



## REPORT OF THE AUDITOR-GENERAL TO THE NORTH WEST PROVINCIAL LEGISLATURE AND THE COUNCIL OF THE DR RUTH SEGOMOTSI MOMPATI DISTRICT MUNICIPALITY

### REPORT ON THE FINANCIAL STATEMENTS

#### Introduction

1. I was engaged to audit the financial statements of the Dr Ruth Segomotsi Mompoti District Municipality set out on pages XX to XX, which comprise the statement of financial position as at 30 June 2014, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget information with actual information for the year then ended, as well as 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 South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP), 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, 2013 (Act No. 2 of 2013) (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 conducting the 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. Because of the matters described in the basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

#### Basis for disclaimer of opinion

##### Property, plant and equipment

4. I was unable to obtain sufficient appropriate audit evidence for work in progress included in property plant and equipment for the prior year as the municipality did not adequately monitor the work in progress completed that should be transferred to infrastructure. I was unable to confirm whether all infrastructure assets were recorded and depreciated accurately by alternative means. Consequently, I was unable to determine whether any adjustments to work in progress of R333 001 908, infrastructure of R1 495 782 387, accumulated depreciation for infrastructure of R179 961 459 or infrastructure depreciation of R32 299 794 disclosed in note 44 to the financial statements were necessary.
5. Contrary to SA Standards of GRAP, GRAP 17, *Property, plant and equipment* the municipality did not classify completed work in progress as infrastructure and grants given as operational expenditure in the current year. Consequently work in progress has been overstated by R104 873 329, accumulated surplus has been overstated by R595 967 and infrastructure by R104 277 353. The effect on depreciation and accumulated depreciation for the current period could not be practicably determined.

6. The municipality did not assess impairment on assets of R16 731 226 classified on the infrastructure asset register as “not in use” and “not equipped”. Furthermore the municipality did not assess the residual values and useful lives of items with a nil carrying amount. This is not in accordance with the SA Standards of GRAP, GRAP 17, *Property, plant and equipment*. Consequently the impairment and depreciation for the current year on these assets could not be practicably determined.

### **Unspent grant liability**

7. I was unable to obtain sufficient appropriate audit evidence for debit transactions included in the unspent grant liability due to the status of the accounting records. Consequently I was unable to determine whether any adjustments relating to the unspent conditional grant liability of R69 940 095 (2013: R106 857 663) in the financial statements was necessary.
8. The municipality incorrectly accounted for revenue and reduced the carrying amount of the unspent conditional grant liability as conditions have not been met. This is not in accordance with the SA Standards of GRAP, GRAP 23, *Revenue from non-exchange transactions*. Consequently, revenue from non-exchange transactions are overstated by R10 905 031 and unspent conditional grants understated by the same.

### **Trade and other receivables**

9. I was unable to obtain sufficient appropriate audit evidence for trade and other receivables due to the status of the accounting records. I was unable to confirm trade and other receivables by alternative means. Consequently, I was unable to determine whether any adjustments to trade and other receivables of R9 447 780 (2013: R28 560 527) in the financial statements was necessary.

### **Value Added Tax (VAT)**

10. The municipality did not appropriately account for VAT transactions in accordance with the Value Added Tax, 1991 (Act No. 89 of 1991). Included in the accounting records are VAT transactions that have been disallowed by SARS for the current and prior periods. Consequently, VAT receivable is overstated by R5 189 567. Additionally, there is a resultant impact on accumulated surplus.

### **Accumulated surplus**

11. I was unable to obtain sufficient and appropriate audit evidence for transfers to and from the accumulated surplus in the current and prior year due to the status of the municipality's accounting records. Consequently, I was unable to determine whether any adjustments relating to the accumulated surplus stated at R1 689 992 536 (2013: R1 651 196 092) in the financial statements was necessary.

### **Revenue**

12. I was unable to obtain sufficient appropriate audit evidence that management has properly accounted for revenue for the current period. This was mainly due to the status of the accounting records that did not allow us to obtain sufficient appropriate audit evidence to confirm government grants and subsidies. I was unable to confirm revenue by alternative means. Consequently I was unable to determine whether any adjustments relating to revenue stated at R431 538 620 in the financial statements was necessary.

### **Expenditure**

13. I was unable to obtain sufficient appropriate audit evidence for expenditure due to the status of the accounting records. I was unable to confirm expenditure by alternative means. Consequently, I was unable to determine whether any adjustments to expenditure stated at R290 478 935 (amount excludes employee related costs and remuneration of councillors) in the financial statements was necessary.



### **Irregular expenditure**

14. Section 125 of the MFMA requires the disclosure of irregular expenditure incurred. I was unable to obtain sufficient appropriate audit evidence to confirm that awards of R220 225 844 (2013: undetermined) were made in terms of the supply chain management requirements. The municipality's records did not permit the application of alternative procedures. Consequently, I was unable to determine whether any adjustment relating to irregular expenditure of R65 703 935 (2013: R18 347 353) disclosed in note 33.3 to the financial statements was necessary.
15. Furthermore the municipality made payments of R14 876 253 in contravention of the supply chain management requirements which were not included in irregular expenditure disclosed. As the municipality did not quantify the full extent of the irregular expenditure, it was impracticable to determine the resultant understatement of irregular expenditure as per note 33.3 to the financial statements.

### **Unauthorised expenditure**

16. Section 125 of the MFMA requires the disclosure of unauthorised expenditure incurred. The municipality incorrectly calculated the unauthorised expenditure for the current year. Consequently, unauthorised expenditure as disclosed in note 33.1 is understated by R5 985 244.

### **Capital commitments**

17. I was unable to obtain sufficient appropriate audit evidence for capital commitments approved but not yet contracted for disclosed in note 35.1 of the financial statements due to the status of the accounting records. I was unable to confirm the capital commitments approved but not yet contracted for by alternative means. Consequently, I was unable to determine whether any adjustments relating to capital commitments approved but not yet contracted for disclosed in note 35.1 at R464 837 657 (2013: R413 337 657) in the financial statements was necessary.
18. The municipality did not account for all capital commitments as required by SA Standards of GRAP, GRAP 17, *Property, plant and equipment*. The municipality is party to a number of contracts that was not included in the capital commitments consequently, capital commitments as disclosed in note 35 are understated by R76 616 358.

### **Cash flow statement**

19. I was unable to confirm that the current and comparative cash flow statement to the financial statements is correct due to the limitations and disagreement misstatements as included in the basis for disclaimer of opinion paragraphs. Sufficient appropriate audit evidence was also not available for items included in the cash flow statement. I was unable to confirm the cash flow statement by alternative means. Consequently, I was unable to determine whether any adjustments relating to the cash flow statement in the financial statements was necessary.

### **Budget disclosure**

20. The municipality did not disclose the budget information in accordance with SA Standards of GRAP, GRAP 24, *Presentation of budget information in the financial statements*. The budget period and explanation of the budgetary and classification basis adopted in the approved budget has been disclosed in the notes to the financial statements and no accounting policy for the budget has been disclosed. No adjustments have been made to amounts to have the actual amounts and budgeted amounts compared on a comparable basis.

### **Operating leases**

21. I was unable to obtain sufficient appropriate audit evidence to confirm prior year amounts disclosed in note 35.2 for operating leases. I was unable to confirm the prior year amounts disclosed by alternative means. Consequently, I was unable to determine whether any



adjustments to the prior year operating leases of R3 322 472 and prior year operating leases of R437 293 in the financial statements were necessary.

### **Accumulation of immaterial uncorrected misstatements**

22. The financial statements were materially misstated due to the cumulative effect of numerous individual immaterial uncorrected misstatements. I was unable to obtain sufficient appropriate audit evidence and to confirm the following items by alternative means:

- Land and buildings and movable assets of R70 480 as included in the non-current assets of R1 775 998 451.
- Trade and other payables and deposits of R291 218 as included in the current liabilities of R158 315 125.

In addition, the following items making up the statement of financial position were misstated:

- Movable and intangible assets reflected in non-current assets as R1 775 998 451 is understated by R1 557 645.
- Non-current assets held for sale of R361 148 is incorrectly included current assets reflected as R105 514 114 resulting in an overstatement.
- Current liabilities reflected as R158 315 125 is understated by R1 535 193.

### **Prior period error**

23. Management failed to provide a description of the nature of the prior period error for each separate transaction disclosed in note 32 of the financial statements as required by SA Standards of GRAP, GRAP 03, *Accounting policies, changes in accounting estimates and errors*. Sufficient appropriate audit evidence could not be obtained to verify the restated balances disclosed.

### **Disclaimer of opinion**

24. Because of the significance of the matters described in the basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

### **Emphasis of matter**

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

### **Restatement of corresponding figures**

26. As disclosed in note 32 to the financial statements, the corresponding figures for 30 June 2013 have been restated as a result of errors discovered during 2014 in the financial statements of Dr Ruth Segomotsi Mompati District Municipality at, and for the year ended, 30 June 2013.

### **Additional matters**

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

### **Unaudited disclosure notes**

28. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.



## Unaudited supplementary schedules

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

## REPORT ON OTHER LEGAL AND REGULARITY REQUIREMENTS

30. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings on the reported performance information against predetermined objectives for the selected objectives presented in the annual performance report, non-compliance with legislation as well as internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

### Predetermined objectives

31. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected objectives presented in the annual performance report of the municipality for the year ended 30 June 2014:
- Objective 1: Basic service delivery and infrastructure on pages XX to XX
  - Objective 2: Basic service - community services on pages XX to XX
  - Objective 3: Good governance and public participation on pages XX to XX
32. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
33. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned objectives. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's Framework for managing programme performance information (FMPPI).
34. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
35. The material findings in respect of the selected objectives are as follows:

### Objective 1: Basic service delivery and infrastructure

#### Usefulness of reported performance information

36. I did not raise any material findings on the usefulness of the reported performance information for basic service delivery and infrastructure.

#### Reliability of reported performance information

37. The FMPPI requires auditees to 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. Adequate and reliable corroborating evidence could not be provided for 100% of significantly important targets to assess the reliability of the reported performance information. This was due to limitations placed on the scope of my work by the auditee due to the state of the information and accounting records.



## **Objective 2: Basic service – community services**

38. I did not raise any material findings on the usefulness and reliability of the reported performance information for basic service – community services.

## **Objective 3: Good governance and public participation**

### **Usefulness of reported performance information**

39. I did not raise any material findings on the usefulness and of the reported performance information for good governance and public participation.

### **Reliability of reported performance information**

40. The FMPPI requires auditees to 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. Adequate and reliable corroborating evidence could not be provided for 33% of significantly important targets to assess the reliability of the reported performance information. This was due to limitations placed on the scope of my work by the auditee.

### **Additional matters**

41. I draw attention to the following matters:

#### **Achievement of planned targets**

42. Refer to the annual performance report on pages XX to XX for information on the achievement of the planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information for the selected objectives reported in paragraphs 36 to 40 of this report.

#### **Unaudited supplementary information**

43. The supplementary information set out on pages XX to XX does not form part of the annual performance report and is presented as additional information. I have not audited these schedules and, accordingly, I do not report thereon.

#### **Compliance with legislation**

44. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

#### **Budgets**

45. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA.

#### **Financial statements, performance and annual reports**

46. 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, but the uncorrected material misstatements and or supporting records that could not be provided resulted in the financial statements receiving a disclaimer of audit opinion.



## **Audit committees**

47. The audit committee did not advise the council on matters relating to the adequacy, reliability and accuracy of financial reporting and information, as required by section 166(2)(a)(iv) of the MFMA.
48. The audit committee did not review the annual financial statements to provide the council with an authoritative and credible view of the financial position of the entity, its efficiency and effectiveness and its overall level of compliance with legislation, as required by section 166(2)(b) of the MFMA.
49. The audit committee did not respond to the council on the issues raised in the audit reports of the auditor-general, as required by section 166(2)(c) of the MFMA.

## **Procurement and contract management**

50. Sufficient appropriate audit evidence could not be obtained that all contracts and quotations were awarded in accordance with the legislative requirements and a procurement process which is fair, equitable, transparent and competitive, as there is insufficient record management processes relating to the procurement documentation.
51. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by Supply Chain Management (SCM) regulations 17(a) and (c).
52. Sufficient appropriate audit evidence could not be obtained that goods and services of a transaction value above R500 000 were procured by means of inviting competitive bids and that deviations approved by the accounting officer were only if it was impractical to invite competitive bids, as required by SCM regulations 19(a) and 36(1).
53. Sufficient appropriate audit evidence could not 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 SCM regulation 27(2)(a).
54. 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 SCM regulation 27(3).
55. Sufficient appropriate audit evidence could not be obtained that invitations for competitive bidding were advertised for a required minimum period of days, as required by SCM regulations 22(1) and 22(2).
56. Sufficient appropriate audit evidence could not be obtained that bids were evaluated by bid evaluation committees which were 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).
57. Sufficient appropriate audit evidence could not 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.
58. Sufficient appropriate audit evidence could not be obtained that bid adjudication was always done by committees which were composed in accordance with SCM regulation 29(2).
59. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded to suppliers based on preference points that were allocated and calculated in accordance with the requirements of the Preferential Procurement Policy Framework Act and its regulations.



60. 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).
61. 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.
62. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
63. The contract performance and monitoring measures and methods were insufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA.
64. Persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM regulation 46(2)(e).
65. 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.

### **Human resource management and compensation**

66. A bonus was awarded to the municipal manager without sufficient and appropriate audit evidence that an evaluation of performance was performed in contravention of section 57(4)(b) Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

### **Expenditure management**

67. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
68. Payments were made from the municipality's bank account without the approval of the accounting officer, as required by section 11(1) of the MFMA.
69. An effective system of expenditure control, including procedures for the payment of funds, was not in place, as required by section 65(2)(a) of the MFMA.
70. Reasonable steps were not taken to prevent unauthorised expenditure, and irregular expenditure, as required by section 62(1)(d) of the MFMA.

### **Conditional grants received**

71. The Municipal Systems Improvement Grant allocation was not spent in accordance with the applicable grant framework, in contravention of section 16(1) of the DoRA.
72. The municipality did not evaluate its performance in respect of programmes or functions funded by the Municipal Systems Improvement Grant allocation and the Local Government Financial Management Grant allocations, as required by section 12(5) of the DoRA.

### **Revenue management**

73. An adequate management, accounting and information system which accounts for revenue and debtors was not in place, as required by section 64(2)(e) of the MFMA.

### **Asset and liability management**

74. An effective system of internal control for liabilities (including a liability register) was not in place, as required by section 63(2)(c) of the MFMA.
75. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.
76. An effective system of internal control for assets (including an asset register for investment property and intangible assets) was not in place, as required by section 63(2)(c) of the MFMA.





77. The municipality did not establish an adequate investment policy that was adopted by council, as required by section 13(2) of the MFMA and Municipal investment regulation 3(1)(a).

### **Strategic planning and performance management**

78. The performance management system and related controls were inadequate as it did not describe and represent the processes of performance review and reporting and how it is conducted, organised and managed, as required by sections 38 of the MSA and regulation 7 of the municipal planning and performance management regulations.

### **Consequences management**

79. Unauthorised and irregular expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.

### **Waste management**

80. The municipality did not exercise its legislative and executive authority as required by section 11(3)(l) and (m) of the MSA by managing, monitoring and enforcing environmental related bylaws to promote a safe and healthy environment.

### **Internal control**

81. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for disclaimer of opinion, the findings on the annual performance report and the findings on non-compliance with legislation included in this report.

### **Leadership**

82. Adequate oversight responsibility regarding financial and performance reporting and compliance and related internal controls is not exercised. Policies and procedures are not adequately implemented and communicated to enable and support understanding and execution of internal control objectives, processes, and responsibilities.

83. Effective human resource management, to ensure that adequate and sufficiently skilled resources are in place and that performance is monitored is not implemented.

### **Financial and performance management**

84. The municipality did not compile and maintain an approved record classification system for paper-based and electronic records to safeguard these records and facilitate their timely retrieval.

85. Controls over daily and monthly processing and reconciling of transactions were not performed on a regular basis, contributing to material misstatements not being prevented or detected in the financial statements. Material corrections had to be made to the financial statements.

## Governance

86. Management did not implement appropriate risk management activities to ensure that regular risk assessments, including consideration of IT risks and fraud prevention, were approved and that a risk strategy to address these risks were developed and monitored.
87. The audit committee service was not effective during the financial year. The recommendations made were not implemented by council.

*Auditor General*

Potchefstroom

30 November 2014



**AUDITOR - GENERAL  
SOUTH AFRICA**

*Auditing to build public confidence*