

Audit Report

Sakhisizwe Municipality

For the Year ended 30 June 2012



AUDITOR - GENERAL
SOUTH AFRICA

The Accounting Officer
Sakhisizwe Local Municipality
PO Box 21

5460

30 November 2012

Reference: 03564REG11-12

Dear Sir

Report of the Auditor-General on the financial statements and other legal and regulatory requirements of Sakhisizwe Local Municipality for the year ended 30 June 2012

1. The above-mentioned report of the Auditor-General is submitted herewith in terms of section 21(1) of the Public Audit Act of South Africa read in conjunction with section 188 of the Constitution of the Republic of South Africa section 121(3) of the Municipal Finance Management Act of South Africa (MFMA).
2. In terms of section 121(4) of the MFMA you are required to include the audit report in the municipal entity's annual report to be tabled.
3. Until the annual report is tabled as required by section 127(2) of the MFMA the audit report is not a public document and should therefore be treated as confidential.
4. Prior to printing or copying the annual report which will include the audit report you are required to do the following:
 - Submit the final printer's proof of the annual report to the relevant senior manager of the Auditor-General of South Africa for verification of the audit-related references in the audit report and for confirmation that the financial statements and other information are those documents that have been read and audited. Special care should be taken with the page references in your report, since an incorrect reference could have audit implications.
 - The signature *Auditor-General* in the handwriting of the auditor authorised to sign the audit report at the end of the hard copy of the audit report should be scanned in when preparing to print the report. This signature, as well as the place and date of signing and the Auditor-General of South Africa's logo, should appear at the end of the report, as in the hard copy that is provided to you. The official logo will be made available to you in electronic format.
5. Please notify the undersigned Senior Manager well in advance of the date on which the annual report containing this audit report will be tabled.
6. Your cooperation to ensure that all these requirements are met would be much appreciated.

Kindly acknowledge receipt of this letter.

Yours sincerely

Signed


.....
Senior Manager: EL08

Enquiries: John Whittal
Telephone: (043) 709 7200
Fax: (043) 709 7300

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

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Sakhisizwe Local Municipality, which comprise the statement of financial position as at 30 June 2012, 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.

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 (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2011 (Act No. 6 of 2011) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. 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.
4. 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.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for qualified opinion

Irregular expenditure

6. Section 125(2) of the MFMA requires the financial statements of the municipality to disclose material irregular expenditure that occurred during the financial year. Audited payments amounting to R16,1 million (2011: R5,4 million) were irregular, as they were made in contravention of the supply chain management (SCM) requirements. These amounts were not included in the irregular expenditure disclosed in note 44 to the financial statements. Consequently, the irregular expenditure disclosed is understated by at least this amount. However, it was not practicable to determine the full extent of the understatement, as there

was no system of control to identify the completeness thereof.

Comparative amounts

7. During the 2010-11 financial year, I was unable to obtain sufficient appropriate audit evidence concerning the value of commitments to be disclosed in note 37 to the financial statements. I was unable to obtain sufficient appropriate audit evidence for the above by alternative means. Consequently, I was unable to determine whether any adjustments to these amounts were necessary. My audit opinion on the financial statements for the period ended 30 June 2011 was modified accordingly. My opinion on the current period's financial statements is also modified because of the possible effect of this matter on the comparability of the current period's figures.

Qualified opinion

8. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Sakhisizwe Local Municipality as at 30 June 2012, and its financial performance and cash flows for the year then ended in accordance with SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

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

Restatement of corresponding figures

10. As disclosed in note 39 to the financial statements, the corresponding figures for the year ended 30 June 2011 have been restated as a result of errors discovered during the current financial year in the financial statements of the municipality at, and for the year ended, 30 June 2011.

Unauthorised expenditure

11. As disclosed in note 42 to the financial statements, the municipality incurred unauthorised expenditure of R10,4 million, as a result of expenditure incurred in excess of the total approved budget.

Additional matter

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

Unaudited supplementary schedules

13. The supplementary information set out on page ... does not form part of the financial statements and is presented as additional information. I have not audited this schedule and, accordingly, I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

14. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

15. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages ... to ... of the annual report.
16. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).
17. The reliability of the information in respect of the selected objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).
18. The material findings are as follows:

Usefulness of information

Consistency

19. Section 41(c) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) requires the integrated development plan (IDP) to form the basis for the annual report, therefore requiring the consistency of objectives, indicators and targets between planning and reporting documents. A total of 101 reported objectives in the annual report were not consistent with the 16 objectives as per the approved IDP. This was due to the absence of a performance management system.

Measurability

20. The FMPPI requires that indicators should have clear, unambiguous data definitions so that data can be collected consistently and is easy to understand and use. A total of 80% of the indicators were not well defined in that clear, unambiguous data definitions were not available to allow for data to be collected consistently. This was due to the fact that management was not aware of the requirements of the FMPPI.
21. The FMPPI requires that the time period or deadline for delivery be specified. All targets were not time bound in specifying a time period or deadline for delivery. This was due to the fact that management was not aware of the requirements of the FMPPI.
22. The FMPPI requires that performance targets be specific in clearly identifying the nature and required level of performance. All targets were not specific in clearly identifying the nature and the required level of performance. This was due to the fact that management was not aware of the requirements of the FMPPI.

Relevance

23. The FMPPI requires that the indicator should relate logically and directly to an aspect of the institution's mandate or the realisation of strategic goals and objectives. A total of 48% of the indicators did not relate logically and directly to an aspect of the institution's mandate or realisation of strategic goals and objectives as per the five-year IDP. This was due to proper performance planning and management practices not having been developed and implemented to provide for the development of performance indicators and targets included in the IDP.

Reliability of selected objectives in the annual performance report

Validity and accuracy

24. The FMPPI requires that processes and systems that produce the indicator should be verifiable and accurate enough for its intended use and respond to changes in the level of performance. A total of 69% of the actual reported indicators were not valid and accurate when compared to source information or evidence provided. This was due to a lack of standard operating procedures for the recording of actual achievements by senior management.

Completeness

25. The FMPPI requires that documentation addressing the systems and processes for identifying, collecting, collating, verifying and storing information be properly maintained. A total of 71% of the actual reported performance for the selected objectives was not completely recorded. This was due to an improper document management system with regard to actual performance achievements.

Additional matter

26. I draw attention to the matter below. This matter does not have an impact on the audit findings on predetermined objectives reported above.

Achievement of planned targets

27. Of the total number of planned targets, only 130 were achieved during the year under review. This means that 41% of the total planned targets were not achieved during the year under review. This was mainly due to the fact that indicators and targets were not suitably developed during the strategic planning process.

Compliance with laws and regulations

28. I performed procedures to obtain evidence that the entity has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the General Notice issued in terms of the PAA are as follows:

Strategic planning and performance management

29. 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 MSA and the principles specified in the FMPPI.
30. The accounting officer of the municipality did not by 25 January submit the mid-year budget and performance assessment report to the mayor, the National Treasury or the relevant provincial treasury, as required by section 72(1)(b) of the MFMA.

Budgets

31. The municipality incurred expenditure in excess of the limits of the amounts provided for in the votes in the approved budget, in contravention of section 15 of the MFMA.
32. The accounting officer did not submit the budget within 10 days of the end of each month to

the mayor and the relevant provincial treasury, as prescribed by section 71(1) of the MFMA.

Annual financial statements, performance report and annual report

33. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA, as material misstatements of assets, liabilities, revenue, expenditure and disclosures were identified by the auditors and subsequently corrected. However, the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.
34. The accounting officer did not make the 2010-11 annual report public immediately after it had been tabled in the council, as required by section 127(5) of the MFMA.
35. The accounting officer did not make the oversight report public within seven days of its adoption by the council, as required by section 129(3) of the MFMA.

Audit committee

36. The audit committee functioning as the performance audit committee did not advise the council and management staff of the municipality on performance evaluation, as specified by section 166(2)(a) of the MFMA.

Internal audit

37. The municipality's internal audit function did not submit quarterly reports on its audits of performance measurement to the municipal manager and the performance audit committee, as stipulated by Municipal Planning and Performance Management Regulation 14(1)(c).

Procurement and contract management

38. Sufficient appropriate audit evidence could not be obtained that certain goods and services with a transaction value below R200 000 were procured by means of obtaining the required price quotations, as required by SCM Regulation 17(a) and (c).
39. Quotations were accepted from prospective providers who are not registered on the list of accredited prospective providers and do not meet the listing requirements prescribed by the SCM policy, in contravention of SCM Regulations 16(b) and 17(b).
40. Certain goods and services with a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM Regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM Regulation 36(1).
41. Bid specifications for the procurement of goods and services through competitive bids were drafted in a biased manner that did not allow all potential suppliers to offer their goods or services, in contravention of SCM Regulation 27(2)(a).
42. Bid specifications were not always drafted by bid specification committees composed of one or more officials of the municipality, as required by SCM Regulation 27(3).
43. Invitations for competitive bidding were not always advertised for the required minimum period, as required by SCM Regulation 22(1) and (2).
44. Sufficient appropriate audit evidence could not be obtained that bids had been evaluated by bid evaluation committees composed of officials from the departments requiring the goods or services and at least one SCM practitioner of the municipality, as required by SCM

Regulation 28(2).

45. Contracts and quotations were awarded to bidders based on points given for criteria that differed from those stipulated in the original invitation for bidding and quotations, in contravention of SCM Regulations 21(b) and 28(1)(a) and the Preferential Procurement Regulations.
46. Bid adjudication was not always done by committees composed in accordance with SCM Regulation 29(2).
47. Awards were made to bidders other than those recommended by the bid evaluation committee without ratification by the accounting officer, as required by SCM Regulation 29(5)(b).
48. Sufficient appropriate audit evidence could not be obtained that councillors of the municipality did not participate in committees evaluating or approving tenders or quotations or attended meetings of committees evaluating or approving tenders or quotations, in contravention of section 117 of the MFMA.
49. The preference point system was not applied in all procurement of goods and services above R30 000, as required by section 2(a) of the Preferential Procurement Policy Framework Act of South Africa, 2000 (Act No. 5 of 2000) (PPPFA) and SCM Regulation 28(1)(a).
50. Contracts and quotations were awarded to bidders based on preference points that were not allocated in accordance with the requirements of the PPPFA and its regulations.
51. Contracts and quotation were awarded to bidders that did not score the highest points in the evaluation process, contrary to section 2(1)(f) of the PPPFA.
52. Contracts were extended without tabling the reasons for the proposed amendment in the council of the municipality, as required by section 116(3) of the MFMA.
53. Contracts were extended or modified without the approval of a properly delegated official, as required by SCM Regulation 5.
54. The performance of contractors and providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
55. Contract performance and monitoring measures and methods were insufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA.
56. Construction contracts were awarded to contractors who were not registered with the Construction Industry Development Board (CIDB) and/or did not qualify for the contract, contrary to section 18(1) of the Construction Industry Development Board Act of South Africa, 2000 (Act No. 38 of 2000) (CIDB Act) and CIDB Regulations 17 and 25(7A).
57. Construction projects were not always registered with the CIDB, as required by section 22 of the CIDB Act and CIDB Regulation 18.
58. Contracts and quotations were awarded to providers whose tax matters had not been declared by the South African Revenue Service to be in order, as required by SCM Regulation 43.
59. Contracts and quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM Regulation 13(c).

60. Awards were made to providers who are persons in the service of other state institutions, in contravention of SCM Regulation 44. Similar awards were identified in the prior year and no effective steps had been taken to prevent or combat the abuse of the SCM process in accordance with SCM Regulation 38(1).
61. The accounting officer failed to implement measures to combat the abuse of the SCM system as per the requirements of SCM Regulation 38(1), as awards were made to providers without verifying whether the supplier:
 - during the last five years, failed to perform satisfactorily on a previous contract with the municipality or municipal entity or other organ of state
 - committed a corrupt or fraudulent act in competing for the contract
 - abused the SCM system of the municipality
 - had been convicted of fraud or corruption during the past five years.
62. Allegations of improper conduct and/or failure to comply with the SCM system laid against officials were not investigated, as required by SCM Regulation 38(1)(b).
63. Appropriate action was not taken against officials where investigations proved improper conduct and/or failure to comply with the SCM system, as required by SCM Regulation 38(1)(b).

Expenditure management

64. The accounting officer did not take reasonable steps to prevent unauthorised, irregular as well as fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.
65. Unauthorised, irregular as well as fruitless and wasteful expenditure was not recovered from the liable person, as required by section 32(2) of the MFMA.
66. The accounting officer did not inform the mayor or the member of the executive council for local government of any unauthorised, irregular or fruitless and wasteful expenditure incurred by the municipality, whether any person is responsible or under investigation for such expenditure, as well as the steps taken to recover or rectify such expenditure and to prevent a recurrence of such expenditure, as stipulated by section 32(4) of the MFMA.
67. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained an effective system of expenditure control, including procedures for the approval, authorisation, withdrawal and payment of funds, as specified by section 65(2)(a) to (d) of the MFMA.
68. The accounting officer did not ensure that payments were made within 30 days of receiving the relevant invoice or statement, as specified by section 65(2)(e) of the MFMA.

Conditional grants

69. The municipality did not submit quarterly performance reports to the provincial treasury and the National Treasury within 30 days after the end of each quarter, as required by section 12(2)(c) of DoRA.
70. The municipality did not evaluate its performance in respect of programmes funded by the allocation or submit the evaluation to the transferring national officer within two months after the financial year-end, as required by section 12(6) of DoRA.

71. The municipality did not timeously submit project registration forms for projects it intended to implement in the financial year under review to the Department of Local Government, as required by the DoRA Framework issued in Gazette No. 34280.
72. The municipality did not submit project implementation plans to the national Department of Cooperative Governance and Traditional Affairs (CoGTA), as required by the Division of Revenue Grant Framework issued in Gazette No. 34280.
73. The municipality did not register its master plans for bulk infrastructure with the integrated national electrification programme, as required by the Division of Revenue Grant Framework issued in Gazette No. 34280.
74. The municipality did not submit MFMA implementation plans to the National Treasury to address weaknesses in financial management, as required by the Division of Revenue Grant Framework issued in Gazette No. 34280.
75. The municipality did not submit its signed activity plan to CoGTA, or did not submit it in the prescribed format, contrary to the Division of Revenue Grant Framework issued in Gazette No. 34280.
76. The municipality did not submit its monthly expenditure reports to CoGTA within 20 days after the end of each month, as required by the Division of Revenue Grant Framework issued in Gazette No. 34280.

Internal control

77. I considered internal control relevant to my audit of the financial statements, report on predetermined objectives and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for the qualified opinion, the findings on the report of predetermined objectives and the findings on compliance with laws and regulations included in this report.

Leadership

78. There was a lack of oversight and accountability by senior management as sufficient monitoring controls were not in place to ensure the proper implementation of internal policies at an operational level. As a result the municipality did not prevent and detect irregular expenditure incurred through non adherence to supply chain prescripts.
79. The municipality has not developed, documented and approved internal policies and procedures to address the collection, recording, processing, monitoring and reporting on predetermined objectives. Consequently the annual performance report was not useful or reliable.

Financial and performance management

80. The municipality did not have a proper system of record management that provides for the maintenance of information that supports the reported information contained in the annual performance report. This includes information which relates to the collection, collation, verification, storing and reporting of actual performance information. As a result the annual performance report was not useful or reliable.
81. The municipality did not have adequate systems for the complete and accurate financial reporting of irregular expenditure, commitments and depreciation. This is as a result of inadequate in-year monitoring of expense transactions to ensure that SCM requirements were fully adhered to. Whilst for commitments and depreciation the commitments register was not maintained throughout the year and asset useful lives incorrectly assessed with the result that

both had to be corrected during the audit.

82. The municipality did not adequately assign responsibility and implement processes to monitor compliance with the approved budget and ensure compliance with all applicable laws and regulations. The municipality thus incurred unauthorised expenditure and did not fully comply with all the requirements of the MFMA, MSA and SCM Regulations.

Governance

83. The municipality did not conduct a risk assessment as required by the MFMA. Consequently, there was failure to monitor compliance with the MFMA, MSA and SCM regulations. In addition, non compliance with the GRAP reporting framework requirements was noted.
84. The performance audit committee and the internal audit function did not have the necessary capacity to review or report on the performance management system or performance reports during the year under review. The municipality thus lost the benefit that may have been obtained had these reports been completed

Auditor General.

East London

30 November 2012



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence