

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

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of Nxuba Local 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, and a summary of significant accounting policies and other explanatory information, 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 South African Standards 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). This responsibility includes, designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

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) 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 that 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 disclaimed audit opinion.

Basis for disclaimer of opinion

Trade and other receivables from exchange transactions

7. Management did not provide explanations for the difference of R7 013 214 between the amount of R6 410 991 per trial balance on the financial system and the amount of R13 424 205 as disclosed in the statement of financial position. The municipality did not reconcile the difference of R7 013 214 between the financial statements and the underlying accounting records. I was unable to determine the effect on the other account balances or classes of transactions contained in the financial statements.
8. Management did not provide their calculation of the impairment of credit losses. As an alternative procedure I recalculated the impairment using industry methodology guidance provided by National Treasury and assumptions provided by management. The recalculation indicated that the impairment for credit losses recorded by the municipality is overstated by R15 522 398.
9. I did not obtain sufficient audit evidence regarding the existence of debtors amounting to an estimated limitation of R27 012 392 using a positive debtors circular and identifying payments made by the debtors for three months after year end. Using the positive debtors circular, I determined that R719 991 of debtors did not agree with the balance owing.
10. Management did not provide audit evidence to substantiate undefined differences amounting to R10 437 183.
11. Management did not provide reasons for not reclassifying debtors with credit balances of R1 423 432. As a result, trade receivables from exchange transactions and trade payables are both understated by this amount.
12. Consequently, I was unable to obtain sufficient and appropriate audit evidence regarding the existence and valuation for trade and other receivables from exchange transactions amounting to R13 424 205 (2010: R5 113 856), as disclosed in the statement of financial position.

Trade and other receivables from non exchange transactions

13. Management did not provide explanations for the difference of R2 215 962 between the amount of R2 631 861 per the trial balance on the financial system and the amount of R4 847 823 as disclosed in the statement of financial position. The municipality did not reconcile the difference of R2 215 962 between the financial statements and the underlying accounting records. I was unable to determine the effect on the other account balances or classes of transactions contained in the financial statements. I was unable to perform alternative procedures and consequently I was unable to obtain sufficient and appropriate audit evidence regarding the existence and valuation for trade and other receivables from non-exchange transactions amounting to R4 847 823 (2010: R5 494 346) as disclosed in the statement of financial position.

VAT receivable

14. Management did not provide explanations for the difference of R1 571 188 between the amount of R1 098 053 per the trial balance on the financial system and the amount of R2 669 241 as disclosed in the statement of financial position. The municipality did not reconcile the difference of R1 571 188 between the financial statements and the underlying accounting records. I was unable to determine the effect on the other account balances or classes of transactions contained in the financial statements. Management has not apportioned input VAT in terms of section 17(1) of the Value-added Tax Act of South Africa, 1991 (Act No. 89 of 1991) (VAT Act). As a result, input

VAT is overstated by R182 370. No supporting documentation was provided to substantiate journal entries to the value of R203 858. I was unable to perform alternative procedures. Consequently, I was unable to obtain sufficient and appropriate audit evidence regarding the valuation and existence of VAT receivable amounting to R2 669 241 (2010: 193 149) as disclosed in the statement of financial position.

Prepayments

15. Management did not provide explanations for the difference of R1 463 815 between the amount of -R246 427 per the trial balance on the financial system and the amount of R1 217 388 as disclosed in the statement of financial position. The municipality did not reconcile the difference of R1 463 815 between the financial statements and the underlying accounting records. I was unable to determine the effect on the other account balances or classes of transactions contained in the financial statements. I was unable to perform alternative audit procedures and consequently I was unable to obtain sufficient and appropriate audit evidence regarding the existence, classification, valuation and completeness of and rights and obligations pertaining to prepayments amounting to R1 217 388 as disclosed in the statement of financial position.

Suspense accounts

16. Management did not provide explanations for the difference of R14 890 222 between the amount of -R12 292 856 per the trial balance on the financial system and the amount of R602 811 as disclosed in the statement of financial position. The municipality did not reconcile the difference of R14 890 222 between the financial statements and the underlying accounting records. I was unable to determine the effect on the other account balances or classes of transactions contained in the financial statements.
17. No supporting documentation was provided to substantiate the balance of R602 811 as disclosed in the statement of financial position. I was not able to perform alternative procedures. Consequently I was unable to obtain sufficient and appropriate audit evidence regarding the existence, classification, valuation and completeness of and the rights and obligations pertaining to the suspense account.

Call investments

18. The municipality was unable to provide audit evidence or explanations to substantiate transfers of approximately R1 634 341. I was unable to perform alternative audit procedures and consequently I was unable to obtain sufficient and appropriate audit evidence regarding the classification, valuation, and completeness of and rights pertaining to call investments amounting to R3 000 131 (2010: R568 048) as disclosed in the statement of financial position.

Cash and cash equivalents

19. Management did not provide explanations for the difference of R1 619 353 between the amount of R4 619 484 per the trial balance on the financial system and the amount of R3 000 131 as disclosed in the statement of financial position. The municipality did not reconcile the difference of R1 619 353 between the financial statements and the underlying accounting records. I was unable to determine the effect on the other account balances or classes of transactions contained in the financial statements.
20. No explanations were provided for the difference of R496 027 between the cashbook balance of R3 494 489 as disclosed in note 9 to the financial statements and the balance of R3 000 131 in the statement of financial position. I was unable to perform alternative procedures. An ABSA bank account (account no. 4063080837) with a

balance of R35 112 (2010: R479 170) was not disclosed in note 9 to the financial statements resulting in an understatement of cash and cash equivalents.

21. Management was unable to explain bank reconciling differences of R197 241 and R628 890 which appear on the bank reconciliations. I was unable to perform any alternative procedures on these differences.
22. The bank overdraft of R610 328 disclosed in the prior year's statement of financial position is duplicated in note 9 to the financial statements as it is included in the cashbook balance of R567 380.
23. Consequently, I was unable to obtain sufficient and appropriate audit evidence regarding the existence, classification, valuation and completeness of and rights and obligations pertaining to cash and cash equivalents amounting to R3 000 131 (2010: R568 048) as disclosed in the statement of financial position.

Property, plant and equipment

24. The fixed asset register did not contain erf numbers for land owned by the municipality. I was unable to confirm that all the land owned by the municipality as per the valuation roll was recognised in the fixed asset register and was unable to perform alternative procedures. I was therefore unable to obtain sufficient evidence regarding the existence of land totalling R1 586 496.
25. The fixed asset register contained movable assets that were disposed of during the year and, as a result, the fixed asset register is not accurate.
26. Management did not explain the difference of R1 155 591 between additions in the fixed asset register of R5 931 148 and additions of R7 086 739 per note 11 to the financial statements. Management did not explain the reasons for the amount of R7 754 506 disclosed under the heading 'difference' in note 11 to the financial statements. I was unable to perform alternative procedures. Consequently I was unable to obtain sufficient and appropriate audit evidence regarding the existence, valuation, classification and completeness of property plant and equipment as disclosed in the financial statements.

Investment property

27. The fixed asset register did not contain erf numbers for vacant land owned by the municipality. I was unable to confirm that all the land owned by the municipality, as per the valuation roll, was included in the fixed asset register and therefore disclosed in the financial statements. I was unable to perform alternative procedures. Consequently, I was unable to obtain sufficient and appropriate audit evidence regarding the existence, accuracy, classification and completeness of investment property as disclosed in the statement of financial position.

Trade and other payables

28. Management could not provide explanations for the difference of R6 524 784 between the amount of R11 075 261 per trial balance on the financial system and the amount of R4 550 477 as disclosed in the statement of financial position. The municipality did not reconcile the difference of R6 524 784 between the financial statements and the underlying accounting records. I was unable to determine the effect on the other account balances or classes of transactions contained in the financial statements. No supporting documentation was provided for journal entries and creditors reconciliations resulting in a factual limitation of R14 467 921. The financial records did not allow for alternative procedures.

29. The municipality did not adhere to paragraph 35 of GRAP 1 as accruals for expenditure of R1 390 610 and accruals for employee-related costs of R485 191 were not recorded in the financial records nor were they disclosed in the statement of financial position.
30. Trade creditors were not initially recorded at fair value and subsequently carried at amortised cost. As a result, trade and other payables are overstated by R148 703 (2010: R561 172). Consequently I was unable to obtain sufficient and appropriate audit evidence regarding the existence, classification, valuation and completeness of trade and other payables amounting to R4 550 477 (2010: 8 206 744) as disclosed in the statement of financial position.

Consumer deposits

31. Management could not provide explanations for the difference of R16 004 847 between the amount of R15 107 911 per trial balance on the financial system and the amount of R896 936 as disclosed in the statement of financial position. The municipality did not reconcile the difference of R16 004 847 between the financial statements and the underlying accounting records. I was unable to determine the effect on the other account balances or classes of transactions contained in the financial statements.
32. No supporting documentation was provided to substantiate consumer deposits to the value of R896 936 (2010: R347 083). The financial records did not allow for alternative procedures. Consequently I was unable to obtain sufficient and appropriate audit evidence regarding the valuation, existence and completeness of and the obligations pertaining to consumer deposits.

Unspent conditional grants

33. Management could not provide explanations for the difference of R528 414 between the amount of R10 579 069 per the trial balance on the financial system and the amount of R11 107 483 as disclosed in the statement of financial position. The municipality did not reconcile the difference of R528 414 between the financial statements and the underlying accounting records. I was unable to determine the effect on the other account balances or classes of transactions contained in the financial statements.
34. No supporting documentation was provided to substantiate the unspent conditional grant of R8 146 533 as well as the undefined difference of -R1 043 473 as disclosed in note 16 to the financial statements. The financial records did not allow for alternative procedures. Consequently I was unable to obtain sufficient and appropriate audit evidence regarding the valuation and existence of and the rights and obligations pertaining to unspent conditional grants amounting to R11 107 483 (2010: 2960 950) as disclosed in the statement of financial position.

Leave pay accrual

35. Management did not record the movement in leave accrual on the financial system, resulting in a difference of R161 851 between the amount of R900 079 per trial balance on the financial system and the amount of R1 066 930 as disclosed in the statement of financial position. My audit procedures revealed calculation errors amounting to R315 453 in the leave accrual opening balance of R1 020 379 as disclosed in note 17 to the statement of financial position, resulting in an understatement of leave accruals and an overstatement of the expenditure incurred during the year.

Revenue from non-exchange transactions

Government grants and subsidies

36. A subsidy of R2 500 000 received from the Department of Local Government and Traditional Affairs was not recorded as revenue. As a result, revenue from government grants and subsidies has been understated.
37. A journal entry of R750 000 was passed to grants and subsidies in error. This journal entry has not been adjusted for and, as a result, grants and subsidies have been understated by this amount.
38. Management could not provide explanations for the difference of R2 089 438 between grants and subsidies per the trial balance amounting to R22 373 382 and the amount of R24 462 820 as disclosed in the statement of financial performance. The financial records did not allow for alternative procedures. Consequently, I could not obtain appropriate audit evidence relating to the occurrence, accuracy and completeness of and cut-off for grants and subsidies amounting to R24 462 820 as disclosed in the statement of financial performance.

Property rates

39. The property rates reconciliation indicated that property rates and trade receivables from non-exchange transactions are overstated by R388 062 in terms of paragraph 12 of GRAP 9.

Revenue from exchange transactions

Service charges

40. Management received revenue from pre-paid electricity that had been outstanding from previous years and recorded the full amount as revenue in the current financial year. As a result, revenue from the sale of pre-paid electricity and the accumulated surplus are overstated by R352 720. At year-end, R255 377 (2009: R353 720) in prepaid electricity had not been recorded as revenue. This has resulted in revenue being understated while receivables are understated by the same amount.
41. Meter readings were not captured accurately, resulting in an overstatement of R3 135 581 (2009: R1 772 492) in service charges and receivables disclosed in the statement of financial position. Electricity consumption is invoiced and recognised in the financial records in the month preceding the month in which it was consumed. The practice is in contravention of the GRAP requirements as revenue should be recognised when it occurs. The effect of this contravention is that revenue is not recognised in the correct financial period. Sale of electricity for July 2010 amounting to R785 580 should have been accounted for in the 2009-10 financial year and sales of electricity of R1 680 003 in July 2011 should have been recorded in the 2010-11 financial year. The net effect is that revenue is understated by R894 423, receivables from exchange transactions is understated by R1 680 003 and the opening balance of accumulated surplus is understated by R785 580.
42. Service charges for refuse removal have been incorrectly invoiced on municipal properties. As a result, services charges and trade receivables from exchange transactions are overstated by R777 401.
43. Management was not able to provide sufficient and appropriate evidence to support integrated amounts as identified in the general ledger. The financial records do not allow for alternative procedures. Incorrect tariff rates were used in calculating service

charges. This error has resulted in service charges being overstated by R849 424. Consequently, I was not able to obtain sufficient and appropriate audit evidence on the accuracy, occurrence, cut-off, classification and completeness of service charges revenue of R16 479 813 (2010: R16 134 525) as disclosed in the statement of financial performance.

Interest earned – outstanding receivables

44. Interest on outstanding debtors' balances has been charged at 13.05% throughout the year. In terms of section 97(1)(e) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) and the municipality's credit policy, interest should be charged at prime plus 1%. As a result, trade receivables and interest disclosed in the statement of financial performance have been overstated by R528 290 (2009: R483 996).

Other income

45. Management was not able to provide sufficient and appropriate audit evidence for transactions recorded as other income. Subsequent inspection indicated that these amounts were VAT refunds received from the South African Revenue Service (SARS) amounting to R557 330. As a result, other income is overstated and VAT receivable is understated by R557 330. No explanations were provided to substantiate the difference of R1 543 656 between other income subsidies per the trial balance amounting to R2 017 819 and the amount of R3 561 475 as disclosed in the statement of financial performance. The financial records did not allow for alternative procedures. Consequently, I could not obtain appropriate audit evidence regarding the occurrence, accuracy and completeness of and cut-off for other income amounting to R3 561 474 as disclosed in the statement of financial performance.

Expenditure

Employee cost

46. Management did not provide explanations for the difference of R1 725 147 (2010: R1 705 328) between the amount of R16 522 811 (2010: 16 511 687) disclosed in the statement of financial performance and the amount of R14 797 664 (2010: R14 806 359) as disclosed in note 24 to the financial statements. The financial records did not allow for alternative procedures. Consequently I could not obtain appropriate audit evidence regarding the accuracy and completeness for employee related costs amounting to R14 797 664 (2010: R14 806 359) as disclosed in note 24 to the financial statements.

Bulk expenditure

47. Expenditure relating to the prior year totalling R1 754 386 was incorrectly recorded in the current financial year. Payments to the value of R2 500 00 made by the Department of Local Government and Traditional Affairs on behalf of the municipality were not disclosed in the financial statements. The net effect of these errors is that bulk expenditure is understated by R530 293.

General expenses

48. Management were unable to provide sufficient and appropriate audit evidence regarding the disposal of RDP houses totalling R6 717 985 (2010: R7 390 434). Audit procedures indicated that this expenditure did not occur during the current financial year, resulting in an overstatement of the disposal of RDP houses as disclosed in note 32 to the financial statements.
49. I was unable to obtain sufficient and appropriate audit evidence to substantiate general expenses of R877 023. Management were unable to provide sufficient and appropriate

audit evidence relating to a journal entry passed totalling R833 448. In addition to this, another journal entry was incorrectly processed to the area visits sub-account instead of audit fees, and as a result, audit fees were understated by R2 644 141 and area visits were overstated by R1 474 150. The financial records did not allow for alternative procedures. Consequently, I was not able to obtain sufficient and appropriate audit evidence regarding the occurrence, accuracy, classification and cut-off assertions relating to general expenses amounting to R12 894 242 (2010: 15 588 412).

Grants and subsidies paid

50. Grant expenditure as disclosed in note 31 to the financial statements has not been presented separately in the financial statements as required by GRAP 1 paragraph 36. As a result, R1 359 430 (2010: R4 233 106) of grant expenditure has been incorrectly classified.
51. Management could not provide explanations for the difference of R276 931 between the amount of R1 636 361 per the trial balance on the financial system and the amount of R1 359 430 as disclosed in the statement of financial position.

Statement of changes in net assets

52. The statement of changes in net assets does not cast and contains an error of R2 925 949. As a result of this error, the accumulated surplus figure in the statement of financial position is overstated by R2 925 949 resulting in the statement of financial position not balancing by the same amount.

Cash flow statement

53. The municipality did not adhere to paragraph 19 of GRAP 2 which requires cash flows from operating activities to be reported using the direct method and disclosure of major classes of gross cash receipts and gross cash payments. The cash flow statement contains undefined differences of R2 609 041 (2010: R610 328) which management could not substantiate. The municipality did not receive any proceeds from the sale of property plant and equipment amounting to R722 555 (2010: R621 567) or from suspense accounts amounting to R602 811) as disclosed in the cash flow statement. I could not obtain appropriate and sufficient audit evidence to substantiate the presentation and disclosure of the cash flow statement.

Commitments

54. I was not able to obtain sufficient and appropriated audit evidence regarding the completeness and accuracy of commitments amounting to R7 238 303 (2010: R1 419 682) as disclosed in note 34 to the financial statements. Audit procedures indicated that commitments were understated by R450 105 and not disclosed in note 34 to the financial statements.

Irregular expenditure

55. Irregular expenditure amounting to R803 587 was not disclosed in the financial statements. This was incurred because the municipality transacted with companies owned by state employees and did not adhere to the supply chain regulations 13(c), 44 and 46(2)(f). Irregular expenditure is not completely and accurately disclosed in the financial statements as required by section 125 of the MFMA.

Financial sustainability

56. While the municipality has prepared financial statements on a going concern basis there are a number of indicators that its financial sustainability is under threat. These include the following:
- Revenue is not being collected (see debtor impairments below)

- The budget has been overspent
- Non-/late payment of suppliers

The municipality might not be able to provide uninterrupted services to its community without the support of provincial and national government.

Disclosure

57. Management did not adhere to the requirements of the reporting framework set out in Directive 5 "Determining the GRAP Reporting Framework", as required by section 122(3) of the MFMA. Examples of this are as follows: Management failed to provide a comparison between actual figures and the budget as required by paragraph 12 of GRAP 1. Management also failed to comply with the disclosure requirements of GRAP 3 relating to the change in accounting policy and correction of prior period errors (refer note 36) by not fully disclosing the reason for the change in accounting policy or error, and not disclosing the previously reported account balance, the effect of the change and the new account balance as per the restated comparative figures. Management failed to comply with the disclosure requirement of IFRS 7 by not fully disclosing all risks associated with the financial instruments disclosed as well as disclosing all significant judgements and estimates relating to financial instruments (refer note 48).

Opinion

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

Emphasis of matters

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

Restatement of corresponding figures

60. As disclosed in notes 36 and 37 to the financial statements, certain comparative figures have been restated as a result of prior period and classification errors.

Fruitless and wasteful expenditure

61. As disclosed in note 40 to the financial statements, fruitless and wasteful expenditure of R481 530 was incurred due to interest and penalties paid to SARS for late submissions, and for outstanding electricity accounts and audit fees.

Material losses

62. As disclosed in note 44 to the financial statements, the municipality has incurred estimated losses in the current year of R7 679 458 due to electricity theft and aging electricity infrastructure.

Impairments

63. As disclosed in note 4 to the financial statements, the municipality has impaired R15 938 324 of the trade and other receivables from the exchange transactions balance.
64. As disclosed in note 5 to the financial statements, the municipality has impaired R13 706 107 of the other receivables from the non-exchange transactions balance.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

65. 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 ... to ... and material non-compliance with laws and regulations applicable to the municipality.

Predetermined objectives

Usefulness of information

66. The following criteria are relevant to the findings below:
- Consistency: Objectives, indicators and targets are consistent between planning and reporting documents;
 - Relevance: A clear and logical link exists between the objectives, outcomes, outputs, indicators and performance targets;
67. Audit findings:
- **The reported development priorities are not consistent with the planned priorities**
For selected programmes, 39% of the priorities were not consistent with the planned priorities.
 - **The reported indicators is not consistent with the planned indicators**
For selected programmes, 25% of the indicators were not consistent with the planned indicators.
 - **The reported targets are not consistent with the planned targets**
For selected programmes, 25% of the targets were not consistent with the planned targets.
 - **Changes to planned indicators are not approved**
All the measures and indicators which were changed during the year were not approved by council.
 - **Planned indicators are not relevant to the mandate of the municipality**
The indicators are not directly linked with the strategic objective of the municipality in 22% of the indicators tested.

Reliability of information

68. 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.
69. Audit findings:
- **Reported performance against targets is not valid, accurate and complete when compared to source information**
The reported performance is materially misstated for validity, accuracy and completeness for the programmes infrastructure development, local economic development and financial viability.

Compliance with laws and regulations

Budgets

70. Unforeseeable and/or unavoidable expenditure not provided for in the annual budget was incurred but was then not appropriated in an adjustment budget, as required by section 29(2)(d) of the MFMA.

Annual financial statements and annual report

71. 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 the financial statements receiving a disclaimer of audit opinion.
72. Fruitless and wasteful expenditure disclosed in the financial statements was not communicated to the MEC for local government or the Auditor-General as required by section 32(4) of the MFMA.
73. Various limitations were imposed on the auditors due to a lack of supporting documentation limiting the scope of the audit. This is in contravention of section 15 of the PAA.

HR management

74. Payroll returns for the 2005, 2007 and 2011 tax years have not been submitted to SARS as required by paragraph 14(3) of schedule 4 of the Income Tax Act, 1962 (Act No. 58 of 1962).
75. SDL payments to SARS were not made timeously as required by section 6 of the Skills Development Levies Act of South Africa, 1999 (Act No. 9 of 1999) (SDLA).

Expenditure and supply-chain management

76. Money owing by the municipality was not always paid within 30 days of receiving an invoice or statement, as required by section 65(2)(e) of the MFMA.
77. Audit fees owing by the municipality to the Auditor-General of South Africa were not settled within 30 days as required by section 23(2) of the PAA and sections 65(2)(e) and (f) of the MFMA.
78. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained a management, accounting and information system which recognised expenditure when it was incurred and accounted for creditors of the municipality, as required by section 65(2)(b) of the MFMA.
79. The municipality entered into prohibited transactions with suppliers controlled by state employees in contravention of regulation 44 of the Municipal Supply Chain Management (MSCM) Regulation of May 2005.
80. The municipality procured goods and services with a transaction value of between R2 000 and R10 000 without obtaining at least three written or verbal quotes, which is in contravention of the MSCM Regulations 12(1)(b), 16(a) and 16(c).
81. The municipality procured goods and services with a transaction value of between R10 000 and R30 000 without obtaining at least three written quotes, which is in contravention of MSCM Regulations 12(1)(c) and 17(1)(a).

82. Deviations from the prescribed procurement processes were not disclosed in the notes to the annual financial statements, as required by MSCM Regulation 25(5)(b)(i).
83. Management has not apportioned input VAT in terms of section 17(1) of the VAT Act.
84. VAT returns were not submitted timeously as required by section 28 of the VAT Act.
85. Certain expenditure incurred has not been disclosed as fruitless and wasteful expenditure as required by section 125(2)(d) of the MFMA.
86. The accounting officer did not take reasonable steps to prevent irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Revenue management

87. The credit control and debt collection policy was not adhered to, as required by section 64(2)(a) as the municipality did not have an effective revenue collection system. As a result, the municipality has not adhered to the requirements of section 96 of the MSA.
88. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained a management, accounting and information system which recognised revenue when it is earned, accounted for debtors or correctly accounted for receipts of revenue, as required by section 64(2)(e) of the MFMA.

Asset management

89. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained a management, accounting and information system which accounts for the assets of the municipality as required by section 63(2)(a) of the MFMA.
90. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained an effective system of internal control for assets (including an asset register) as required by section 63(2)(c) of the MFMA.
91. The municipality is operating its landfill sites without a permit in contravention of schedule 1 (section 19) of the National Environmental Management: Waste Act of South Africa, 2008 (Act No. 59 of 2008).

INTERNAL CONTROL

92. 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 disclaimer of opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

93. During the period under review, the accounting officer failed to exercise oversight responsibility over the preparation of financial statements, reporting on predetermined objectives, compliance with the laws and regulations and internal control.
94. This was evident from the numerous instances of non-compliance with laws and regulations, the findings on reporting against predetermined objectives and material misstatements identified in the financial statements that were noted throughout the

audit process. This is of particular concern given the fact that none of internal audit and audit committee's recommendations appear to have been implemented.

- 95. Availability of key staff was an ongoing challenge for the duration of the audit.
- 96. There is over-reliance on the external service providers for the information technology (IT) functions of the municipality.

Financial and performance management

- 97. The municipality's systems for record-keeping do not function adequately. This resulted in some information not being supplied for audit purposes.
- 98. The processing of and reporting on financial and predetermined objectives were inadequate to ensure that reliable and complete reports were produced and submitted for audit purposes. This has resulted in the disclaimed audit opinion on the financial statements as well as the findings on predetermined objectives.
- 99. The municipality's controls to ensure compliance with relevant laws and legislation are not functioning adequately, hence the numerous instances of non-compliance with laws and regulations identified.
- 100. In addition to the above, the information systems control environment is weak. This puts the municipality at great risk since it is heavily reliant on its IT systems for performing day-to-day and reporting activities.

Governance

- 101. Risk identification and management processes are not designed to identify changes in processes or risks and to verify that the design of underlying controls remains effective. The municipality has not selected and developed internal controls to prevent, detect and correct material misstatements in financial reporting and reporting on predetermined objectives.
- 102. An internal audit function was established during the year however; there is no evidence to indicate that recommendations are being implemented to mitigate material risks identified.
- 103. The audit committee was in place for the full period under review and is independent of management.

Auditor - General.

East London
30 November 2011



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence