

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

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of Amahlathi Municipality set out on pages ... to ..., which comprise statement of financial position as at 30 June 2013, the statement of financial performance, statement of changes in net assets, the cash flow statement for the year then ended, the statement of comparison of budget and actual amounts, and the notes, comprising a summary of significant accounting policies.

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 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 audit opinion.

Opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of Amahlathi Municipality as at 30 June 2013 and its financial

performance and cash flows for the year then ended, in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

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

Restatement of corresponding figures

8. As disclosed in note 43 and 44 to the financial statements, the corresponding figures have been restated as a result of a change in accounting policy and errors only corrected during the year ended 30 June 2013 that existed in the financial statements at, and for the year ended, 30 June 2012.

Material under-spending of the conditional grant

9. As disclosed in note 26 to the financial statements the municipality under-spent the municipal infrastructure grant funding by R7.5 million. As a consequence the municipality did not achieve its objectives on roads infrastructure.

Material impairments

10. Debt impairments of R4.4 million as disclosed in note 32 to the financial statements were made against trade debts. These debts are long outstanding and considered to be irrecoverable.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

11. 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

12. 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.
13. 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 development priorities. 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 Framework for managing programme performance information (FMPP)*.
14. The reliability of the information in respect of the selected development priorities is

assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete). The material findings are as follows:

Usefulness of information

Presentation

15. Section 46 of the Municipal Systems Act 2000 (Act No. 32 of 2000) (MSA) requires disclosure in the annual performance report of measures taken to improve performance where planned targets were not achieved. Measures to improve performance for a total of 33% of the planned targets not achieved were not reflected in the annual performance report. This was due to the lack of review of the presentation of the annual performance report by management.

16. Section 46 of the MSA requires disclosure in the annual performance report of measures taken to improve performance where planned targets were not achieved. Adequate and reliable corroborating evidence could not be provided for 67% measures taken to improve performance as disclosed in the annual performance report. The municipality's records did not permit the application of alternative audit procedures due to absence of information system and procedures to be applied for the reported performance targets. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the reliability of the measures taken to improve performance.

Measurability

Performance indicators not specific

17. The FMPPI requires that performance targets be specific in clearly identifying the nature and required level of performance. A total of 21% of the targets and significantly important targets in relation to the service delivery of the municipality were not specific in clearly identifying the nature and the required level of performance. This is due to the municipality not having a formal policy in place to govern the performance of and reporting of predetermined objectives that ensures that all laws and regulations are met and that targets set are in accordance with legislation.

Performance indicators not time bound

18. The FMPPI requires that the time period or deadline for delivery be specified. A total of 64% of the targets relevant to infrastructure and service delivery were not time bound in specifying a time period or deadline for delivery. This is due to the municipality not having a formal policy in place to govern the performance and reporting of predetermined objectives that ensures that all laws and regulations are met and that targets set are in accordance with legislation.

Performance indicators not well-defined

19. The FMPPI requires that indicators should have clear unambiguous data definitions so that data is collected consistently and is easy to understand and use. A total of 21% of the indicators and significantly important indicators in relation to service delivery were not well defined in that clear, unambiguous data definitions were not available to allow for data to be collected consistently. This is due to management not having a system in place for collection, coordination and compilation of the reported performance information.

Performance indicators not verifiable

20. The FMPPI requires that it must be possible to validate the processes and systems that produce the indicator. A total of 21% 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 lack of key controls, policies and procedures in the relevant systems of collection, collation, verification and storage of actual performance information.

Reliability of information

21. The FMPPI requires that institutions should have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. The information presented with respect to the selected development priority to infrastructure and service delivery was not reliable when compared to the source information and evidence provided.
22. This was due to the lack of standard operating procedures for the accurate recording of actual achievements and that completeness of source documentation in support of actual achievements was not monitored.

Compliance with laws and regulations

23. 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

24. The municipality did not determine the frequency of reporting and the lines of accountability for performance as required by regulation 7(2)(e) of the Municipal Planning and Performance Management Regulation (MPPMR).
25. The municipality did not provide for procedures by which the system is linked to the municipality's integrated development planning processes, as required by MPPMR 7(2)(g).
26. The municipality had set performance targets with regard to each development priority and objective and key performance indicators as per the integrated development plan (IDP), however these targets were not measurable as required by section 41(1)(b) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) and MPPMR regulations 12(1) and 12(2)(e).
27. The performance management system of the municipality did not provide for the monitoring of performance and for the measuring and review of performance at least once per year, with regard to each of those development priorities and objectives and against the key performance indicators and targets set, as required by section 41 of the MSA.
28. The municipality did not take steps to improve performance with regard to the development priorities and objectives where performance targets were not met, as required by section 41(1)(d) of the MSA.
29. The municipality did not have and maintain effective, efficient and transparent systems of

financial and risk management and internal controls as required by section 62(1)(c)(i) of the MFMA.

30. The municipality did not set key performance indicators, including input indicators, output indicators and outcome indicators, in respect of each of the development priorities and objectives set out in the IDP, as required by section 41(1)(a) of the MSA and regulation 1 and 9(1)(a) of the MPPRM.

Annual financial statements, performance and annual reports

31. 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 of non-current assets, current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently.
32. The annual performance report for the year under review did not include a comparison of the performance with set targets and performances in the previous financial year, as required by section 46 (1)(b) of the MSA.

Procurement and contract management

33. Awards were made to service providers who are in the service of other state institutions or whose directors are in the service of other state institutions, which is in contravention with section 112(j) of the MFMA and SCM regulations 44. Similar awards were identified in the prior year and no effective steps were taken to prevent or combat the abuse of the SCM process in accordance with SCM regulation 38(1).

Human resource management and compensation

34. The community services manager was appointed without having met the prescribed minimum competency levels and the continued employment in the position was not made subject to meeting such requirements by 1 January 2013, as required by section 56(1)(b) of the MSA and regulation 18(2) of the minimum competency levels.
35. Job descriptions were not established for all posts in which appointments were made in the current year, in contravention of section 66(1)(b) of MSA.
36. Sufficient appropriate audit evidence could not be obtained that a newly appointed manager directly accountable to the municipal manager submitted proof of previous employment prior to appointment as per the requirements of regulation 4 of general notice regulation 805.
37. Sufficient appropriate audit evidence could not be obtained that the appointment of a senior manager directly accountable to the municipal manager was approved by municipal council, as required by 56(1)(a) of the MSA.
38. Sufficient appropriate audit evidence could not be obtained on whether the municipality performed checks on the appointment of the municipal manager and senior managers to determine whether they had not been dismissed for financial misconduct in the past 10 years.
39. The annual report of the municipality did not reflect information on compliance with prescribed minimum competencies as required by the regulation 14 (2)(b) of the minimum competency levels.
40. The senior managers directly accountable to the municipal manager did not sign performance agreements timeously, as required by section 57(2)(a) of the MSA.

Expenditure management

41. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred and accounted for creditors, as required by section 65(2)(b) of the MFMA.
42. The accounting officer did not take effective steps to prevent unauthorised, irregular as well as fruitless and wasteful expenditure, as required by sections 62(1)(d) and 95(d) of the MFMA.

Conditional grants

43. The municipality did not submit project registration forms timeously, for projects it intended implementing in the financial year under review, to the Department of Local Government, as required by the Division of Revenue Grant Framework, (DoRA), Gazette No.34280.
44. The municipality did not submit project implementation plans to the national Department of Cooperative Governance and Traditional Affairs, as required by the DoRA Framework, Gazette No.34280.

Revenue management

45. A credit control and debt collection policy was not implemented, as required by section 96(b) of the MSA and section 62(1)(f)(iii) of MFMA.

Asset management

46. The municipality did not establish an investment policy that was adopted by the council, as required by section 13(2) of the MFMA and Municipal Investment Regulation 3(1)(a)/3(2).
47. Investments were made without proper care being exercised as required by Municipal Investment Regulation 5.

Internal control

48. I considered internal control relevant to my audit of the financial statements, annual performance report 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 findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

49. The accounting authority did not adequately review the financial statements and the annual performance report prior to their submission for auditing, which resulted in the identification of material misstatements that were subsequently corrected. Furthermore the internal control environment within the human resource section remained weak resulting in numerous repeated control deficiencies being identified. The action plans which were developed to address all internal control deficiencies within the municipality were ineffective as similar findings were identified in the current year.
50. The municipality did not have adequate documented policies and procedures to guide

the operations of the municipality, including the information technology systems, resulting in numerous instances of non-compliance with the MFMA. In addition to this, the municipality did not have documented and approved internal policies and procedures to address the process of collection, recording, processing, monitoring and reporting of performance information.

Financial and performance management

51. Management did not implement daily and monthly controls as designed for the entity's business processes, resulting in the identification of significant misstatements during the audit, which were subsequently corrected. The municipality did not have an adequate filing system that provides for the maintenance of information that supports the reported performance contained in the annual performance report. Compliance with the applicable laws and regulations was not monitored on a regular basis, which resulted in an increase in the number of non-compliance findings since the previous year. The municipality's information technology systems environment remained weak as numerous deficiencies identified in the prior year had still not been addressed.

Governance

52. The municipality had established a risk committee, however action plans to address some of these risks have not been implemented.
53. Although the internal audit unit and audit committee met regularly throughout the year, they were not fully effective in strengthening the control environment within the municipality as numerous material misstatements that were subsequently corrected by management as well as material findings on performance reporting and compliance matters were identified during the audit process.

OTHER REPORTS

Investigation

54. The Department of Local Government conducted an investigation on the municipality relating to complaints received. Although the investigation was completed the outcome of the investigation had not yet been reported.
55. An investigation was undertaken into the alleged fraudulent activities by an employee. The investigation was finalised and the individual was dismissed.



East London

29 November 2013



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence