

Audit Report

Elundini Municipality

For the Year ended 30 June 2011

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

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the Elundini 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 XX to XX.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and 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 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 about whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

7. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Elundini Municipality as at 30 June 2011, and its financial performance and cash flows for the year then ended in accordance with GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

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

Significant uncertainties

9. Enquiries of management and the attorneys revealed that the municipality is a defendant in several lawsuits. The potential loss arising from these lawsuits is R1.85 million as disclosed in note 45 to the financial statements. The outcome of these lawsuits cannot be determined at present and no provision has been made for any liability that may result.

Restatement of corresponding figures

10. As disclosed in notes 28 and 29 to the financial statements, the corresponding figures which relate to the year ended 30 June 2010 have been restated as a result of the early adoption of GRAP 104 on financial instruments as well as reclassifications and errors discovered during the current financial year.

Unauthorised expenditure

11. As disclosed in note 35.1, unauthorised expenditure amounting to R1.18 million was incurred during the year ended 30 June 2011. This was due to overspending of budget on certain votes.

Fruitless and wasteful expenditure

12. The municipality incurred fruitless and wasteful expenditure of R11 021 relating to interest and penalties as disclosed in note 35.2 to the financial statements. The balance of fruitless and wasteful expenditure relating to the 2009/10 financial year has been condoned by Council.

Material losses

13. The municipality suffered significant electricity losses of 6 430 721 kWh with a value of R3.7 million during the year under review as disclosed in note 35.4 to the financial statements. The municipality also suffered water losses of 314 868 mega litres with a value of R2.4 million as disclosed in note 35.4 to the financial statements.

Material impairments

14. The municipality listed outstanding debtors totalling R60.02 million at 30 June 2011, for which the recoverability is considered to be doubtful. This is disclosed in notes 14 and 15 to the financial statements.

Material underspending of the budget

15. The municipality has materially underspent on its capital budget. As disclosed in note 34.3 to the financial statements R36.43 million of the capital budget remained unspent at 30 June 2011.

Additional matter

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

Unaudited supplementary schedules

17. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. We have not audited these schedules and, accordingly, we do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

18. 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 and material non-compliance with laws and regulations applicable to the Municipality.

Predetermined objectives

Presentation of information

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

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

20. Audit finding:

- **The annual performance report did not contain measures to improve performance**

The annual performance report did not contain measures taken to improve performance where objectives were not met, as required by regulation 13(2) of the Municipal Planning and Performance Management Regulations.

Usefulness of information

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

- Consistency: Objectives, indicators and targets are consistent between planning and reporting documents

22. Audit findings:

- **Performance objectives are not consistent**

Fifty eight percent of the selected reported performance objectives are not consistent with the Service Delivery and Budget Implementation Plan (SDBIP) and Integrate Development Plan (IDP), as required by section 26(i) of the Municipal Systems Act (MSA), read together with paragraph 4, page 2 of the MFMA Circular 13.

- **Changes to the objectives of the approved annual performance plan were not disclosed and explained**

Changes to the objectives of the approved annual performance plan for the year under review, were not disclosed and explained as required in terms of the relevant National Treasury preparation guide. Of the 12 objectives included in the original IDP, only eight of these were in the balance scorecard. In addition the balanced scorecard includes an additional 42 objectives that were not initially included in the IDP.

Reliability of information

23. 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

24. Audit findings:

- **Non-submission of source documentation to verify the actual achievements**

The non-submission of source documentation to verify the actual achievements disclosed in the annual performance report has resulted in a limitation of scope and as such, impeded our ability to determine if the reported performance statistics are complete, accurate and valid. Of the selected objectives, 44% could not be verified for validity, accuracy and completeness.

- **Non-compliance not affecting the fair presentation of the report on predetermined objectives**

The municipality did not follow the prescribed process in terms of sections 27, 28, 29, 30, 31, 32 and 34(b) of the MSA, as well as regulation 3 of the Local Government: Municipal Planning and Performance Management Regulations relating to the implementation of a new balanced scorecard. A council resolution passed on 17 September 2010 resolved that a new, improved balanced scorecard would supersede the institutional balanced scorecard in the IDP, which was adopted on 15 June 2010.

- **No allocation of budget amounts**

The municipality did not allocate budget amounts for each strategic objective/priority as required by Section 6 of the Local Government: Municipal Planning and Performance Management Regulations.

Compliance with laws and regulations

Budgetary reporting

25. The municipality incurred expenditure that was not budgeted for, in contravention of section 15 of the MFMA.

Procurement and contract management

26. Sufficient appropriate audit evidence could not be obtained that bid specifications were drafted by bid specification committees which were composed of one or more officials of the municipality as required by Supply Chain Management (SCM) regulation 27(3).
27. Bids were not always evaluated by bid evaluation committees which were composed of at least one SCM practitioner of the municipality as per the requirements of SCM regulation 28(2).

Material underspending of the budget

28. The municipality has materially underspent on its capital budget. As disclosed in note 34.3 to the financial statements R36.43 million of the capital budget remained unspent at 30 June 2011.

Expenditure management

29. The accounting officer did not take reasonable steps to prevent fruitless and wasteful expenditure, as required by section 95(d) of the MFMA.

INTERNAL CONTROL

30. 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 findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

31. In the year under review, the leadership structure has been stable and has worked to implement action plans to address prior year audit findings. This has had a positive impact on the number of audit findings raised. However a lack of formal controls over the IT systems was noted, resulting in findings relating to security, access control, program change management and disaster recovery.

32. The findings linked to non-compliance are as a result of a skills shortage within the surrounding areas of the municipality, creating challenges relating to the recruitment and retention of suitable skilled employees.

Financial and performance management

33. Inconsistencies were noted between the IDP, SDBIP and performance report through our audit of performance objectives due to incorrect information being submitted for audit purposes. The lack of formal controls in the IT systems has resulted in the reliability, availability and protection of information potentially being compromised.

Governance

34. Insufficient action was taken by the governance structures within the municipality to ensure that risks relating to the monitoring and reporting of performance objectives and compliance with laws and regulations were addressed thus resulting in repeat audit findings in this area.

Auditor - General.

East London

30 November 2011



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence