



**AUDITOR - GENERAL
SOUTH AFRICA**

Auditing to build public confidence

Sakhisizwe Municipality

Audit Report

For the year ended 30 June 2016

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

Report on the financial statements

Introduction

1. I have audited the financial statements of the Sakhisizwe Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2016, 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, 2015 (Act No. 1 of 2015) (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 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 the Sakhisizwe Local Municipality as at 30 June 2016 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.

Unauthorised expenditure

8. As disclosed in note 36.1 to the financial statements, the municipality incurred unauthorised expenditure of R19 million (2015: R11,9 million) as a result of incurred expenditure exceeding the total approved budget.

Irregular expenditure

9. As disclosed in note 36.3 to the financial statements, the municipality incurred irregular expenditure of R12,4 million (2015: R17,2 million) as a result of non-compliance with procurement requirements. Goods and services were received for the supply chain management-related irregular expenditure disclosed in note 36.3.

Material losses and impairments

10. As disclosed in note 23 to the financial statements, material impairments of R16,1 million (2015: R0,6 million) were incurred as a result of the write-off of irrecoverable trade receivables. Furthermore, note 36.4 to the financial statements discloses material losses of R1,8 million as a result of electricity reticulation losses.

Additional matters

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

Unaudited supplementary schedules

12. 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 report thereon.

Unaudited disclosure notes

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 objectives 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 objectives presented in the annual performance report of the municipality for the year ended 30 June 2016:
 - Key performance area 1: local economic development on pages x to x
 - Key performance area 2: basic service delivery on pages x to x
16. 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 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).
17. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
18. The material findings in respect of the selected development objectives are as follows:

Key performance area 1: local economic development

Reliability of reported performance information

19. 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. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of 43% of the reported performance. This was due to limitations placed on the scope of my work due to the absence of information systems, the fact that the municipality could not provide sufficient appropriate evidence in support of the reported performance information, and the municipality's records not permitting the application of alternative audit procedures.
20. Furthermore, 20% of the targets or significantly important targets were not valid, accurate and complete when compared to the source information or evidence provided. Overall, 63% of the targets or significantly important targets were not reliable.

Key performance area 2: basic service delivery

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. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to

the reliability of 27% of the reported performance. This was due to limitations placed on the scope of my work due to the absence of information systems, the fact that the municipality could not provide sufficient appropriate evidence in support of the reported performance information, and the municipality's records not permitting the application of alternative audit procedures.

22. Furthermore, 25% of the targets or significantly important targets were not valid, accurate and complete when compared to the source information or evidence provided. Overall, 52% of the targets or significantly important targets were not reliable.

Additional matter

23. I draw attention to the following matter:

Achievement of planned targets

24. Refer to the annual performance report on pages x to x 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 reliability of the reported performance information in paragraphs xx to xx of this report.

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:

Expenditure management

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

Procurement and contract management

27. Construction contracts were awarded to contractors that were not registered with the Construction Industry Development Board (CIDB) and/or did not qualify for the contract, in contravention of section 18(1) of the CIDB Act of South Africa, 2000 (Act No. 38 of 2000) and CIDB regulations 17 and 25(7A).
28. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
29. Bids were not always evaluated by bid evaluation committees composed of officials from the departments requiring the goods or services, as required by supply chain management (SCM) regulation 28(2).

Consequence management

30. Unauthorised, irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine whether any person was liable for the expenditure, in accordance with the requirements of section 32 of the MFMA.

Strategic planning and performance management

31. The local community was not afforded the opportunity to comment on the final draft of the integrated development plan (IDP) before adoption, as required by section 42 of the MSA and MPPMR 9, 13(1), 13(4)(c) and 15(3).
32. 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 Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000).
33. The amendments to the IDP were not published for public comment for 21 days, as required by MPPMR 7.

Internal control

34. 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

35. The slow response to the audit message remained a challenge. Although the roles and responsibilities for recording and filing financial and performance information were communicated to all relevant staff, there was a lack of effective oversight by senior leadership to ensure accountability.
36. The municipality did not develop documented and approved internal policies and procedures to address the collection, recording, processing, monitoring and reporting of predetermined objectives. Consequently, material misstatements were identified in the annual performance report.

Financial and performance management

37. Management did not implement daily and monthly controls as designed for the municipality's business processes and did not have a proper system of record management that provided for the maintenance of information to be reported in the annual performance report.
38. Compliance with applicable legislation was not monitored regularly and the municipality's information technology systems environment remained weak, as numerous deficiencies identified in the prior year had still not been addressed. This can mainly be attributed to a lack of credible in-year reporting by the leadership and oversight committees in respect of performance management and compliance matters, resulting in numerous recurring findings.

39. Management did not have adequate controls in place to ensure that disclosure notes are adequately recorded and disclosed in the financial statement. The audit process was utilised to correct misstatements in the financial statements which improved the audit outcome from a qualified opinion to an unqualified opinion.

Governance

40. There were no governance structures in place during the year to strengthen the control environment within the municipality. There was no audit committee during the financial year and internal audit were not sufficiently capitated with the required number of staff in order to effectively carry out their mandate. This resulted in recurring findings on internal controls, financial statements, performance reporting and compliance matters.
41. The municipality did not conduct a risk assessment as required by the MFMA. Consequently, the municipality did not monitor compliance with the MFMA, the MSA, SCM regulations or the GRAP reporting framework requirements.

AUDITOR-GENERAL

East London

30 November 2016



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