

Audit Report
Baviaans Municipality
For the Year ended 30 June 2011

REPORT OF THE AUDITOR-GENERAL TO THE EASTERN CAPE PROVINCIAL LEGISLATURE AND THE COUNCIL ON BAVIAANS MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the accompanying financial statements of the Baviaans Municipality, which comprise the statement of financial position as at 30 June 2011 and 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, and the accounting officer's report, as set out on pages ... to

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 Statements of Generally Recognised Accounting Practice (GRAP) and in the manner required by 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), and 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 South Africa, 1996 (Act No. 108 of 1996) and section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) my responsibility is to express an opinion on these financial statements based on conducting the audit in accordance with the International Standards on Auditing and General Notice 1111 of 2010 issued in *Government Gazette* 33872 of 15 December 2010. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer of opinion

Expenditure

4. Expenditure of R39,7 million for the financial year under review is disclosed in the statement of financial performance.
5. Included in the total expenditure are amounts to the value of R8,5 million (2010: R4,1 million) for which adequate supporting documentation could not be provided. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, occurrence, accuracy, cut-off and classification of expenditure.
6. Also included in the total expenditure is an amount of R2,7 million for expanded public works programme wages that were incorrectly classified. Consequently, employee costs are understated and the expanded public works programme is overstated by R2,7 million.

Revenue

7. According to the statement of financial performance, revenue for the financial year under review amounted to R44,8 million.
8. Included in this revenue are amounts totalling R4,2 million (2010: R5 million) for which adequate supporting documentation could not be provided. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, occurrence, accuracy, cut-off and classification of revenue.
9. Included in the total revenue above is an amount of R576 472 relating to expenditure for repairs and maintenance, and electricity that was incorrectly processed to revenue. Consequently, revenue and expenditure are both understated by R576 472.
10. The audit report on the financial statements of the municipality for the year ended 30 June 2010 was modified on occurrence and accuracy of revenue by an amount of R623 645. The receivables could not be traced to subsequent receipts. The corresponding figures in the current year financial statements have not been amended to record the misstatements.

Government grant and subsidies

11. According to the statement of financial performance government grant and subsidies for the financial year under review amounted to R26,3 million.
12. Included in grant revenue are amounts totalling R1,3 million for which adequate supporting documentation could not be provided. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, occurrence, accuracy, cut-off and classification of government grant and subsidies.
13. GAMAP 9 prescribes that revenue from conditional government grants only be recognised to the extent that the conditions have been met. Contrary to this requirement, an amount of R935 242 was incorrectly recognised as revenue from government grants. As a consequence of not adhering to this accounting standard government grants and subsidies revenue that is disclosed in the statement of financial performance and in note 25 is overstated and unspent conditional grants and receipts in the statement of financial position is understated by R935 242.

Irregular expenditure

14. Irregular expenditure for the financial year under review of R3,1 million is disclosed in note 43 to the financial statements.
15. Adequate supporting documentation to the value of R4,8 million could not be provided to confirm the adherence to the procurement processes. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, accuracy and classification of irregular expenditure that is disclosed in note 43 of the financial statements.
16. Irregular expenditure amounting to R5 million related to payments made in contravention of the procurement processes. Furthermore, irregular expenditure to the amount of R5 790 relating to section 8(1) of the Remuneration of Public Office Bearers,

1998 (Act No. 20 of 1998) was not included in note 43. Consequently, the irregular expenditure in note 43 is understated by an amount of R5 million.

17. Included in general expenditure is an amount of R624 979 where the grant was not utilised per the required grant condition. This amount was not recognised as irregular expenditure and consequently irregular expenditure is understated by R624 979.

Unauthorised expenditure

18. Disclosed in note 41 to the financial statements is unauthorised expenditure for the financial year under review of R3,1 million. Section 15 of the MFMA requires the municipality to incur expenditure only in terms of and within each vote limit of an approved budget. Contrary to this requirement, expenditure of R6,3 million was incurred, which exceeded the budget per vote. Furthermore, grant expenditure of R2,4 million was spent in contravention of the grant conditions. Consequently, the unauthorised expenditure disclosed in note 41 of the financial statements is understated by R8,7 million.

Value added tax (VAT)

19. Included in the VAT receivable from exchange transactions is an amount of R508 169 (2010: R1,2 million) for which adequate supporting documentation could not be provided. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, valuation, existence, classification and rights and obligations of the VAT receivable from exchange transactions.
20. Section 7 of the Value-Added Tax Act, 1991 (Act No. 89 of 1991) prescribes that a vendor is liable for VAT for the supply of goods or services calculated at a rate of 14% on the value of the supply. An amount of R406 218 (2010: R491 557) relating to the adjustment to output VAT overdeclared on revenue was incorrectly accounted for by the municipality. Consequently, the VAT receivable from exchange transactions and revenue is overstated.
21. An opening balance of R436 814 relating to the prior year VAT receivable from exchange transactions was not brought forward. Consequently, the VAT receivable from exchange transactions and the accumulated surplus are overstated.
22. The prior year VAT receivable from exchange transactions was not adjusted based on the VAT assessment received from the South African Revenue Service to the amount of R113 444. Consequently, the VAT receivable from exchange transactions and the accumulated surplus are understated by R113 444.

Property, plant and equipment

23. Property, plant and equipment of R37,7 million (2010: R25,9 million) is disclosed in the statement of financial position of the municipality.
24. Documentation to support the disclosure of property, plant and equipment of R7,5 million could not be provided. Furthermore, the fixed asset register did not reflect all land and buildings, assets did not always have unique numbers to identify them and the fixed asset register only reflected additions from 2008. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, valuation, existence, classification, and rights and obligations of property, plant and equipment.

25. GRAP 17: *Property, plant and equipment*, requires assets to be disclosed per category. An amount of R8,7 million was misclassified between the categories of property, plant and equipment. Consequently, infrastructure assets, community assets and other equipment is overstated by R1 million, R931 070, R6.7 million respectively and plant and equipment, furniture and fittings, electronic equipment, vehicles and infrastructure assets is understated by R620 713, R1.7 million, R5.1 million, R775 891 and R465 535 respectively.
26. GRAP 17 also prescribes that the amount of contractual commitments for the acquisition of property, plant and equipment should be disclosed in the financial statements for each class of property, plant and equipment recognised in the financial statements. Capital commitments of R19.3 million was identified that did not agree to the capital commitments of R20.5 million disclosed in note 10 to the financial statements. Consequently, capital commitments are overstated by R1,2 million.
27. GRAP 17 also requires that the existence and amounts of restrictions on title and property, plant and equipment pledged as securities for liabilities, should be disclosed in the financial statements for each class of property, plant and equipment recognised in the financial statements. Assets to the value of R1,5 million, which were pledged as security were not included in the amount of R1,7 million disclosed in note 10 in the financial statements. Consequently, the value of assets pledged as security is understated by R1,5 million.
28. GRAP 17, *Property, plant and equipment*, requires that various classes of property, plant and equipment that are of a similar nature or function should be shown as a single item for the purpose of disclosure in the financial statements. The disclosure in note 10 for property, plant and equipment does not reflect assets to the value of R3,2 million held separately under a finance lease.
29. The audit report of the previous financial year was modified in respect of property, plant and equipment due to overstatements and understatements of R144 826 and R117 859, respectively, as expenses were incorrectly capitalised and fixed asset additions and finance lease expenses were incorrectly expensed. The prior year amounts that are disclosed in the financial statements for the year under review have not been amended to record this misstatement. Consequently, property, plant and equipment are overstated by R26 967.

Investment properties

30. Investment property of R10 155 is disclosed in the statement of financial position and note 9 to the financial statements.
31. Adequate supporting documentation and records such as a property register with sufficient detail of descriptions, locations and references that correlated to the physical assets could not be provided to confirm this disclosure. Furthermore, the municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, valuation, existence, classification, and rights and obligations of investment property.

Cash and cash equivalents

32. Included in the statement of financial position for the financial year under review is a bank overdraft of R289 375 (2010: cash and cash equivalent of R193 465).
33. IAS 39 prescribes that a financial liability will be derecognised when it is extinguished

and the obligation specified in the contract is discharged or cancelled, or expires. Included in reconciling items of R537 741 is an amount of R533 128 relating to trade payables. The municipality withheld a payment at year-end due to cash flow difficulties being experienced. Consequently, the bank overdraft and trade payables are understated by R533 128.

Trade and other payables

34. Trade and other payables from exchange transactions of R9,8 million (2010: R5,8 million) are disclosed in the statement of financial position and note 14 to the financial statements.
35. Included in the trade and other payables from exchange transactions is an amount of R3,4 million (2010: R2,1 million) for which adequate supporting documentation could not be provided. The municipality could also not provide sufficient appropriate audit evidence to support payments of R2,9 million that were made subsequent to year-end. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, valuation, existence, classification and rights and obligations of the trade and other payables.
36. The audit report on the financial statements of the municipality for the year ended 30 June 2010 was modified on existence and the valuation of the trade and other payables from exchange transactions by an amount of R1,1 million. The trade and other payables from exchange transactions included bank transfers resulting in a misclassification. The corresponding figures in the current year financial statements have not been amended to record the misstatements. As a result my opinion on the financial statements for the current year is also modified on the corresponding figures.

Trade and other receivables from exchange transactions

37. According to the statement of financial position and note 5 to the financial statements trade and other receivables from exchange transactions for the financial year are R194 673 (2010: R463 279).
38. Included in these trade receivables from exchange transactions is an amount of R759 050 and a write-off of irrecoverable receivables of R2,5 million for which adequate supporting documentation could not be provided. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, valuation, existence, classification, and rights and obligations of the trade receivables from exchange transactions.
39. Provision for debt impairment of assets of R901 411 disclosed in note 7 is not in terms of IAS 39, *Financial Instruments: Recognition and Measurement*. The municipality could not provide supporting documentation to substantiate the inputs and assumptions used to calculate the provision for the balance provided. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, valuation, existence, classification, and rights and obligations of the provision for debt impairment of assets.
40. The audit report on the financial statements of the municipality for the year ended 30 June 2010 was modified as insufficient documentation was obtained to substantiate receivables and journals relating to receivables to the amount of R1,3 million for completeness, valuation, existence, classification, and rights and obligations.

Furthermore, the provision for debt impairment was calculated by management using the 31 March 2010 debtors age analysis instead of the debtors age analysis as at 30 June 2010. The corresponding figures in the current year financial statements have not been amended to record the misstatements. As a result, my opinion on the financial statements for the current year is also modified on the corresponding figures.

Accumulated surplus

41. Disclosed in the statement of financial position is the accumulated surplus of R28,6 million (2010: R23,5 million).
42. Included in the prior year accumulated surplus restatement of R12 million, disclosed in note 37, is an amount of R436 814 for which adequate supporting documentation could not be provided. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, valuation, existence, classification and rights and obligations of accumulated surplus.
43. The opening balance of the accumulated surplus in the statement of changes in net assets to the financial statements of R19,3 million has been restated by R1,1 million. Adequate supporting documentation could not be provided for this restatement. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the disclosure of accumulated surplus.

Provision for landfill site

44. The prior year balance includes an amount of R989 634 for which adequate supporting documentation could not be provided. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness, valuation, existence, classification and rights and obligations of the provision for landfill sites.
45. A provision for landfill sites has not been recognised or measured in terms of the GRAP 19, *Provisions, contingent liabilities and contingent assets*. The municipality did not elect to adopt Directive 4 in the 30 June 2010 financial statements. The contingent liability as disclosed in note 22 is thus not sufficient regarding the provision for landfill sites. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to determine the extent of the misstatement of the provision for landfill sites.

Remuneration of councillors

46. Councillors' remuneration of R1 million is disclosed in the statement of performance and note 29 to the financial statements.
47. Various allowances were incorrectly classified in note 29 to the financial statements. This resulted in an understatement of R1,1 million and an overstatement of basic salary councillors amounting to R1 million. Consequently, remuneration of councillors is understated by R64 189.

Retirement benefits

48. IAS 19, *Employee benefits*, requires that a present obligation should be recognised for a defined benefit plan, whereas a defined contribution plan will not give rise to a liability and will be disclosed as an expense in the financial statements. The retirement benefit plan is recognised, measured and disclosed in note 20 as a defined contribution plan. The municipality could not provide sufficient appropriate audit

evidence to support the treatment of the plan. The municipality's accounting records did not permit the application of alternative audit procedures. Consequently, I could not obtain sufficient appropriate audit evidence to satisfy myself as to the valuation, existence and disclosure of the retirement benefit plan.

Cash flow

49. Presentation of a cash flow statement summarising the entity's operating, investing and financing activities, is required by Standard of Generally Recognised Accounting Practice, GRAP 2, *Cash flow statements*. The following material misstatements were identified during my audit:
50. Included in net cash flows from operating activities in the cash flow statement and note 34 to the financial statements is an adjustment to trade and other payables of R4,2 million. As this adjustment does not relate to cash transactions, both net cash flows from operating activities in the cash flow statement and note 34 are overstated by R4,2 million.
51. Proceeds from sale of financial assets of R7,3 million (2010: R11 million) is overstated by R1 million (2010: R46 584) due to the misclassification of investments in the current and prior year. Furthermore, this resulted in the closing balance for cash and cash equivalents being understated by R5 810 (2010: R1 million) and the opening balance for cash and cash equivalents being understated by R1 million (2010: R972 885).

Financial statement disclosure

52. VAT to the value of R2,9 million has been incorrectly classified as a financial instrument in note 38 to the financial statements. The municipality did not disclose all the information required by the IFRS 7 (AC 144), *Financial instruments: Disclosures*.

Financial sustainability

53. GRAP 1, paragraph 27, requires that management disclose any material uncertainties which may cast significant doubt upon its ability to continue as a going concern. The municipality is currently in a net liability position of R8,4 million and is unable to settle short-term debts timeously and, considering the material adjustments required to liabilities and expenses, the municipality would not be in a profitable position. Furthermore, the municipality could not provide assurance of the ability to settle short-term debt to mitigate the liquidity situation. There is significant uncertainty as to whether the municipality will be able to settle its obligations as they fall due. Management has not disclosed any of the material uncertainties as required.

Accumulation of immaterial uncorrected misstatements

54. The financial statements as a whole are materially misstated due to the cumulative effect of various individually immaterial uncorrected misstatements in the following elements making up the statement of financial performance:
 - Employee costs, note number 28, R212 983
 - General expenditure, note number 32, R535 976
 - Revenue, note number 23, -R95 489
 - Finance costs, note number 23, -R170 281

55. In addition, I was unable to obtain sufficient appropriate audit evidence and consequently, I was unable to confirm or verify the following elements making up the statement of financial performance by alternative means:
- Employee costs, note number 28, R48 690
 - General expenditure, note number 32, -R174 420
 - Revenue, note number 23, R277 486
 - Government grants and subsidies, note number 25, R196 630.

Disclaimer of opinion

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

Emphasis of matter

57. I draw attention to the matter below. My opinion is not modified in respect of this matter:

Restatement of corresponding figures

58. As disclosed in note 37 to the financial statements, the corresponding figures for 30 June 2010 have been restated due to errors discovered during the period ended 30 June 2011 in the financial statements of Baviaans Municipality at, and for the year ended, 30 June 2010.

Additional matter

59. I draw attention to the matter below. My opinion is not modified in respect of this matter:

Unaudited supplementary schedules

60. The supplementary information set out on pages XX to XX and 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.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

61. In accordance with PAA and in terms of *General Notice 1111 of 2010*, issued in *Government Gazette 33872* of 15 December 2010, we include below our findings on the annual performance report as set out on pages XX to XX and material non-compliance with laws and regulations applicable to the municipality.

PREDETERMINED OBJECTIVES

Presentation of information:

62. The following criteria are relevant to the findings below:

- Performance against predetermined objectives is reported using the National Treasury guidelines.

63. Audit findings:

Reasons for major variances between planned and actual reported targets were not provided in the report on predetermined objectives

- Adequate explanations for any of major variances between the planned and the actual reported targets were not provided, as required in terms of the relevant reporting guidance.

Usefulness of information

64. The following criteria are relevant to the findings below:

- Relevance: A clear and logical link exists between the objectives, outcomes, outputs, indicators and performance targets
- Measurability: Indicators are well-defined and verifiable, and targets are specific, measurable and time bound.

65. Audit findings:

Planned and reported indicators are not well defined

- Sixty-four of the planned and reported indicators that were selected were not clear, as unambiguous data definitions were not available to allow for data to be collected consistently.

Planned and reported indicators are not verifiable

- Valid performance management processes and systems, that produce actual performance against the planned indicators, do not exist for 47% of the selected indicators.

Planned and reported targets are not specific

- Targets were not specific in clearly identifying the nature and the required level of performance in respect of 55% of the selected objectives.

Planned and reported targets are not measurable

- Seventy-four per cent of the planned and reported targets for the selected indicators were not measurable in identifying the required performance.

Planned and reported targets are not time bound

- All the planned and reported targets that were selected were not time bound in

specifying the time period or deadline for delivery.

Planned objectives and indicators are not relevant to the mandate and objectives of the entity

- In more than 39% of instances the indicator and targets as per the integrated development plan did not relate directly to the institution's strategic goals and objectives as per the five-year integrated development plan.

Reliability of information

66. The following criteria are relevant to the findings below:

- Validity: Actual reported performance has occurred and pertains to the entity
- Accuracy: Amounts, numbers and other data relating to reported actual performance have been recorded and reported appropriately
- Completeness: All actual results and events that should have been recorded have been included in the annual performance report.

67. Audit findings:

Reported performance against targets is not valid, accurate and complete when compared to source information

- Sixty-seven % of the reported targets for the selected objective were not accurate and valid based on the source information provided.
- All of the reported targets for the selected objectives were not valid and accurate based on the source information provided.
- None of the reported targets in respect of the selected objectives are complete, based on the source information provided.
- Fifty per % of the reported targets for the selected objectives were not valid and accurate based on the source information provided.
- Based on the source information provided, 33% of the reported targets for 33% of the selected objectives were not complete.

Reasons for major variances between planned and actual reported targets were not provided in the report on predetermined objectives

- Adequate explanations for all of major variances between the planned and the actual reported targets for none of the objectives, as required in terms of the relevant reporting guidance, could not be provided.

Compliance with laws and regulations

Strategic planning and performance management

68. The municipality did not implement a framework that describes and represents how the municipality's cycle and processes of performance planning, monitoring, measurement, review, reporting and improvement will be conducted, organised and managed, including determining the roles of the different role players as required by sections 38, 39, 40 and 41 of the Municipal Systems Act, 2000 (Act No.32 of 2000) (MSA) and Regulations 7 and 8 of the Local Government Municipal Planning and Performance Management, 2001 (MPPR) published in *General Notice* 796 of 24 August 2001.

69. The accounting officer of the municipality did not submit the results of the assessment on the performance of the municipality during the first half of the financial year to the

mayor of the municipality, the National Treasury, and the Provincial Treasury as required by section 72(1) (b) of the MFMA.

Budgets

70. In contravention of section 15 of the MFMA, the municipality incurred expenditure that was not budgeted for and incurred expenditure in excess of the limits of the amounts provided for in the votes in the approved budget.
71. The annual budget of the municipality is not based on the development priorities and objectives as well as the performance targets set by the municipality in its intergraded development plan required by regulation 6 of the MPPR.

Financial statements, performance and annual reports

72. 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 identified by the auditors were not adequately corrected, which resulted in an adverse audit opinion for the year under review.
73. The accounting officer neither submitted the council's oversight report on the 2009-10 annual report within seven days of its adoption (section 129(3) of the MFMA), nor did he make the annual report for 2009-10 public immediately after the annual report was tabled in the council (section 127(5) of the MFMA).
74. The report containing the council's comments on the annual report for 2009-10 was not adopted within two months from the date on which the annual report was tabled in the council as required by section 129(1) of the MFMA.
75. The performance report for the financial year under review was not prepared as required by section 46 of the MSA and section 121(3) (c) of the MFMA.

Audit committee/performance audit committee

76. The audit committee did not advise the council, the accounting officer and the management staff of the municipality on matters relating to accounting policies and performance evaluation. It also did not review the annual financial statements and also did not meet at least four times a year (section 166 of MFMA).
77. The performance audit committee or another committee functioning as the performance audit committee did not review the quarterly reports of the internal auditors on their audits of the performance measurements or submit a report to the council regarding the performance management system at least twice during the financial year (MPPR regulation 14).

Procurement and contract management

78. It was not possible to determine whether goods and services with a transaction value of between R10 000 and R200 000 were either procured without obtaining written price quotations from at least three different or quotations had not been obtained at all (Supply Chain Management (SCM) regulation 17) due to the lack of documentation provided.
79. Adequate documentation was not submitted to confirm that quotations were accepted from suppliers who are not on the list of accredited prospective providers and sufficient or that they meet the listing requirements of SCM regulations 16 and 17.
80. Sufficient evidence could not be obtained that goods and services with a transaction value above R200 000 were procured by inviting competitive bids as per the

requirements of SCM Regulations 19(a) and 36(1), or that bid specifications for procurement of goods and services were drafted in an unbiased manner that allowed all potential suppliers to offer their goods or services (SCM regulation 27).

81. Due to the lack of evidence it was not possible to confirm that awards were granted in terms of criteria that were stipulated in the original bid documents as per the requirements of SCM regulations 21(b) and 28(1). Sufficient evidence could also not be provided to confirm that, in all cases, invitations for competitive bidding were advertised for 30 days (SCM regulation 22), that bid specifications were the product of a bid specification committee (SCM regulation 27) or that bids were evaluated by properly composed bid evaluation committee (SCM regulation 28).
82. Inadequate audit evidence could not be obtained to confirm that final awards and/or recommendation of awards to the accounting officer were made by an adjudication committee that was constituted in terms of the requirements of SCM regulation 29.
83. Sufficient audit evidence could not be obtained to confirm that awards were made to suppliers who were able to provide tax clearance certificates stating that their tax matters declared by the South African Revenue Service are in order as required by SCM regulation 43.
84. Awards were made to suppliers who did not submit a declaration on their employment by the state or their relationship with a person employed by the state as per the requirements of SCM regulation 13(c).
85. Due to the lack of audit evidence it could not be confirmed that all items over R30 000 were procured in terms of the preference point system that is prescribed by section 2 of the Preferential Procurement Policy Framework Act, 2000 (Act No. 5 of 2000) (PPPF Act) and SCM regulation 28. It was also not possible to obtain confirmation that, in all cases, awards were made to suppliers based on preference points that were allocated and calculated in accordance with the requirements of the various sections of PPPF Act and its regulations. Insufficient evidence could not be obtained to ascertain that awards were made to suppliers that scored the highest points as required by section 2(1) (f) of PPPF Act.
86. The performance of contractors or suppliers was not monitored effectively on a monthly basis as required by section 116(2) of the MFMA.
87. Sufficient appropriate audit evidence could not be obtained that construction contracts were awarded to contractors that were registered and qualified for the contract in accordance with the various prescripts of the Construction Industry Development Board (CIDB).
88. Awards were made to suppliers whose principal shareholders are persons in the service of other state institutions, in contravention of the requirements of SCM regulation 44. Furthermore, sufficient and appropriate audit evidence could not be obtained that the provider declared that he is in the service of the state as required by SCM regulation 13(c).

Expenditure management

89. The amount owing by the municipality to creditors was not always paid within 30 days of receiving an invoice, as is required by section 65(2)(e) of the MFMA. In certain cases it was not possible to determine that suppliers were paid within 30 days of receiving an invoice or statement, due to the lack of documentation provided.
90. All reasonable steps were not taken to ensure that the municipality had and maintained an effective systems expenditure control and management. Furthermore, inadequate steps were not taken to ensure that the accounting and information system which recognised expenditure and accounted for creditors of the municipality functioned effectively (section 65(2) of the MFMA). Sufficient appropriate steps were also not taken to prevent unauthorised, irregular and fruitless and wasteful expenditure, as required by section 62(1) (d) of the MFMA.
91. The municipality did not determine whether unauthorised, irregular or fruitless and wasteful expenditure resulted from inappropriate actions of officials and thus did not take steps to recover amounts from officials where they were negligent or in any other way caused the municipality to breach the requirements of section 32(2) of the MFMA.

Transfers and conditional grants

92. In certain cases the financial management grant, municipal infrastructure grant, municipal systems improvement grant and tourism training grant were not utilised for the purposes for which they were made available in terms of section 15(1) of the DoRA. It was also not always possible to determine whether these grants had been used for their intended purpose due to the lack of documentation that could be made available.

Revenue management

93. Adequate steps were not taken to ensure that the municipality had and maintained an adequate management, accounting and information system which recognised revenue when it is earned, accounted for debtors and receipts of revenue, as required by section 64(2)(e) of the MFMA.

Asset management

94. Adequate mechanisms did not exist to ensure that internal controls and the accounting and information systems relating to asset management (section 63(2)(a) of the MFMA).

Personnel expenditure and councillors' remuneration

95. Section 124(1) of the MFMA prescribes that the detail of salaries, allowances and benefits of all political office-bearers, councillors, the municipal manager, the chief financial officer, every senior manager and such categories of other officials should be disclosed in the financial statements. The municipality did not disclose this detail in its notes to the financial statements as required by this provision.

INTERNAL CONTROL

96. 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 adverse opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

97. Management has not always acted decisively in addressing audit findings of the previous financial year. This resulted in material deficiencies not being sufficiently addressed to avoid similar finding again being reported. This was caused by the lack of oversight and effective leadership.
98. The leadership does not exercise sufficient control and direction to ensure that there is a general regard and compliance for laws and regulations that govern the municipality. This resulted in significant irregular expenditure being incurred, often not being detected by the municipality but rather through the audit process. The lack of action taken to address the irregular expenditure reported in the previous financial year is also an indication of management's reluctance and willingness to address the non-compliance with laws and regulations.
99. The risks relating to predetermined objectives were also not adequately identified and addressed by management. This resulted in inadequate structuring of the performance reporting process and an inability to support actual achievements with reliable and relevant documentation. It also gave rise to inadequate monitoring and review and culminated in many service delivery objectives and targets not being met.

Financial and performance management

100. Sufficient attention was not given to the strategic financial management direction and control. Consequently, many of the prior year audit findings were not addressed and were raised again during the financial year under review. Proper record keeping was not maintained to ensure that complete, relevant and accurate information is accessible and available to support financial and performance reporting. This was despite the municipality making use of financial consultants to carry out a leading role in the compiling of annual financial statements.
101. The material misstatements and lack of available supporting documentation bear testimony to the lack of review of transactions at all levels of financial management. Furthermore, accounting disciplines are not in the form of regular daily, weekly and monthly reconciliations and review.
102. The overriding root cause of the inability of the municipality to accurately record and provide support for financial transactions is that officials are not in all respects fulfilling their assigned duties and functions with the required diligence and enthusiasm.

Governance

103. The audit committee continues to play a limited role in governance matters. The audit committee issues the reports of internal audit to the council without making a direct contribution by informing the council or the oversight committee of its concerns and recommendation in terms of its legislated mandate. The audit committee does not promote accountability through evaluating and monitoring responses to risks and providing oversight over the effectiveness of the internal control environment including financial and performance reporting and compliance with laws and regulations.

OTHER REPORTS

Investigations

104. An investigation is being conducted by an independent consulting firm on request of the municipality. The investigation was initiated based on fraud relating to prepaid electricity.
105. The investigation was still ongoing at the reporting date.

Auditor-General

East London

30 November 2011



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

4.2.1 Mayor's analysis of Auditor General's Report

BACKGROUND

Firstly, it is important to note that the Audit Report 2009/10 was only received in April 2011. The local elections took place on 18 May 2011 and the Auditor General's report with the business plan was only tabled to Council on 15 June 2011.

The next round of auditing already started in July 2011. There was a request from the Auditor General to audit the trial balance as on 31 May 2011. There was also a request from the Auditor General to start earlier in order to have the Audit completed on 31 October 2011.

The consultant, Altimax, assisted by the personnel started compiling the Annual Financial statements in July / August 2011. Thus, a bottleneck developed which was impossible for the Finance Department to handle.

Furthermore, it was impossible to implement the business plan to address the Auditor General's 2009/10 report, which was normally tabled to Council in December. There were thus no rectifications done from the previous book year!

PERSONNEL

The Baviaans Council was already warned by internal auditors; Audit Committee and the Auditor General as far back as 2009 that controls in the Finance Department were poor or non-existent. This led to Council appointing three accountants who had to assist the CFO and implement controls.

Attached to this document are the job descriptions of the three accountants. There is emphasis on the accountants because they were appointed to address the lack of control.

In anticipation to the Audit process 2010/11 the following problems in terms of personnel were highlighted:

- 1) Personnel in the Finance Department was not using the SAMRAS system correctly
- 2) The Accountants could not fulfil their control function as prescribed in their job descriptions
- 3) The CFO experienced problems in terms of:
 - Compilation of financial statements in GRAP format
 - Management function in his department
 - Manage working time effectively

FINANCIAL SYSTEM

SAMRAS is the system on which the financial figures are handled. SAMRAS is currently employed the top six municipalities in the country. Thus, it is not the SAMRAS system, which is the problem, but aspects like:

- 1) Comprehension of the system
- 2) Communication with the system
- 3) Rectification of figures on the system

Baviaans is a very small municipality and therefore must compete with bigger and stronger municipalities for the attention of SAMRAS.

REASONS FOR OPINION (DISCLAIMER)

I. Controls

During evaluation of the 2010 /11 Audit report, it is clear that most of the qualifications are due to lack of controls, for example:

Qualifications: 5; 12; 15; 35; 38; 39; 40; 42; 44 (Lack of documentation)

II. 2009/10 Results not correctly rectified

- 1) Due to the late presentation of the 2009/10 Audit report, qualifications of AFS 2009/10 were not rectified, for example number 10
- 2) Due to the problems with the SAMRAS system an age analysis for creditors could not be done on 30 June and the consultants who compile the financial statements did adjustments of creditors without evidence – number 8 / 50 (Creditors as on 30 June)
- 3) VAT not brought over from 2009/10 – number 21
- 4) VAT not adjusted – number 22
- 5) The Auditor General experienced problems with the assessment of the provision for landfill site in 2009/10. Adjustments were done without documentation
- 6) Previous year's surplus incorrectly displayed – R 436 000 – number 42
- 7) Adjustment to trade and other payables – number 50 (see [2] above)

III. Uncertainty about qualifications from the side of the Municipality that must still be clarified

- 1) R 1, 3 million: No documentation for grant revenue – number 12 and 40
- 2) R 624 979: Wrongful spending of allocation – number 17
- 3) R 8, 4 million short term creditors which does not make the municipality financially sustainable according to the Auditor General – number 53
- 4) Adjustments of yearend figures 2009/10 – number 36 and 43
- 5) IAS 19. Employment benefits – number 48
- 6) R 2, 4 million not spent according grant conditions – number 18

IV. Supply Chain

The biggest qualifications are in terms of Supply Chain

- 1) Lack of documentation – number 15
- 2) Wrongful handling of processes – number 16

V. Incorrect calculation

- 1) Interest incorrectly calculated as Grant income – number 13
- 2) Incorrect documenting of figures – number 9
- 3) Incorrect classification of investments – number 51

VI. Provision for bad debt

Incorrect calculation on financial statements – number 39; 40

VII. Qualifications for reference to Altimax, compilers of the financial statements

- 1) Wrong figures used – number 54 and 55
- 2) VAT incorrectly classified – number 52
- 3) Calculation of providence – number 39 and 40
- 4) Remuneration of Councillors incorrectly classified – number 46
- 5) GRAP. 19 – wrong directive followed – number 45
- 6) Over spending not defined – number 18. R 6, 3 million (Approval for over spending not obtained or not considered)
- 7) Assets from previous year's audit report not changed – number 29

Altimax's response is attached

VIII. VAT

- 1) No documents due to problems with SAMRAS – R 508 169 – number 19
- 2) VAT – over declaration – R 406 218 – number 20

IX. Assets

The management of assets, compiling of asset register and unbundling of assets is currently a big problem as noted in the qualifications – number 24; 25; 26; 27; 28; 31 (GRAP compliance)

X. Other qualifications

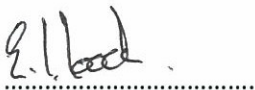
- 1) R850 000 was allocated to the municipality for job creation. During the book year R 2, 7 million worth casual work was created and there was a dispute whether it should be part of salaries or not. This was solved in the first Audit process – see number 6
- 2) Although not a physical bank overdraft the bank account showed an overdraft (R 289 375 – without the proper consent) – number 32
- 3) IAS 39 – obligations not paid on 30 June due to cash flow problems – number 33

SUMMARY

In the evaluation of the Audit Report 2010/11, some aspects stand out:

- 1) In some instances, an incorrect calculation caused more than one qualification.
- 2) There are numerous mistakes in the previous financial year's statements (2009/10) which were carried over without being adjusted
- 3) Huge problems are still experienced with the implementation of the municipal Supply Chain Policy.
- 4) Inaccurate data contributes largely to wrong VAT claims. Qualifications on VAT claims are largely because of an inaccurate date put into the system.
- 5) The use of the SAMRAS systems contributes to qualifications
- 6) Lack of control systems on a daily, weekly and monthly basis

- 7) The conversion to GRAP still causes problems
- 8) The municipality is not capable of displaying its assets in the new format
- 9) That the personnel (accountants) who have to do preparations for the compilation of the financial statements (see job descriptions and compare it with qualifications from AG) have to be part of the process.
- 10) That Section 57 managers apart from the CFO must fulfil their obligations in terms of the MFMA Section 78 (1 & 2)
 - Overspending of budgeted votes
 - Payments from the correct votes
 - Spending of funds according to the allocation
- 11) It is clear that confusion about the Auditor General's auditing process exists due to lack of communication
 - Commencement and time of Auditing
 - Handling of municipal files in the Audit process
 - Communication between Auditors and municipal officials
 - Effectiveness of Audit Steering Committee (It is essential that minutes are kept of outstanding issues as well as issues that are agreed upon)
 - Consultants to be part of Steering Committee. Communication of consultant to Auditor General to be minuted
 - Independent person to do the minutes of Steering Committee
- 12) That the use of journals should be avoided as far as possible
- 13) Bank reconciliation should be done correctly from 01 July and has to correspond with the main ledger on the system



Mayor / Speaker

Baviaans Municipality

Ewald Loock

RESPONSE TO AUDIT REPORT – BAVIAANS MUNICIPALITY

The following points were raised by the mayor Mr Ewald Loock in my telephonic conversation with him. He required response to the following points.

NOTE 18 UNAUTHORIZED EXPENDITURE

The amount of unauthorized expenses was provided by the CFO. We were never informed of the differences between the amounts of the AFS and the AG. The disclosure as requested by the AG would not have been a problem and could have resulted in a removal of this disclaimer paragraph.

NOTE 29 PPE

According to me all PPE adjustments for the prior year as per the previous audit report were corrected in the current financial year. Could the AG please indicate how they calculated these amounts.

NOTE 39 TRADE RECEIVABLES

We never received any communication regarding this paragraph. According to me we provided the AG with working papers as to how we calculated the provision of R901 411.

NOTE 40 TRADE RECEIVABLES

As indicated in our response to the prior year audit report the provision for doubtful debts was not calculated on the 31 March 2010 figures. This was an error on our behalf as the working papers for this amount indicated 31 March 2010. The figures used however were for 30 June 2010.

NOTE 46 & 47 REMUNERATION OF COUNCILLORS

We never received communication regarding the differences in disclosure, This could be rectified quite easily.

NOTE 52 DISCLOSURE OF VAT

We never received communication regarding the disclosure of VAT as a financial instrument

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Directors: MG de Wet AGA(SA) (Executive Chairperson) A Carstens CA(SA) (MD)

Senior Executive: N Slogrove MBA

Executive: E Stander Professional Accountant (SA)

NOTE 54 & NOTE 55

This disclaimer is due to the accumulated differences/mistakes and would be influenced if some of the issues raised in the audit report are addressed.

GENERAL

Please note that we at Altimax only received the Management Report for the first time on 26 October 2011 as per the last audit steering committee meeting. After discussions with Mr Vumazonke, we were informed that it would not be necessary to respond to the issues raised as it would not have any effect on the audit report.

We believe that the municipality's future audit reports can improve if the day to day accounting functions are being controlled. This includes the daily and monthly reconciliations as well as accurate record keeping and filing.

We trust that you will find our response useful and appropriate.

Regards

ALTIMAX

