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

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Gariep Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2012, the statement of financial performance, statement of changes in net assets and the cash flow statement for the year then ended, and the notes, comprising 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 Generally Recognised Accounting Practice (GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 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 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

Property, plant and equipment

6. GRAP 17 requires that an item of property, plant and equipment that qualifies for an asset to be measured at cost or revaluation model. The municipality did not recognise and measure property, plant and equipment in accordance with GRAP 17. Infrastructure assets as disclosed in note 4 were not accurately valued in the financial statements. Consequently, property, plant and equipment and accumulated surplus is understated by R10.3 million.

7. In addition, sufficient appropriate audit evidence was not available for the amounts disclosed as land and buildings in note 4 to the financial statements and hence I was unable to verify the valuation of land and buildings. The municipality's records did not permit the application of alternative audit procedures. Consequently property, plant and equipment and accumulated surplus is overstated by R26.7 million.

Cash and cash equivalents

8. Contrary to the requirements of section 62 of the MFMA the municipality did not have adequate systems in place to investigate and clear prior year reconciling items. The balance per the cash book did not agree to the general ledger which resulted in cash and cash equivalents, as disclosed in note 10 of the annual financial statements, being overstated by R3.8 million in the current year and by R10.3 million in the prior year.

Investment property

9. The municipality adopted the fair value model for the recognition and measurement of investment property. GRAP 16 requires investment property to reflect the market conditions at reporting date. The municipality used historical cost to measure investment property at the reporting date. Consequently investment property as disclosed in note 3 and accumulated surplus to the annual financial statements is understated by R12.7 million.

VAT receivable – Prior year misstatement

10. The municipality was unable to reconcile the VAT receivable of R963 567 as disclosed in the statement of financial position, to the returns submitted to the South African Revenue Services (SARS). The municipality's records did not permit the application of alternative audit procedures to audit this balance. Consequently, I was not able to verify the completeness, existence and valuation of the VAT receivable disclosed on the statement of financial position.

Qualified Opinion

In my opinion, except for the 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 Gariep municipality as at 30 June 2012 and its financial performance and cash flows for the year then ended, in accordance with applicable GRAP financial reporting framework and the requirements of the MFMA.

Emphasis of matters

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

Significant uncertainties

12. The municipality may be liable for a penalty of R10 million for not obtaining a license for five landfill sites which are in use as disclosed in note 34.

Restatement of corresponding figures

13. Misstatements were identified during my audit of the financial statements of the current financial year. Management corrected the misstatements by restating the corresponding figures relating to:

    - Property, plant and equipment as disclosed in note 4,
    - Receivables as disclosed in note 9,
    - Finance lease liability as disclosed in note 11,
    - Unspent conditional grants as disclosed in note 12,
    - Provisions as disclosed in note 13,
    - Other long term employee benefits as disclosed in note 15,
    - Trade payables as disclosed in note 16,
    - Revenue as disclosed in note 18,
    - Unauthorised expenditure as disclosed in note 41,
    - Fruitless and wasteful expenditure as disclosed in note 42,
    - Irregular expenditure as disclosed in note 43.

Financial sustainability

14. 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 under collected,
    - Loans are not being paid timeously,

24. This is due to the lack of review of objectives, indicators and targets set during strategic planning.

Measurability

25. The National Treasury Framework for managing programme performance information (FMPPI) requires that performance targets be specific in clearly identifying the nature and required level of performance. A total of 42% of the targets were not specific in clearly identifying the nature and the required level of performance. This was due to the fact that management was aware of the requirements of the FMPPI but did not receive the necessary training to enable application of the principles.

26. The National Treasury Framework for managing programme performance information (FMPPI) requires that the time period or deadline for delivery be specified. A total of 33% of the targets were not time bound in specifying a time period or deadline for delivery. This was due to the fact that management was aware of the requirements of the FMPPI but did not receive the necessary training to enable application of the principles.

27. The National Treasury Framework for managing programme performance information (FMPPI) requires that indicators/measures should have clear unambiguous data definitions so that data is collected consistently and is easy to understand and use. A total of 45% 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 aware of the requirements of the FMPPI but did not receive the necessary training to enable application of the principles.

28. The National Treasury Framework for managing programme performance information (FMPPI) requires that it must be possible to validate the processes and systems that produce the indicator. A total of 45% of the indicators were not verifiable in that valid processes and systems that produce the information on actual performance did not exist. This was due to the fact that management was aware of the requirements of the FMPPI but did not receive the necessary training to enable application of the principles.

Relevance

29. The National Treasury Framework for managing programme performance information (FMPPI) requires that the indicator should relate logically and directly to an aspect of the institution's mandate, the realisation of strategic goals and objectives. A total of 26 % of indicators did not relate logically and directly to an aspect of the institution's mandate and realisation of strategic goals and objectives as per the three-year integrated development plan. This was due to the lack of development and implementation of proper performance planning and management practices to provide for the development of performance indicators and targets included in the integrated development plan.

Reliability of information

Validity

30. The National Treasury Framework for managing programme performance information (FMPPI) requires that processes and systems which produce the indicator should be verifiable. I was unable to obtain all the information and explanations I considered necessary to satisfy myself as to the validity of the actual reported performance relevant

to 72% of development priorities. This was due to the institution's records not permitting the application of alternative audit procedure.

Accuracy

31. The National Treasury Framework for managing programme performance information (FMPPI) requires that the indicator be accurate enough for its intended use and respond to changes in the level of performance. I was unable to obtain all the information and explanations I considered necessary to satisfy myself as to the accuracy of the actual reported performance relevant to 72% of development priorities. This was due to the institution's records not permitting the application of alternative audit procedures.

Additional matter

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

Achievement of planned targets

33. Of the total number of 81 targets planned for the year, 23 of targets were not achieved during the year under review. This represents 28% of total planned targets that were not achieved during the year under review.

34. 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

35. 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.

Strategic planning and performance management

36. The municipality did not set appropriate key performance indicators as a yardstick for measuring performance, including outcomes and impact, with regard to the municipality's development priorities and objectives set out in its integrated development plan.

Budgets

37. 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 Municipal Finance Management Act.

Annual financial statements, performance and annual report

38. 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 qualified opinion.

39. The municipal council did not adopt an oversight report, containing comments on the annual report, within two months from the date on which the 2011 annual report was tabled, as required by section 129(1) of the Municipal Finance Management Act.

40. A written explanation was not submitted to council setting out the reasons for the delay in the tabling of the 2011 annual report in the council, as required by section 127(3) of the Municipal Finance Management Act.

41. The 2011 annual report was not tabled in the municipal council within seven months after the end of the financial year, as required by section 127(2) of the Municipal Finance Management Act.

42. The accounting officer did not make the 2011 annual report public immediately after the annual report was tabled in the council, as required by section 127(5)(a) of the Municipal Finance Management Act.

43. The accounting officer did not make public the council's oversight report on the 2011 annual report within seven days of its adoption, as required by section 129(3) of the Municipal Finance Management Act.

Internal audit

44. Internal audit did not report to the audit committee on matters relating to compliance with the Municipal Finance Management Act, the Division of Revenue Act and other applicable legislation as required by section 165(2)(b) of the MFMA.

45. The internal audit did not audit the results of performance measurements, as required by section 45(1)(a) of the Municipal Systems Act and Municipal Planning and Performance Management Regulation 14(1)(a).

46. The internal audit unit did not assess the functionality of the performance management system, whether the performance management system complied with the requirements of the Municipal Systems Act and the extent to which the performance measurements were reliable in measuring the performance of the municipality on key and general performance indicators, as required by Municipal Planning and Performance Management Regulation 14(1)(b).

47. The internal audit unit did not audit the performance measurements on a continuous basis and, as required by Municipal Planning and Performance Management Regulation 14(1)(c).

Expenditure management

48. 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 and TR 8.2.3.

49. The accounting officer did not take reasonable steps to prevent unauthorized expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA and section 95(d) of the Municipal Finance Management Act .

Revenue management

50. Interest was not charged on all accounts in arrears as, required by section 64(2)(g) of the Municipal Finance and Management Act.