who worked overtime during the financial year:

No	Name
1	JJ Jacobs
2	A Fourie
3	GG Frye
4	JC Wolmarans
5	EB Blauw
6	D van Wyk
7	M Nelani
8	L Levendal
9	W Young
10	WC Young
11	P Opperman
12	D Gous
13	J du Preez
14	MD Madikane
15	SM Van Zyl
16	GO Fortuin
17	W Booysen
18	JA Claasen
19	J Fortuin
20	JJM Josephs
21	J Jantjies
22	E Laws
23	KS Scheepers
24	A Terblanche
25	N Oosthuizen
26	G Smit
27	BJK Stander
28	DKF Krohn

Root cause

- (i) Employees responsible for authorising overtime payments are not complying with the municipality's overtime policy.
- (ii) *Operational* – Directive, preventive and detective controls are not adequate and focused on achieving efficient resource usage and effectiveness, as measured by the extent to which specific control objectives are achieved.

Risk

Overtime may be paid to employees who are not authorised to work overtime.

Recommendation

Personnel approving employee overtime payments should only do so after inspecting supporting documentation authorising the employee to work overtime.

Management response

Overtime approval must be approved prior by the employee's supervisor or line manager. When the employee works the overtime an overtime form is completed afterwards and then signed by the supervisor/line manager and the Manager of the Department. These forms are then submitted to the Salary Section if the employee prefers to have it paid out. If an employee prefer to take the time off instead, the completed form is attached to a leave form, indicated the period that the time off will be taken, signed by the supervisor/line manager and Manager of the department. This is then submitted to HR for filing on the employee's leave file.

Name: G Le Roux

Position: Deputy Manager: Human Resources

Date: 30 October 2009

Auditor's comments

Management comments noted. However this does not resolve the audit finding, since sufficient appropriate audit evidence is not available to verify that overtime was approved before it is worked.

B.3. Leave approval

Audit Finding

For the leave taken by the following employees during the current year, it was noted that the leave was taken before it was approved:

	Employee ID	Initials	Surname	Date from	Date to	Date of Approval
1	590927 5068 08 5	A	Terblanche	2008 07 29	2008 08 01	2008 08 29
2	500624 5047 08 1	J	Esau	2008 08 07	2008 08 07	2008 08 08
3	500421 5156 08 1	JJ	Benson	2008 07 02	2008 07 02	2008 07 03
4	670702 5631 08 0	M	Rhixana	2008 07 23	2008 07 24	2008 07 28
5	601112 5875 08 9	N	Blayi	2008 06 30	2008 07 01	2008 07 02
6	580714 5176 01 5	C	Stoffels	2008 07 16	2008 07 18	2008 07 21
7	610716 5742 08 8	M	Mpindwana	2008 09 16	2008 09 16	2008 09 17
8	710124 5228 08 4	MC	Kellies	2008 11 03	2008 11 03	2008 11 04

Root cause

Ongoing monitoring and supervision are not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Risk

Leave taken may not be timeously captured on PAYDAY or not captured at which could result in employees taking leave for which they have inadequate leave credits.

Recommendation

Leave applications should be forwarded to a central point and approved before the leave is taken by the employee and sent for capturing on the PAYDAY system.

Management response

The majority of employee's on the list took either family responsibility leave or sick leave. In order for family responsibility and sick leave to be approved the employee must present a doctors certificate and this is only issued on the date of examination. Employees also do not arrange their sick leave prior. they call in to notify the employer of their absence on that day. Subsequently, leave forms are completed when the employees return to work.

There is however three of the employees on the list that took annual leave. The leave procedures stipulate that annual leave must first be approved before an employee can take such leave. This requirement was not adhere to by the supervisors because employees might not be in a position to fill in the necessary forms and could therefore have telephonically requested leave.

Auditors comment

Management comments noted. However the leave information was taken from the data file for annual leave. The fact that management is stating that a different category of leave is within the sampling error is of a concern.

Please provide sufficient appropriate evidence that the leave categories were correctly classified on PAYDAY.

Management also did not provide the names or employee number of the 3 employees who leave was not approved before it was taken.

Since the 3 employees leave was not approved appropriately the audit finding is not resolved.

B.4. Leave gratuity

Audit Finding

The following employee's services were terminated during the current year. The leave gratuities payable to these employees on termination has been calculated incorrectly as follows:

Employee name	Month paid	Annual salary as per PayDay (R)	Monthly salary (R)	Leave days paid out	Leave value recalculated (R)	Leave value per PayDay (R)	Difference (R)
BOOYSEN TG	08-Jul	153 588	12 799	9	5 591	(172)	5 763
BAAIDJIES K	08-Aug	49 212	4 101	2	394		394
DE BOD D	08-Oct	48 024	4 002	2	384		384
RAMUKUMBA T	08-Dec	169 572	14 131	2	1 357		1 357
VAN RENSBURG C	09-Jan	49 212	4 101	6	1 181	1 088	94
					8 906	915	7 991

Root cause

- (i) There is no independent verification to ensure that the amounts as per the PayDay system are correctly calculated.
- (ii) *Organisational structure* - The entity's organisational structure does not adequately address areas of responsibility and establish lines of reporting in order to support effective internal control over financial reporting.

Risk

Leave gratuities is understated by of an amount R7 991.

Recommendation

A process must be developed to ensure that the leave gratuity paid out to employees on the termination of their services is calculated accurately.

Management response

I am not in agreement with the finding for the following reason. Proof that leave was paid out correctly is, attached. This matter was also clarified with Human Resources (Hailey Oktober) and discussed with the auditor.

Name Marisa Jacobsz
Position : Senior Accountant
Date: 19 November 2009

B.5. Classification of assets

Audit Finding

Section 63(2) of the MFMA states:

“The accounting officer must for the purposes of subsection (1) take all reasonable steps to ensure—

- (a) that the municipality has and maintains a management, accounting and information system that accounts for the assets and liabilities of the municipality;*
- (b) that the municipality’s assets and liabilities are valued in accordance with standards of generally recognised accounting practice; and*
- (c) that the municipality has and maintains a system of internal control of assets and liabilities, including an asset and liabilities register, as may be prescribed.*

The following items were recorded on the fixed asset register. Per enquiry of municipality staff it was confirmed that these items should have been expensed and not classified as assets as they do not meet the asset definition.

Description	Value per asset register (R)
Volleyball set	605.24
Monopoly games	789.42
Plasing van wapen op T-hempde	3 419.34
Sport toebehore	4 778.06
Sokkerkit	1 315.79
Sokkerballe	219.30
Truie	9 784.21
Shorts	964.91
Rugby togs	2 875.44
Duiksakke	2 803.51
Paal beskermers	2 016.67
Helmets	698.25
Bull boxes	52.63
Thigh pads	339.47
Team bags	786.84
W/keeper pads	873.68
W/keeper gloves	1 049.12
Oefen balle	210.53
Krieket kolwe	1 049.12
Wedstryd balle	368.42
TOTAL	34 999.95

Root cause

- (i) The incorrect vote number was used to record the acquisition of these items.
- (ii) *Ongoing monitoring* - Ongoing monitoring and supervision are not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Risk

Expenditure is understated by R34 999.95 and fixed assets are overstated by the same amount.

Recommendation

The financial statements should be amended to account for this incorrect classification.

Management response

This will be corrected when the financial statements for 2009/2010 are submitted.

Auditor's response

Statement of Financial Performance not amended to account for the error identified. Therefore, audit finding not resolved.

B.6. Existence of trade receivables

Audit Finding

The following trade receivables outstanding at year-end have either not made any repayments for a long time or have not made any repayments at all. It is, therefore, not possible to verify that these receivables actually exist.

No	Debtor	Debtor no	Amount (R)	Latest Repayment Amount (R)	Latest Repayment Date
1	J Matthews	201243	16 319.76	3 246.53	01/04/2004
2	K Coetzee	201404	14 442.33	80.18	23/06/2008
3	J Tarentaal	201474	25 190.62	72.74	26/06/2006
4	I H Kerspuy	202025	39 097.39	500.00	03/03/2009
5	C Fernol	201833	32 177.76	1 400.00	17/03/2008
6	M Grootboom	201706	43 141.99	1 000.00	09/09/2005
7	A P Blom	201549	23 940.65	1 476.00	01/04/2004
8	A van Aardt	201341	19 576.55	1 000.00	21/08/2007
9	L Prinsloo	201571	22 814.79	200.00	26/05/2004
10	C J Pietersen	5095	13 761.04	2 823.30	22/08/2005
11	N A Du Plessis	5102	23 894.01	49.24	05/06/2002
12	J Groenewald	5161	15 446.90	0.00	0
13	A Thyssen	5224	27 888.64	63.72	19/06/2009
14	I G van Jaarsveld	40012003	16 964.33	0.00	0
15	H H du Plessis	50018004	13 558.17	0.00	0
16	Chummy Truter Trust	50028001	21 515.56	0.00	0
17	Beyers Family Trust	50060022	12 204.51	0.00	0
18	Grootwal Boerdery	30119568	16 545.14	5 692.37	13/06/2003
19	J Buys	39000114	11 133.30	4 000.00	29/05/2008
20	C M Cumming	38100211	15 957.89	1 255.66	20/02/2001
21	M J Wolvaardt	37000670	50 359.26	0.00	0
			464 797.29		

Root cause

- (i) The municipality is not authorised to write off these receivables as it does not have an approved credit control policy.
- (ii) *Policies and procedures* – Policies related to reliable financial reporting are not established and communicated throughout the entity, and do not have corresponding procedures that result in management directives being carried out.

Risk

- (i) Although these receivables are not able to pay their outstanding balances, services to them cannot be terminated unless the credit policy has been approved. This will result in the municipality rendering services for which they will not receive any payment.
- (ii) It is difficult to prove that these receivables exist as they have been outstanding for a long time.

Recommendation

- (i) The municipality must ensure that the credit control policy is approved by council as soon as possible.
- (ii) The municipality must provide supporting evidence to prove that these amounts are owed to it as per the receivables age analysis.

Management response

A report is in a process to write off bad debts and to be served to the council for approval.

Name: J P Zeelie

Position: Asst. Director Finance

Date: 29 October 2009

B.7. Estimates

Audit Finding

Paragraph 2.2.3 of the CREDIT CONTROL, DEBT COLLECTION AND INDIGENT POLICY states *"should premises on which measuring mechanisms are installed be locked or for whatsoever reason be inaccessible to the official responsible for reading meters, the Municipality shall be entitled to render to the user an account based on the estimated use, as estimated by the Manager: Financial Services"*.

These estimates are not performed in a consistent manner. There is no set policy prescribed to calculate the estimate. Currently, the guideline being used is a three month average. However, it was noted that this method was not used for estimating the amount to be billed for all estimations. Instead, estimates were sometimes made using a three-month average as indicated in the guidelines and sometimes on an ad hoc basis.

Root cause

There is no set policy prescribed to calculate estimates.

Ongoing monitoring and supervision are not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Risk

Revenue and debtors may be misstated if estimates are not appropriately calculated.

Recommendation

Management should ensure a policy is in place ensuring estimates are appropriately calculated.

Management response

The council's credit control policy is in the process of reviewing. The calculation of estimations will be included in the revised credit control policy.

B.8. Authorisation for obtaining quotes

Audit Finding

According to the Supply Chain Policy, there are a number of individuals that are authorised to obtain quotes for purchasing purposes.

Although Mr. Mornè Stevens (IT department) is not one of those, his name appeared on a number of quotes that were sent to the municipality for IT purchases.

Root cause

Ongoing monitoring and supervision are not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Risk

This may lead to incorrect processes being followed in the process of obtaining the quotes.

Recommendation

Management should ensure that the Supply chain policy stipulations are adhered to at all times.

Management response

Any employee may obtain quotes for purchasing purposes.

Only employees with delegated power may sign requisitions and Order forms.

Auditor's response

The Supply chain management policy states that only certain individual are authorised to obtain quotes, yet the management response indicates that anybody can obtain quotes, which is non-compliance with the supply chain management policy.

Furthermore, during the audit the names of employees who are authorised to obtain quotes were requested. Mr Stevens was not one of the employees provided to audit who are authorised to obtain quotes.

B.9. Offsetting of income and expenses

Audit Finding

Paragraph 42 of GRAP 1 states that “Assets and liabilities, revenue and expenses, shall not be offset unless required or permitted by a Standard of GRAP.”

In the Statement of Financial Performance of Roads financial statements, expenses have been set off against the income.

The remaining balance is then referred to as Appropriation for the year.

Details are as follows:

Revenue		(R)
5 105 060	Allocation Indirect Account	6 749 109.65
		82 458 189.20
5 105 062	Normal Repair & Maintenance	53 835 490.61
5 105 063	Emergency Expenses	15 270 199.72
5 105 064	Re – Surfacing	8 344 193.11
5 105 065	Fencing	0.00
5 105 068	Road Signs	1 171 300.99
5 105 069	Minor Roads	3 369 980.19
5 105 071	Approved Capital Project	467 024.58

Expenditure		(R)
7135033	Allocation Indirect Account	(R6 749 110)
7135045	R5 CONTRA ACCOUNT	(R82 458 189)

Root cause

Non-compliance with the applicable GRAP standards.

Ongoing monitoring and supervision are not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Risk

Non-compliance with the applicable GRAP standards.

Recommendation

Management should ensure compliance to applicable GRAP standards.

Management response

See attached report from Mr Kobus Burger an employee of Mubesko Africa.

Auditor’s response

Audit cannot accept management response relating to the fact that IMFO is still applicable to the roads function as GRAP is the accounting framework for the municipality. As the net effect of this is zero, no further action will be taken.

B.10. Inventory issues

Audit Finding

Paragraph 43 of GRAP 12 *Inventories* states:

"When inventories are sold, exchanged or distributed the carrying amount of those inventories shall be recognised as an expense in the period in which the related revenue is recognised. If there is no related revenue, the expense is recognised when the goods are distributed, or related service is rendered."

Although the following inventory issues were made before year-end it was only recorded as an expense in the 2009/10 financial year:

No.	Descriptions	Stock no	Batch Date	Batch No.	Issue Date	Qty	Issue No.
1	Cement	01 - 2505	29-Jul-09	452	22-Jun-09	50	18475
2	Air Filter Tata	01 - 1159	29-Jul-09	453	24-Jun-09	1	17575
3	Hour Meters	01 - 2192A	29-Jul-09	453	29-Jun-09	1	17584
4	2 Piece Overall	01 - 2560	29-Jul-09	453	30-Jun-09	1	17588
5	Cement	01 - 2505	29-Jul-09	453	30-Jun-09	5	17593

Root cause

- (i) The system in place for recording inventory issues is not adequate to record such issues timeously.
- (ii) *Policies and procedures* – Policies related to reliable financial reporting are not established and communicated throughout the entity, and do not have corresponding procedures that result in management directives being carried out.

Risk

The cost of inventories issued is recorded in the incorrect period.

Recommendation

Management must implement a system of recording inventory issues that will ensure that such issues are recorded timeously.

Management response

Inventory issues on year end are updated and recorded timeously to reflect the correct inventory on hand. In future, I will personally make sure that the store man on year end records and updated all store inventories on year end and not in the new financial year.

Name: Jefferey Adams
Position: Assistant Manager: SCM & Store
Date: 6 November 2009

B.11. Slow moving inventory

Audit Finding

GRAP implementation guide for Inventory (GRAP 12) states the following:

"The individuals responsible for the stock take should identify slow moving and obsolete stock as well as stock that need to be impaired. "

Through discussion with management it was found that the municipality does have slow moving stock at year-end. However, value of this stock was not impaired in the preparation of the financial statements.

The municipality is in a process of identifying what is slow moving stock and only when the process is complete they will reclassify the relevant stock items. It is therefore no possible to establish the total value of such stock.

Root cause

- (i) Management is not aware of this requirement to value slow moving inventory at its impaired value.
- (ii) *Policies and procedures* - Policies related to reliable financial reporting are not established and communicated throughout the company, and do not have corresponding procedures which result in management directives being carried out.

Risk

Inventory at year end could be overstated in the financial statements.

Recommendation

Slow moving and obsolete inventory should be identified at the inventory count. This inventory should be valued at its impaired value in the financial statements.

Management response

I am not in agreement with the finding for the following reason: Stock losses are approved by council with the approval of the revised budget.

Auditor's response

Management's response indicates that it is an implied approval by Council and not an explicit approval by Council of stock losses. Council must specifically approve the stock losses presented to them.

B.12. Inventory adjustment

Audit Finding

Section 99(2) of the MFMA states:

“The accounting officer must for the purpose of subsection (1) take all reasonable steps to ensure: that the entity has and maintains an effective system of expenditure control including procedures for the approval, authorisation, withdrawal and payment of funds;...”

The municipality processed a journal (number E744) to account for inventory losses amounting to R156 692.21 during the year. This loss was accounted for in the adjustments budget and in the annual financial statements.

Neither the adjustments budget nor the inventory losses were approved by the council or the municipal manager respectively.

Root cause

- (i) Inventory losses are not appropriately approved.
- (ii) Policies related to reliable financial reporting are not established and communicated throughout the company, and do not have corresponding procedures which result in management directives being carried out.

Risk

- (i) The write-off of inventory losses without the required approval could lead to irregular expenditure.
- (ii) Inventory losses accounted for in the financial statements in excess of the approved budget could lead to unauthorised expenditure.

Recommendation

- (i) Management should ensure that inventory losses are appropriately approved before being written off.
- (ii) Management should take reasonable steps to ensure that inventory losses do not exceed the approved budget.

Management response

I am not in agreement with the finding for the following reason: Stock losses are approved by council with the approval of the revised budget.

Auditor’s response

Management’s response indicates that it is an implied approval by Council and not an explicit approval by Council of stock losses. Council must specifically approve the stock losses presented to them.

B.13. Current portion of long term liabilities

Audit Finding

Paragraph 71 of GRAP 1 *Presentation of Financial Statements* states:

"A liability shall be classified as current when it satisfies any of the following:

(c) it is due to be settled within twelve months after the reporting date..."

Upon inspection of Note 3 to the AFS the current portion relating to the following long-term loans is understated as follows.

Loan Type	Auditors Calculation (R)	AFS (R)	Difference (R)
Annuity Loan	519 992.14	255 587.92	264 404
			264 404

Root cause

- (i) The calculation of the current portion was calculated incorrectly.
- (ii) *Financial reporting information* – Pertinent information is not identified, captured, used at all levels of the company and distributed in a form and time frame that support the achievement of financial reporting objectives.

Risk

The amount recorded for the current portion of long-term liabilities is understated by R264 404 and the non-current portion is overstated by the same amount.

Recommendation

The AFS must be amended for the error identified.

Management response

The financial statements will be adjusted and include the amended current portion of long term liabilities.

Name: Louise Hoek
Position: Chief Accountant
Date: 05 November 2009

Auditor response

The financial statements were incorrectly adjusted for annuity loans. Audit finding not resolved.

B.14. Distribution losses

Audit Finding

The municipality did not calculate electricity distribution losses incurred during the year.

The Credit control and Debt collection policy has not been approved yet by the council, as a result EDEN Municipality is unable to monitor and investigate any distribution losses relating to electricity.

Expenditure is understated by the amount of distribution losses.

Root cause

- (i) The municipality does not have a process in place to calculate distribution losses.
- (ii) *Policies and procedures* - Policies related to reliable financial reporting are not established and communicated throughout the entity, and do not have corresponding procedures that result in management directives being carried out.

Risk

Expenditure in the financial statements is understated by the amount of these distribution losses not calculated.

Recommendation

Management should implement a process in order to calculate distribution losses.

Management response

I am not in agreement with the finding for the following reason: The calculation of distribution losses is available on the audit file.

Name. Johan Zeelie
Position. Asst Manager Finance
Date 18 November 2009

Auditor's response

This was not presented to the auditors when requested. The impact is, however, not material due to the fact that a district municipality does not primarily deliver basic services.

B.15. Credit control policy

Audit Finding

Although the municipality does have a credit control policy in place it has not yet been approved by council.

Root cause

- (i) The credit control policy has not yet been presented to council for approval.
- (ii) *Policies and procedures* – Policies related to reliable financial reporting are not established and communicated throughout the entity, and do not have corresponding procedures that result in management directives being carried out.

Risk

The effect of this is that services to non paying customers cannot be terminated. This will result in services being rendered without any realistic possibility of the municipality recovering the amounts billed from customers.

Recommendation

The credit control policy must be approved by council as soon as possible.

Management response

See the attached resolution DC 11/02/08 (Appendix B)

Name: JP Zeelie

Position: Asst. Director Finance

Date; 29 October 2009

Auditor's response

Credit policy was not in place or implemented during the financial year under review. Therefore, audit finding has to be reported for 2008/09.

B.16. Bad debts write-off policy

Audit Finding

The municipality does not have an approved bad debt write-off policy.

Root Cause

- i) There has been no approval for bad debt to be written off.
- ii) Ongoing monitoring and supervision are not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Risk

The debtors could be overstated as a portion relating to bad debt would not have been written off.

Recommendation

Management should ensure a bad debt policy is in place indicating the process to write off debtors when they become unlikely to be recoverable.

Management response

The council's credit control policy is in the process of reviewing. The policy on write offs will be included in the revised credit control policy.

B.17. Government departments and other public body receivables

Audit Finding

The municipality does not perform any reconciliations for amounts owing from government departments and other public bodies.

Root cause

- (i) The municipality is not aware of the requirement to perform reconciliations for these receivables.
- (ii) *Selection and development of control activities* – Control activities are not selected and developed with consideration of their cost and their potential effectiveness in mitigating risks to the achievement of financial reporting objectives.

Risk

It is not possible to verify that the amounts disclosed in the AFS as owing by government departments and public bodies to the municipality is accurate.

Recommendation

Reconciliations for all government department and other public body receivables must be performed and made available to the AG as soon as possible.

Management response

Full history detail of each debtor account is available on the ABAKUS financial system. The asst accountant (A Van Rensburg) is in contact with each department with outstanding debtor amounts.

Name: JP Zeelie

Position: Asst. Director Finance

Date: 2 November 2009

Auditor's response

A full history will not reflect any possible reconciling items. Therefore, audit finding not resolved.

B.18. Budget information

Audit Finding

The budget was not prepared in the same format as the annual financial statements i.e. not in accordance with Generally Recognised Accounting Practice (GRAP).

Root Cause

Budget is prepared as prescribed by the MFMA.

Risk

Non cash items will not be budgeted for or budgeted at all resulting in unauthorised expenditure being incurred.

Recommendation

Management should ensure that the budget was not prepared in the same format as the annual financial statements i.e. in accordance with Generally Recognised Accounting Practice (GRAP).

Management response

The new budget for 2009/10 will be prepared in accordance with GRAP.

Auditor's response

Management will only comply with this practice for the year ended 2009/10. Therefore, audit finding will be reported for 2008/09.

B.19. Government department receivables

Audit Finding

In terms of section 64(3) of the MFMA the municipality should report all organs of state to National Treasury in the event of them regularly having accounts older than 30 days. Even though the following government departments regularly have accounts older than 30 days, no such report was sent to National Treasury by the municipality:

No	Department Name	Amount outstanding for longer than 30 days (R)
1	Openbare Werke	219 695.29
2	Transport and Public Works	142 504.74
3	Rural Development and Land Reform	1 791.44
		363 991.47

Root cause

- (i) Government departments rarely pay the outstanding amounts as per their invoices. The balance due by them is usually disputed resulting in accounts being unpaid for longer than 30 days.
- (ii) *Ongoing monitoring* – Ongoing monitoring and supervision are not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Risk

Non-compliance with the provisions of the MFMA.

Recommendation

All government department debtors, whose accounts are in arrears for longer than 30 days, should be reported to National Treasury.

Management response

By default no reports was send to National Treasury in terms of the MFMA. The assistant director and assistant accountant are currently in correspondence with Department of Public works about the outstanding amounts and awaiting their payments. In future we will comply with the MFMA.

Name: Johan Zeelie
Position: Assistant Manager: Income & Expenditure
Date: 6 November 2009

B.20. Insurance Proceeds

Audit Finding

GRAP 17.74 *Property, Plant and Equipment* states:

“Compensation from third parties for items of property, plant and equipment that were impaired, lost or given up shall be included in surplus or deficit when the compensation becomes receivable.”

It has been noted that insurance proceeds amounting to R11 973.69 has been recognised in the Gain on Disposal account no. 1101018 7036001 in the current financial year.

These proceeds relate to an insurance claim received in 2007/08 which was submitted to the insurance companies in relation to a motor vehicle (CAW 53381).

The proceeds, from the insurance companies, were received in the 2007/2008 financial year for a motor vehicle, with registration no. CAW53381.

This motor vehicle was involved in an accident in the 2007/2008 financial year.

Management therefore made the following incorrect accounting entries:

- The insurance proceeds should not be recorded as a gain on disposal, but under other income as insurance proceeds.
- The insurance proceeds should be recorded in the 2007/2008 financial year as the proceeds were received in the 2007/2008 year.

Root cause

Ongoing monitoring and supervision are not undertaken to enable management to determine whether compliance to the relevant accounting standards is present and functioning.

Risk

- (i) Profit on sale of assets may be overstated and write off expenses understated.
- (ii) Gains from insurance proceeds may be recognised in the incorrect period thereby resulting in the gains on disposal account being overstated.

Recommendation

- (i) Management should ensure that the thefts of assets are appropriately accounted for in accordance with the applicable standards.
- (ii) Management should ensure that all transactions are accounted for in the correct period.

Management response

- i) The financial statements will be adjusted as follow:
 - Gains on disposal of assets will be decreased by R92,658
 - Insurance proceeds of R92,658 will be disclosed under other income
- ii) Noted.

Auditor's response

Adjustment partially made. The balance of the misstatements will be reflected as an unadjusted misstatement.

B.21. Details of assets

Audit Finding

Section 63(2) of the MFMA states:

“The accounting officer must for the purposes of subsection (1) take all reasonable steps to ensure—

- (a) *that the municipality has and maintains a management, accounting and information system that accounts for the assets and liabilities of the municipality;*
- (b) *that the municipality’s assets and liabilities are valued in accordance with standards of generally recognised accounting practice; and*
- (c) *that the municipality has and maintains a system of internal control of assets and liabilities, including an asset and liabilities register, as may be prescribed.”*

Whilst inspecting the supporting documentation for the following asset, it was discovered that the supporting documentation did not agree to the detail in the asset register for the following assets:

- (i) Tables

	Quantity	Unit cost (R)	Total (R)
As per register	37	917.48	33 946.76
Value should be recorded (per invoice)	37	437.00	16 169.00
Difference			17 777.76

- (ii) Chairs

	Quantity	Total (R)
As per asset register	386	17 301.57
Value should be recorded (per invoice)	386	33 929.00
Difference		16 627.43

Upon further investigation it was discovered that the amounts recorded on the fixed asset register because the values were incorrectly swapped around for these assets.

Root cause

- (i) Additions of fixed assets are updated to the asset register manually. Due to human error the incorrect details were entered on the fixed asset register.
- (ii) *Ongoing monitoring* - Ongoing monitoring and supervision are not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Risk

The fixed asset register is not accurate which would result in the fixed asset disclosure in the financial statements to be inaccurate.

Recommendation

Management should implement a system to ensure that accurate information is recorded and captured on the fixed asset register.

Management response

No management response received.

B.22. Creditors

Audit Finding

(a) The information per the detailed ledger for journal E115 does not agree to the supporting documentation for the journal.

As per the detailed ledger the information relating to journal E115 is as follows:

Trn	Transaction Description	Date	Reference	Pd	Debit	Credit	Narration
105	MAIN LEDGER JOURNAL	09/09/2008	E115	3		(R615.51)	TJ ED514843 AUG 08

As per journal E115's supporting documentation the detail is as follows:

Trn	Transaction Description	Date	Refer	Pd	Debit	Credit	Narration
	MAINLEDGER JOURNAL	30/09/2009	E115	3		(R42 710.92)	CORRECTI ONOFE85

(b) Section 65(2)(e) of the MFMA states:

"that all money owing by the municipality be paid within 30 days of receiving the relevant invoice or statement, unless prescribed otherwise for certain categories of expenditure"

The following payments were paid more than 30 days after receipt of the invoice:

NO	DATE	ORDER NUMBER	CREDI-TOR	POSTING NUMBER	GRV NUMBE R	AMOUNT (EXCL. VAT)	VAT	TOTAL
10	11/06/09	D0013711	Blitsdruk	10101850 38235	102391	R4 009	R561	R4 571
26	30/06/09	D0013819	Fujitsu Services	10120750 28002	111937	R4 558	R638	R5 197
32	26/05/09	126359	Spandau Driving School	24011510 5032	210062	R21 440	-	R21 440

Number 10 - Invoice amount is R2,170.02 dated 13/5/09 and paid 29/6/09

Number 26 - Invoice received 6/7/09 and paid 24/8/09

Number 32 - Invoice dated 26/5/09 and paid 9/7/09

The following accounts payable balances did not agree to the suppliers' statements.

NUMBER	DATE	CREDITOR	AMOUNT	VAT	TOTAL
2	2011/06/09	Blitsdruk	R4 009	R561	R4 571
16	1930/06/09	MTN	R4 356	R610	R4 966

Number 2 - The invoice amount, relating to the order, is R2 170.02 and no statement was found.

Number 16 - Insufficient supporting evidence was found to substantiate the balance of R4 965.78 (3 statements were not attached).

Root cause

- (i) The same journal numbers are used every year for Eden as well as for Roads (The numbers start with E1 and P1.
- (ii) Lack of management supervision and review to ensure payments are made within the required time period.
- (iii) Suppliers statements are not reconciled to the accounts payable amounts.
- (iv) *Policies and procedures:* Policies related to reliable financial reporting are not established and communicated throughout the entity, and do not have corresponding procedures that result in management directives being carried out.

Risk

- (i) The possibility exists that not all journals are recorded and that they may be recorded in the incorrect accounting period.
- (ii) Non-compliance with the MFMA.
- (iii) There is a risk that creditors will be overpaid which will negatively impact the municipality's financial resources.

Recommendation

- (i) Journals should be numbered sequentially from one accounting period to the next.
- (ii) All creditor payments should be made within 30 days to ensure adherence to the section 65 (2) (e) of the Municipal Finance Management Act.
- (iii) Management should request that suppliers provide regular statements so that any discrepancies can be followed up timeously.
- (iv) A reconciliation should be performed between goods received notes and invoices which will indicate if all amounts paid to creditors are valid.

Management response

No management response was received.

B.23. Unspent conditional grants

Audit Finding

In terms of section 2.3.2 of the GRAP Implementation Guide for Municipalities:

“Ensure that the municipality maintains the following minimum bank accounts:

Unutilised Capital Receipts – this is to account for unutilised conditional capital grant monies.”

Eden District Municipality does not maintain a separate bank account for unspent conditional grants.

Root cause

- (i) The municipality might be unaware of this requirement.
- (ii) *Policies and procedures* – Policies related to reliable financial reporting are not established and communicated throughout the entity, and do not have corresponding procedures that result in management directives being carried out.

Risk

Non-compliance with GRAP Implementation guide for municipalities, section 2.3.2.

Recommendation

A separate bank account should be opened for unspent conditional grants.

Management response

No management response received.

B.24. Prepaid electricity

Audit Finding

GRAP 9.22 states:

“Revenue is recognised only when it is probable that the economic benefits or service potential associated with the transaction will flow to the entity.”

Included in the current year revenue is unearned portion relating to prepaid electricity.

A portion of prepaid electricity sold in June 2009 will only be utilised by customers in the following financial year. The effect of this is that the revenue in the current year will be overstated by the unutilised portion at year-end.

Root cause

- (i) Management did not calculate the unearned portion of revenue relating to the sale of prepaid electricity at year end
- (ii) *Policies and procedures* – Policies related to reliable financial reporting are not established and communicated throughout the entity, and do not have corresponding procedures that result in management directives being carried out.

Risk

Revenue will be overstated at year-end by an amount equal to the unutilised electricity sold before year-end.

Recommendation

Management should estimate the amount of unutilised electricity at year-end. Revenue should be reduced by this amount and revenue received in advance should be recognised for the corresponding amount.

Management response

We agree with your finding, but are however of the opinion that based on the materiality of pre-paid electricity sales for a district municipality, the recommendation is not practical to implement.

Total prepaid electricity for the 2008/2009 financial year amounts to R1,303,278.

Total prepaid electricity for the 2007/2008 financial year amounts to R1,048,499.

Based on average consumption, the last 7 days sales of June 2009 will amount to R24,994, and the last 7 days sales of June 2008 will amount to R20,108.20, with a net overstatement of income of R4,886.

B.25. Tariffs for rental property

Audit finding

Although the tariffs charged by the municipality on rental properties are in terms of the contracts, these tariffs are not market related as the contracts are not revised on a regular basis.

Root cause

- (i) Management have not established adequate processes to ensure the review of rental contracts on a regular basis.
- (ii) *Policies and procedures* – Policies related to reliable financial reporting are not established and communicated throughout the entity, and do not have corresponding procedures that result in management directives being carried out.

Risk

Although this is not a misstatement of revenue, it does result in a loss of potential revenue for the municipality.

Recommendation

Management should establish a process whereby contracts for rental property are reviewed on a regular basis and amended to ensure that market related tariffs are raised.

Management response

Management is in the process of adhering to the recommendation.

ANNEXURE C: ADMINISTRATIVE MATTERS

C.1. Unidentified receipts

Audit Finding

The MFMA states the following:

“General financial management functions of accounting officers

95. The accounting officer of a municipal entity is responsible for managing the financial administration of the entity, and must for this purpose take all reasonable steps to ensure-

(b) that full and proper records of the financial affairs of the entity are kept;

Monthly reconciliation of revenue and accounts

98. The accounting officer of a municipal entity must take all reasonable steps to ensure that-

(a) all revenue received by the entity, including revenue received by any collecting agency on its behalf, is reconciled on a monthly or more regular basis; and

(b) all accounts of the entity are reconciled each month.”

The municipality does not have a proper system in place to follow-up on unidentified deposits received. These amounts are recorded in the Unallocated Fund Account but are not traced to the debtor accounts timeously.

Root cause

- (i) Operational – directive, preventive, and detective controls are not adequate and focused on achieving efficient resource usage and effectiveness as measured by the extent to which specific control objectives are achieved.
- (ii) Ongoing monitoring - Ongoing monitoring and supervision is not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Risk

Debtor accounts would be overstated by amounts paid but not allocated to their accounts.

Recommendation

- (i) An unidentified receipts register should be kept and reconciled to the Unallocated Funds account regularly.
- (ii) A senior official should review this reconciliation and sign as proof of review.

Management response

No management response received.

C.2. Returned Cheques

Audit Finding

The MFMA states the following:

“General financial management functions of accounting officers

95. The accounting officer of a municipal entity is responsible for managing the financial administration of the entity, and must for this purpose take all reasonable steps to ensure—

(b) that full and proper records of the financial affairs of the entity are kept;

Monthly reconciliation of revenue and accounts

98. The accounting officer of a municipal entity must take all reasonable steps to ensure that—

(a) all revenue received by the entity, including revenue received by any collecting agency on its behalf, is reconciled on a monthly or more regular basis; and

(b) all accounts of the entity are reconciled each month.”

Through inspection of the returned cheques file, it could not be confirmed if there were any follow-ups performed on these cheques to ensure that the accounts of debtors who paid with these cheques are not reduced with these payments.

Root cause

- (i) Operational – directive, preventive, and detective controls are not adequate and focused on achieving efficient resource usage and effectiveness as measured by the extent to which specific control objectives are achieved.
- (ii) Ongoing monitoring - Ongoing monitoring and supervision is not undertaken to enable management to determine whether internal control over financial reporting is present and functioning.

Risk

Debtor accounts could be reduced erroneously if it is reduced by the amount of returned cheques.

Recommendation

A returned cheque register should be maintained and all cheques in this register should be traced back to the respective debtors to ensure that these amounts are not deducted from their accounts.

Management response

No management response received.