

Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on the Dr Beyers Naude Local Municipality

Report on the audit of the financial statements

Disclaimer of opinion

1. I was engaged to audit the financial statements of the Dr Beyers Naude Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2017, 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 to the financial statements, including a summary of significant accounting policies.
2. I do not express an opinion on the financial statements of the municipality. Because of the significance of the matter described in the basis for disclaimer of opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

Basis for disclaimer of opinion

Limitations on the financial statements

3. I was unable to obtain sufficient appropriate audit evidence regarding the financial statements as a whole, as the financial statements were presented for audit purposes without accurate and complete underlying accounting records. I was unable to audit the financial statements by alternative means. Consequently, I was unable to determine whether any adjustments relating to the financial statements as a whole were necessary.

Other matters

4. I draw attention to the matters below:

Withdrawal from the audit engagement

5. Due to the limitation imposed on the scope of the audit by management, I have disclaimed my opinion on the financial statements. Were it not for the legislated requirement to perform the audit of the municipality, I would have withdrawn from the engagement in terms of the International Standards on Auditing (ISAs).

Unaudited disclosure notes

6. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with this legislation. 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 information

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

Responsibilities of the accounting officer for the financial statements

8. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the 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, 2016 (Act No. 3 of 2016) (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.
9. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the accounting officer either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

10. My responsibility is to conduct an audit of the financial statements in accordance with the ISAs and to issue an auditor's report. However, because of the matters described in the basis for disclaimer of opinion section of my report, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.
11. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) together with the ethical requirements that are relevant to my audit of the financial statements in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.

Report on the audit of the annual performance report

Introduction and scope

12. 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 material findings on the reported performance information against predetermined objectives for selected objectives presented in the annual performance report. I performed procedures to raise findings but not to gather evidence to express assurance.
13. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the

planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.

14. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected objectives presented in the annual performance report of the municipality for the year ended 30 June 2017:

| Objectives | Pages in the annual performance report |
|---|---|
| KPA 2 – Basic service delivery and infrastructure development | x – x |
| KPA 3 – Local economic development | x – x |

15. I performed procedures to determine whether the reported performance information was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.

16. I did not raise material findings on the usefulness and reliability of KPA 3 – Local economic development. The material findings in respect of the usefulness and reliability of KPA 2 – Basic service delivery and infrastructure development are as follows:

KPA 2 – Basic service delivery and infrastructure development

Usefulness

Performance indicators not well defined

Upgrading of waste water treatment works in Klipplaat by 31 March 2017

17. The source information, evidence and method of calculation for the achievement of the planned indicator were not clearly defined, as required by the Framework for Managing Programme Performance Information.

Reliability

Reported achievement not supported by sufficient appropriate audit evidence

Various indicators

18. I was unable to obtain sufficient appropriate audit evidence for the 2 indicators below relating to this programme. This was due to limitations placed on the scope of my work. I was unable to confirm the reported achievements by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements of the following indicators:

| Nr | Description | Reported Achievement |
|----|---|--|
| 1. | Construction of 4km pipeline between Wanhoop WTW and Willowmore by 30 June 2017 | Camp Establishment – 100%, Locate existing pipeline 90%, Setting out new pipeline – 90%, Excavate trench – 40%; |
| 2. | To extend the Indigent Register by registering 120 houses by 30 June | 187 Households registered |

Other matters

19. I draw attention to the matters below.

Achievement of planned targets

20. Refer to the annual performance report on pages x to x and x to x for information on the achievement of planned targets for the year and explanations provided for the under-achievement of a number of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 25 and 26 of this report.

Adjustment of material misstatements

21. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of KPA2 – Basic service delivery and infrastructure. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

Report on the audit of compliance with legislation

Introduction and scope

22. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to raise findings but not to gather evidence to express assurance.

23. The material findings on compliance with specific matters in key legislation are as follows:

Annual financial statements and annual report

24. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Supporting records that could not be provided resulted in the financial statements receiving a disclaimer of audit opinion.

Strategic planning and performance management

25. The service delivery and budget implementation plan for the year under review did not include monthly revenue projections by source of collection, the monthly operational and capital expenditure by vote, and the service delivery targets and performance indicators for each quarter, as required by section 1 of the MFMA.
26. A mid-year performance assessment was not performed, as required by section 72(1)(a)(ii) of the MFMA.
27. A performance management system was not established, as required by section 38(a) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) and municipal planning and performance management regulation 8.

Budget

28. Reasonable steps were not taken to prevent unauthorised expenditure of R33,7 million as disclosed in note 39 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The full extent of the unauthorised expenditure could not be quantified, as indicated in the basis for disclaimer of opinion paragraph.

Expenditure management

29. Money owed by the municipality was not always paid within 30 days, as required by section 65(2) of the MFMA.
30. An effective system of expenditure control was not in place, including procedures for approval and authorisation, as required by section 65(2) of the MFMA.
31. An adequate management, accounting and information system was not in place to recognise expenditure when it was incurred and to account for creditors and payments made, as required by section 65(2)(b) of the MFMA.
32. Effective steps were not taken to prevent irregular expenditure of R2,1 million as disclosed in note 41 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The full extent of the irregular expenditure could not be quantified, as indicated in the basis for disclaimer of opinion paragraph.
33. Effective steps were not taken to prevent fruitless and wasteful expenditure of R1,5 million as disclosed in note 40 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The full extent of the fruitless and wasteful expenditure could not be quantified, as indicated in the basis for disclaimer of opinion paragraph.

Revenue management

34. A tariff policy was not adopted for the levying of fees for the provision of municipal services, as required by section 74(1) of the MSA and section 62(1)(f)(i) of the MFMA.
35. A credit control and debt collection policy was not adopted, as required by section 96(b) of the MSA and section 62(1)(f)(iii) of the MFMA.

36. A policy on the levying of rates on rateable property within the municipality was not adopted, as required by section 3(1) of the Municipal Property Rates Act of South Africa, 2004 (Act No. 6 of 2004) and section 62(1)(f)(ii) of the MFMA.
37. An adequate management, accounting and information system was not in place to account for revenue, debtors and receipts of revenue, as required by section 64(2)(e) of the MFMA.
38. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.
39. Revenue due to the municipality was not calculated on a monthly basis, as required by section 64(2)(b) of the MFMA.
40. Accounts for municipal tax and charges for municipal services and service charges were not prepared on a monthly basis, as required by section 64(2)(c) of the MFMA.

Asset management

41. The municipality did not establish an investment policy that was adopted by council, as required by section 13(2) of the MFMA.
42. 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.
43. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Liability management

44. An adequate management, accounting and information system which accounts for liabilities was not in place, as required by section 63(2)(a) of the MFMA.
45. An effective system of internal control for liabilities was not in place, as required by section 63(2)(c) of the MFMA.

Conditional grants

46. The municipality did not evaluate its performance in respect of programmes funded by the municipal infrastructure grant, as required by section 12(5) of DoRA.

Consequence management

47. Unauthorised, irregular and 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) of the MFMA.

Human resource management

48. An approved staff establishment was not in place, as required by section 66(1)(a) of the MSA.
49. Appropriate systems and procedures were not developed and adopted to monitor, measure and evaluate staff performance, as required by section 67(1)(d) of the MSA.

50. Senior managers did not sign performance agreements within the prescribed period, as required by section 57(2)(a) of the MSA.

Procurement and contract management

51. Goods and services with a transaction value below R200 000 were procured without obtaining the required price quotations, in contravention of supply chain management (SCM) regulation 17(a) and (c).

52. Competitive bids were adjudicated by a bid adjudication committee that was not composed in accordance with SCM regulation 29(2).

Internal control deficiencies

53. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the disclaimer of opinion, the findings on the performance report and the findings on compliance with legislation included in this report.

54. There was a lack of leadership in the municipality, as no permanent municipal manager and chief financial officer were appointed for the financial year. This contributed to the breakdown in the control environment and administration of the municipality and the lack of implementation of approved policies and procedures.

55. Leadership did not exercise oversight over financial, performance and compliance reporting, as the annual financial statements, annual report and compliance reporting were not adequately reviewed, which contributed to the material findings reported.

56. The municipality did not maintain a proper record management system for electronic records, or for the timely retrieval thereof, as evidenced by the fact that the annual financial statements were not supported by relevant schedules and supporting documentation. Furthermore, the general ledger and trial balance did not agree to the annual financial statements, and numerous instances of material non-compliance with legislation were identified.

57. The audit committee did not review the annual financial statements and annual performance report in the current year, as it was submitted late for their review.

58. The internal audit unit lacked the capacity required to effectively perform their duties. Furthermore, management did not follow up the implementation of internal and external audit recommendations to address internal control deficiencies.

Auditor-General

East London

30 November 2017



**AUDITOR - GENERAL
SOUTH AFRICA**

Auditing to build public confidence