

**REPORT OF THE AUDITOR-GENERAL TO THE EASTERN CAPE PROVINCIAL
LEGISLATURE AND THE COUNCIL ON SUNDAYS RIVER VALLEY MUNICIPALITY
REPORT ON THE FINANCIAL STATEMENTS**

Introduction

1. I have audited the accompanying financial statements of the Sundays River Valley Municipality, which comprise the statement of financial position as at 30 June 2011, the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, a summary of significant accounting policies and other explanatory information as set out on pages 3 to 43.

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 South African Standards of Generally Recognised Accounting Practice (GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2010 (Act No. 1 of 2010 as amended) (DoRA), as well as for such internal control as management determines necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 (Act No. 108 of 1996) (The Constitution) and section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with International Standards on Auditing and General Notice 1111 of 2010 issued in Government Gazette 33872 of 15 December 2010. 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. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for qualified opinion

Provision for leave pay

7. The scope of my audit was restricted as leave forms were not completed for days employees did not work, various attendance registers were missing and approved leave forms were not deducted from employees leave balances. The municipality's leave records have been used as the basis for the calculation of the provision for leave pay and did not permit the application of alternative procedures. Consequently, I was unable to confirm or verify the existence, completeness and valuation of the leave pay provision stated at R1.9 million in note 14 to the financial statements.

Prior year comparative information

8. The scope of my audit was restricted as I was unable to obtain supporting documentation for certain trade creditors totalling R3.4 million included in the comparative amount of note 10 to the financial statements. Management could not provide the supplier statements to support the amounts recorded in the general ledger, neither could the statements be obtained directly from the suppliers. Consequently, I was unable to perform alternative procedures and was therefore unable to confirm or verify the existence, completeness and valuation of trade creditors of R16.93 million disclosed in the comparative amount of note 10 to the financial statements.
9. Management was unable to reconcile a difference of R2.5 million between the salary reports of R24.3 million and employee related costs of R24.1 million and remuneration of councillors of R2.7 million, as disclosed in the comparative amounts of note 26 and note 27 respectively to the financial statements. Consequently I was unable to perform alternative procedures and was therefore unable to confirm or verify the occurrence, cut-off, classification and accuracy assertions.
10. The scope of my audit was restricted as I was unable to obtain adequate source documentation for general expenses of R1.9 million and grant expenses of R1.8 million per the comparative amounts in note 33 and note 32 respectively to the financial statements. Neither could management provide any other reliable supporting documentation relating to these expenditures. Consequently, I was unable to confirm or verify by alternative means the occurrence of the above expenditures.

Opinion

11. In my opinion, except for the possible effects of the matters described in the Basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Sundays River Valley Municipality as at 30 June 2011 and its financial performance and cash flows for the year then ended, in accordance with GRAP and the requirements of the MFMA.

Emphasis of matters

12. I draw attention to the matters below. My opinion is not modified in respect of these matters:

Restatement of comparative figures

13. As disclosed in note 48 to the annual financial statements, the comparative figures for 30 June 2010 have been restated due to expiry of the transitional provisions contained in Directive 4: Transitional Provisions for Medium and Low Capacity Municipalities, and as a result of errors in the 2010 financial statements which were only corrected in the current financial year.

Financial sustainability

14. Note 1.3 to the financial statements indicates that the financial sustainability of the municipality is uncertain and that the municipality is currently placed under administration in terms of section 139(1)(b) of The Constitution.

Unauthorised, irregular and fruitless and wasteful expenditure

15. As disclosed in note 38 to the annual financial statements, the following instances of unauthorised, irregular and fruitless and wasteful expenditure were incurred by the municipality during the financial year:

- actual expenses per the statement of financial performance exceeded the budget by R7.5 million resulting in unauthorised expenditure which was subsequently approved as irrecoverable and written off by the administrator;
- the municipality incurred irregular expenditure of R5.6 million in contravention of the supply chain management requirements;
- and the municipality incurred fruitless and wasteful expenditure of R1.2 million arising from interest and penalties due to the South African Revenue Service and salary payments being made to an employee whilst being on suspension which was subsequently approved as irrecoverable and written off by the administrator.

Material losses/ Impairments

16. As disclosed in note 2 to the financial statements, there was an increase in the doubtful debts provision of R15.7 million and an actual write-off of bad debts of R26.4 million during the financial year.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

17. In accordance with the PAA and in terms of *General notice 1111 of 2010*, issued in *Government Gazette 33872 of 15 December 2010*, I include below my findings on the annual performance report as set out on pages 1 to 91 and material non-compliance with laws and regulations applicable to the municipality.

Predetermined objectives

18. There were no material findings on the annual performance report concerning the presentation, and reliability of the information.

Usefulness of information

19. The following criteria are relevant to the findings below:
 - Consistency: Objectives, indicators and targets are consistent between planning and reporting documents
20. Audit findings:

Reported objectives are not consistent when compared with the planned objectives

- The actual achievements with regard to 48% of all planned objectives specified in the integrated development plan for the year under review were not included in the annual performance report.

Compliance with laws and regulations

Budgets

21. The accounting officer did not always submit the monthly budget statements to the mayor and the relevant provincial treasury, as required by section 71(1) of the MFMA.
22. The municipality incurred expenditure in excess of the limits of the amounts provided for in the votes in the approved budget, in contravention of section 15 of the MFMA.

Annual financial statements, performance and annual report

23. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of capital assets, current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors were subsequently corrected, but the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.

Expenditure management

24. Certain payments due to creditors were not settled within 30 days from the receipt of an invoice, as per the requirements of section 38(1)(c)(ii) of the MFMA
25. The accounting officer did not take all reasonable steps to prevent irregular expenditure, as disclosed in note 41.1, as required by section 62(1)(d) of the MFMA.

INTERNAL CONTROL

26. In accordance with the PAA and in terms of General notice 1111 of 2010, issued in *Government Gazette 33872 of 15 December 2010*, I considered internal control relevant to my audit, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters reported below are limited to the significant deficiencies that resulted in the Basis for qualified opinion the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

27. There is inadequate oversight by senior officials as there is a lack of regular reviews by management on monthly reporting. Key staff members were not always available for meetings throughout the audit and the human resource policies are not adequately followed as certain staff members within the finance department do not understand the applicable financial reporting framework and there is also a lack of capacity at management level within the municipality.

Financial and performance management

28. The municipality did not exercise adequate controls over daily and monthly processing and reconciling of transactions because it was noted that certain significant accounts and schedules were not reviewed or reconciled either in part or throughout the financial year. In addition to this, controls were weak regarding both authorization and capturing of leave forms and certain masterfile amendments.

Governance

29. The internal audit department was utilised by the municipality during the financial year to implement and correct certain internal controls; this limited their function as an independent review function which would normally report directly to the audit committee. In addition to this the internal audit department was not operational for the last six months of the year.
30. As a result of the impaired functioning of the internal audit department the audit committee could not effectively evaluate and monitor responses to risks and provide oversight over the effectiveness of the internal control environment including financial and performance reporting and compliance with laws and regulations.

OTHER REPORTS

Investigations

31. In the prior year, a forensic investigation was undertaken, and has been finalised in the current year.

The purpose of the investigation was to determine whether the municipality owed the Department of Housing monies which the municipality disputed on the basis that the monies were used for the building of additional houses. The Department of Housing did not take into consideration certain houses that were built in addition to the original approved plans.

The outcome of the investigation was that the municipality had fulfilled their responsibilities in terms of the original agreement.

The Department of Housing then acknowledged the debt owing to the municipality due to the additional houses built.

Subsequent to year end the outstanding amounts owed by the Department of Housing was received to settle outstanding claims due to the municipality. These amounts have been utilised to settle certain outstanding housing creditors.

A decision was made by the MEC in the current year that the developer status reverts back to the Department of Housing.

Auditor General

Port Elizabeth

30 November 2011



AUDITOR - GENERAL
SOUTH AFRICA

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