

REPORT OF THE AUDITOR-GENERAL TO THE FREE STATE LEGISLATURE AND THE COUNCIL ON THE METSIMAHOLO LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Metsimaholo Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2013, the statement of financial performance, statement of changes in net assets and 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 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 the financial statements in accordance with 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, 2012 (Act No. 5 of 2012) (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 the 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. I was unable to obtain sufficient appropriate audit evidence that management has identified and recorded all instances of irregular expenditure for the current and prior year as the controls over the system was ineffective and management did not review the entire population to ensure that all instances of irregular expenditure were identified and recorded. I was unable to confirm the irregular expenditure by alternative means. Consequently, I was unable to determine whether any adjustments to irregular

expenditure stated at R239 611 446 (2012:R162 913 899) as disclosed in note 52 to the financial statements were necessary.

Qualified opinion

7. In my opinion, except for the possible effects of the matter described in the basis for qualified opinion paragraph, the financial statements present fairly, in all material respects, the financial position of the Metsimaholo Local 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.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

8. 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

9. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages xx to xx of the annual report.
10. 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 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).

The reliability of the information in respect of the selected development objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).

11. The material findings are as follows:

Usefulness of information

12. 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 26% of the planned targets not achieved were not reflected in the annual performance report. This was due to the lack of review of the performance measures by management.
 - Adequate and reliable corroborating evidence could not be provided for 71% measures taken to improve performance as disclosed in the annual performance report. The municipality records did not permit the application of alternative audit procedures. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the reliability of the measures taken to improve performance.

Reliability of information

13. 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.
14. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of information presented with respect to KPA 2 - basic service delivery and infrastructure investment. This was due to the fact that the municipality could not provide sufficient appropriate evidence in support of the information presented with respect to the KPA 2 basic service delivery and infrastructure investment.

Compliance with laws and regulations

15. I performed procedures to obtain evidence that the entity had 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

16. 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.

Annual financial statements, performance and annual reports

17. 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 disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.
18. The annual performance report for the year under review does not include the performance of the municipality and each external service provider, as required by section 46 (1)(a) of the MSA and section 121(3)(c) of the MFMA.
19. The council's oversight report on the 2011-12 annual report was not made public within seven days of its adoption, as required by section 129(3) of the MFMA.

Expenditure management

20. Money owing by the municipality was not always paid within 30 days or an agreed period, as required by section 65(2)(e) of the MFMA.
21. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Procurement and contract management

22. Sufficient appropriate audit evidence could not, in all instances, be obtained that bid specifications for procurement of goods and services through competitive bids were drafted in an unbiased manner that allowed all potential suppliers to offer their goods or services, as per required by supply chain management (SCM) regulation 27(2)(a).
23. Sufficient appropriate audit evidence could not, in all instances, be obtained that bid specifications were drafted by bid specification committees which consisted of one or more officials of the municipality, as required by SCM regulation 27(3).

24. Sufficient appropriate audit evidence could not, in all instances, be obtained that contracts and quotations were awarded to bidders based on points given for criteria that were stipulated in the original invitation for bidding and quotations, as required by SCM regulations 21(b) and 28(1)(a) and Preferential Procurement Regulations.
25. Sufficient appropriate audit evidence could not, in all instances, be obtained that bid adjudication was always done by committees which were formed in accordance with SCM regulation 29(2).

Human resource management and compensation

26. Sufficient appropriate audit evidence could not be obtained that newly appointed municipal managers/managers directly accountable to municipal managers submitted proof of previous employment and disclosure of financial interests prior to appointment, as per the requirements of Municipal Performance Regulations, regulation 4 of GNR 805.
27. Sufficient appropriate audit evidence could not be obtained that the senior managers were not dismissed for financial misconduct in a previous position and re-appointed before the expiry of 10 years, in contravention of section 57A of the MFMA.
28. The competencies of financial and SCM officials were not assessed in a timely manner in order to identify and address gaps in competency levels, as required by the regulation 13 of the Municipal Regulations on Minimum Competency Levels.
29. The municipality did not submit a report on compliance with prescribed competency levels to the National Treasury and relevant provincial treasury, as required by regulation 14(2)(a) of the Municipal Regulations on Minimum Competency Levels.
30. The annual report of the municipality did not reflect information on compliance with prescribed minimum competencies, as required by regulation 14(2)(b)/14(3) of the Municipal Regulations on Minimum Competency Levels.

Liability management

31. Short-term debt was incurred without a resolution of the municipal council approving the debt agreement, in contravention of section 45(2) of the MFMA.

Internal control

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

Leadership

33. The occurrence of material irregular expenditure during the year under review indicates that integrity and ethical values were not adequate to prevent irregular expenditure and to set the standard for sound corporate governance as it was not prevented by management.
34. The accounting officer did not take appropriate action to address the lack of discipline at the SCM section, resulting in non-compliance with applicable legislation. This, in turn, resulted in irregular expenditure. This occurred due to limited capacity at the SCM unit.
35. The slow response of the accounting officer to take appropriate action to identify all irregular expenditure in the previous financial year resulted in a qualification on the completeness of irregular expenditure.

36. Internal policies and procedures for performance information management and reporting were not developed approved and implemented due to a slow response by management on the recommendations in the previous audit report.

Financial and performance management

37. The staff members of the municipality were not sufficiently skilled to ensure that the daily financial activities were fully and correctly recorded in the records of the municipality. Management also did not ensure that adequate controls were in place to detect and correct all errors in the financial records.
38. The financial statements were subjected to material corrections resulting from the audit process, which are attributable to weaknesses in the design and implementation of internal control in respect of financial management and financial reporting and weaknesses in the information systems of the municipality.
39. The action plan that was in place to address shortcomings in the performance management and reporting process were not effective due to a lack of monitoring by management.
40. The municipality did not have a proper system of record management that provides for the maintenance of information that supports the reported performance due to a lack of capacity in the performance information unit.

Bloemfontein

30 November 2013



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence