

# Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on the Blue Crane Route Municipality

## Report on the financial statements

### Introduction

1. I have audited the financial statements of the Blue Crane Route Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2015, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts 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) 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, 2014 (Act No. 10 of 2014) (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 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 municipality'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 municipality'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 the Blue Crane Route Municipality as at 30 June 2015 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**

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 42 to the financial statements, the corresponding figures for 30 June 2014 have been restated as a result of errors discovered during the current financial period.

### Material losses

9. As disclosed in note 27 to the financial statements, electricity losses of 24% (2013-14: 27%) and water losses of 44% (2013-14: 42%) were incurred during the financial year.

### Irregular expenditure

10. As disclosed in note 48 to the financial statements, irregular expenditure of R39,6 million (2013-14: R31,1 million) was incurred as a result of the contravention of supply chain management (SCM) requirements.

## **Additional matter**

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

### Unaudited supplementary information

12. The supplementary information (appendix A) 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 this schedule and, accordingly, I do not express an opinion thereon.

### Unaudited disclosure note

13. 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.

## Report on other legal and regulatory requirements

14. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report, compliance with legislation and 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

15. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development priority presented in the annual performance report of the municipality for the year ended 30 June 2015:
  - Development priority 2: Services delivery and infrastructure development on pages x to x
16. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
17. 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 development priority. 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).
18. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
19. The material findings in respect of the selected development priority are as follows:

### **Service delivery and infrastructure development**

#### Usefulness of reported performance information

20. I did not identify material findings on the usefulness of the reported performance information.

#### Reliability of reported performance information

21. 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. Significantly important targets were not reliable when compared to the source information or evidence provided. This was due to a lack of standard operating procedures or documented system descriptions for the accurate recording of actual achievements as well as

technical indicator descriptions for the accurate measurement, recording and monitoring of performance.

## **Additional matters**

22. I draw attention to the following matters:

### **Achievement of planned targets**

23. Refer to the annual performance report on page(s) x to x and x to x for information on the achievement of planned targets for the year. This information should be considered in the context of the material findings on the reliability of the reported performance information for the selected development priority reported in paragraph 21 of this report.

### **Adjustment of material misstatements**

24. I identified material misstatements in the annual performance report submitted for auditing on the reported performance information for the development priority relating to basic service delivery and infrastructure development. As management subsequently corrected only some of the misstatements, I identified material findings on the reliability of the reported performance information.

## **Compliance with legislation**

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

## **Annual financial statements and annual report**

26. 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 property, plant and equipment, investment properties, trade and other receivables, commitments, distribution losses, subsequent events and contingent liabilities identified by the auditors in the submitted financial statements were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.

## **Strategic planning and performance management**

27. The local community was not afforded the opportunity to comment on the final draft of the integrated development plan before adoption, as required by section 42 of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) and municipal planning and performance management regulations 9, 13(1), 13(4)(c) and 15(3).

28. The annual performance report for the year under review did not include measures taken to improve performance, as required by section 46(1)(c) of the MSA.

29. The performance management system and related controls were inadequate, as it did not describe and represent the processes of performance planning, monitoring,

measurement, review, reporting and improvement as well as how it is to be conducted, organised and managed, as required by section 38 of the MSA and municipal planning and performance management regulation 7.

## **Expenditure management**

30. Reasonable steps were not taken to prevent unauthorised, irregular as well as fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

## **Human resource management**

31. Sufficient appropriate audit evidence could not be obtained that job descriptions had been established for all posts in which appointments were made in the current year, as required by section 66(1)(b) of the MSA.
32. The competencies of the chief financial officer, head of the SCM unit as well as financial and SCM officials were not assessed in a timely manner to identify and address gaps in competency levels, as required by municipal regulation on minimum competency levels 13.
33. The annual report of the municipality did not reflect information on compliance with the prescribed minimum competencies, as required by municipal regulation on minimum competency levels 14(2)(b).
34. The municipality did not develop and adopt appropriate systems (policies) and procedures to monitor, measure and evaluate the performance of staff, in contravention of section 67(d) of the MSA.

## **Audit committee**

35. The audit committee did not advise the council and the accounting officer on matters relating to performance management and performance evaluation, as required by section 166(2)(a) of the MFMA.
36. The audit committee did not review the municipality's performance management system and make recommendations to the council, as required by municipal planning and performance management regulation 14(4)(a)(ii).

## **Internal audit**

37. The internal audit unit did not function as required by section 165(2) of the MFMA, due to the following:
  - There was no evidence of approval of the risk-based audit plan and an internal audit programme for the financial year under review.
  - The unit did not advise the accounting officer and report to the audit committee on matters relating to accounting procedures and practices as well as loss control.

## **Consequence management**

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

## **Procurement and contract management**

39. Construction projects were not always registered with the Construction Industry Development Board (CIDB), as required by section 22 of the CIDB Act of South Africa, 2000 (Act No. 38 of 2000) and CIDB regulation 18.
40. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
41. The contract performance and monitoring measures and methods were insufficient to ensure effective contract management, contrary to section 116(2)(c) of the MFMA.
42. Awards were made to providers whose directors are in the service of other state institutions, in contravention of section 112(j) of the MFMA and 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, contrary to SCM regulation 38(1).
43. Persons in the 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, contrary to SCM regulation 46(2)(e).

## **Internal control**

44. 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 findings on the annual performance report and the findings on compliance with legislation included in this report.

## **Leadership**

45. Leadership did not fulfil its oversight responsibility to ensure that the SCM manager position was filled timeously. This contributed to the material compliance findings in procurement and contract management.
46. Leadership did not enforce consequences for poor performance and transgressions of legislation, resulting in a culture where repeat findings have become a norm.

## **Financial and performance management**

47. The municipality did not introduce appropriate mechanisms, processes, procedures, systems or internal controls to ensure that transactions were correctly recorded, classified, reconciled and reported on in accordance with SA Standards of GRAP. As a result, material misstatements were identified during the audit process, which were subsequently corrected by management.

48. Overall, there was a slow response to audit recommendations, as evidenced by repeat findings on the financial statements, annual performance report and compliance with legislation.

## **Governance**

49. The internal audit unit did not submit its reports and recommendations to management and the audit committee in a timely manner to enable management to implement the unit's recommendations adequately. As a result, the audit committee was also unable to provide the required level of assurance.

*Auditor General*

East London

27 November 2015



**A U D I T O R - G E N E R A L**  
**S O U T H A F R I C A**

*Auditing to build public confidence*