

# REPORT OF THE AUDITOR-GENERAL TO FREE STATE LEGISLATURE AND COUNCIL ON LEJWELEPUTSWA DISTRICT MUNICIPALITY

## REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

### Introduction

1. I have audited the consolidated financial statements of the Lejweleputswa District Municipality set out on pages 241 to 423, which comprise, the statement of financial position as at 30 June 2012, the statement of financial performance, statement of changes in net assets and statement of cash flows for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

### The accounting officer's responsibility for the consolidated financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these consolidated 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 Division of Revenue Act of South Africa, 2011 (Act No. 6 of 2011) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of consolidated 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 consolidated 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 consolidated financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements present fairly, in all material respects, the financial position of the Lejweleputswa District Municipality as at 30 June 2012, and their financial performance and cash flows for the year then ended in accordance with South African Standards of GRAP, 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 35 to the consolidated financial statements, the corresponding figures for 30 June 2011 have been restated as a result of an error discovered during 2012 in the consolidated financial statements of the Lejweleputswa District Municipality at and for the year ended 30 June 2012.

## **Irregular expenditure**

9. As disclosed in note 42 to the consolidated financial statements, irregular expenditure to the amount of R13 516 242 (2011:R3 211 471) was incurred mainly due to the non-adherence to supply chain management procedures as prescribed by Supply Chain Management Regulations (SCM). The full extent of the irregularities of R25 549 016 is still in the process of being determined.

## **Unauthorised expenditure**

10. As disclosed in note 40 to the consolidated financial statements, unauthorised expenditure to the amount of R227 750 (2011:R617 890) was incurred as a result of expenditure not incurred in terms of the approved budget.

## **Material Impairments and losses**

11. As disclosed in note 24 to the consolidated financial statements, a debt impairment provision to the amount of R9 246 284 was made for sundry debtors due to poor collection practices.

## **Additional matter**

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

## **Unaudited supplementary schedules**

13. The supplementary information set out on pages 219 to 240 does not form part of the consolidated 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 REGULATORY REQUIREMENTS**

### **PAA REQUIREMENTS**

14. 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**

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15. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages 70 to 159 of the annual report.
16. 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 annual reporting principles and whether the reported performance is consistent with the planned 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 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).

17. The material findings are as follows:

#### **Usefulness of information**

##### **Presentation**

18. Improvement measures in the annual performance report for a total of 74% of the planned targets not achieved were not disclosed as required by section 46 of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 200) (MSA). This was due to inadequate internal policies and procedures over the processes pertaining to the reporting of performance information.

##### **Consistency**

19. The MSA, section 41(c) requires that the integrated development plan should form the basis for the annual report, therefore requiring the consistency of objectives, indicators and targets between planning and reporting documents. A total of 78% of the reported indicators are not consistent with the indicators as per the approved integrated development plan. The municipality did not develop and implement policies and procedures to facilitate effective performance management, evaluation and reporting.
  
20. The MSA, section 41(c) requires that the integrated development plan should form the basis for the annual report, therefore requiring the consistency of objectives, indicators and targets between planning and reporting documents. A total of 79% of the reported targets are not consistent with the targets as per the approved integrated development plan. The municipality did not develop and implement policies and procedures to facilitate effective performance management, evaluation and reporting.

### **Measurability**

21. The FMPPI requires that performance targets be specific in clearly identifying the nature and required level of performance. A total of 98% of the targets relevant to good governance and public participation, local economic development, and basic service delivery and infrastructure investments were not specific in clearly identifying the nature and the required level of performance. This was mainly because the municipality did not develop and appropriately implement policies and procedures to facilitate the effective performance planning, monitoring, evaluation and reporting.
  
22. The FMPPI requires that performance targets be measurable. The required performance could not be measured for a total of 98% of the targets relevant to good governance and public participation, local economic development, and basic service delivery and infrastructure investments. This was mainly because the municipality did not develop and appropriately implement policies and procedures to facilitate the effective performance planning, monitoring, evaluation and reporting.

23. The FMPPI requires that indicators/measures should have clear unambiguous data definitions so that data is collected consistently and is easy to understand and use. A total of 77% of the indicators relevant to good governance and public participation, local economic development, and basic service delivery and infrastructure investments were not well defined in that clear, unambiguous data definitions were not available to allow for data to be collected consistently. This was mainly because the municipality did not develop and appropriately implement policies and procedures to facilitate the effective performance planning, monitoring, evaluation and reporting.
24. The FMPPI requires that it must be possible to validate the processes and systems that produce the indicator. A total of 100% of the indicators relevant to good governance and public participation, local economic development, and basic service delivery and infrastructure investments were not verifiable in that valid processes and systems that produce the information on actual performance did not exist. This was mainly because the municipality did not develop and appropriately implement policies and procedures to facilitate the effective performance planning, monitoring, evaluation and reporting.

### **Reliability of information**

#### **Validity**

25. The FMPPI requires that processes and systems which produce the indicator should be verifiable. I was unable to obtain all the information and explanations I considered necessary to satisfy myself as to the validity of the actual reported performance relevant to 74% of good governance and public participation, local economic development, and basic service delivery and infrastructure investments. This was due to limitations placed on the scope of my work by lack of appropriate systems to collect, collate, verify and store performance information. The institution's records did not permit the application of alternative audit procedures.

#### **Accuracy**

26. The FMPPI requires that the indicator be accurate enough for its intended use and respond to changes in the level of performance. I was unable to obtain all the information and explanations I considered necessary to satisfy myself as to the accuracy of the actual reported performance relevant to 74% of good governance and public participation, local economic development, and basic service delivery and infrastructure investments. This was due to limitations placed on the scope of my work by lack of appropriate systems to collect, collate, verify and store performance information. The institution's records did not permit the application of alternative audit procedures.

#### **Completeness**

27. The FMPPI requires that documentation addressing the systems and processes for identifying, collecting, collating, verifying and storing information be properly maintained. I was unable to obtain all the information and explanations I considered necessary to satisfy myself as to the completeness of the actual reported performance relevant to 100% of good governance and public participation, local economic development, and basic service delivery and infrastructure investments. This was due to limitations placed on the scope of my work by lack of appropriate systems to collect, collate, verify and store performance information. The institution's records did not permit the application of alternative audit procedures.

### **Compliance with laws and regulations**

28. I performed procedures to obtain evidence that the entity has 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**

29. The municipal council did not consult with the local community in the drafting and implementation of the municipality's IDP, by means of a municipal wide structure for community participation or through a forum that enhances community participation, as required by section 28 of the MSA and Local Government: Municipal planning and performance management regulations 15(1)(a)(i).
30. Lejweleputswa District Municipality which has sole control of Lejweleputswa Development Agency (municipal entity) did not ensure that annual performance objectives and indicators for the municipal entity are established by agreement and included in the municipal entity's multi-year business plan as required by section 93B(a) of the MSA.
31. The municipality did not afford the local community at least 21 days to comment on the final draft of its integrated development plan before the plan was submitted to council for adoption, as required by regulation 15(3) of the Municipal Planning and Performance Management Regulations.
32. The performance of the Lejweleputswa Development Agency was not monitored and annually reviewed, as part of the annual budget process, as required by section 93B(b) of the MSA.

#### **Budgets**

33. The municipality incurred expenditure that was not budgeted for and, in contravention of section 15 of the MFMA.

#### **Annual consolidated financial statements, performance and annual report**

34. The consolidated 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, vat, other receivable, employee costs, commitments, cash flow statements, contingent liabilities identified by the auditors were subsequently corrected, resulting in the consolidated financial statements receiving an unqualified audit opinion.
35. The accounting officer did not make the 2011 annual report public immediately after the annual report was tabled in the council, as required by section 127(5)(a) of the MFMA.
36. The accounting officer did not make public the council's oversight report on the 2011 annual report within seven days of its adoption, as required by section 129(3) of the MFMA.

#### **Internal audit**

37. The internal audit unit did not function as required by section 165(2) of the MFMA, in that:
  - it did not prepare a risk-based audit plan and an internal audit programme for the financial year under review.
  - it did not report to the audit committee on the implementation of the internal audit plan.

- it did not advise the accounting officer and report to the audit committee on matters relating to internal audit, internal controls, accounting procedures and practices, risk and risk management and loss control.

### **Procurement and contract management**

38. Goods and services with a transaction value of between R10 000 and R200 000 were procured without obtaining written price quotations from at least three different prospective providers as per the requirements of SCM regulation 17(a) & (c).
39. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids as per the requirements of SCM regulation 19(a) and 36(1)
40. Awards were made to providers whose directors / principal shareholders are persons in service of other state institutions, in contravention of SCM regulations 44.
41. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by the code of conduct for councillors issued in terms of the MSA.

### **Expenditure management**

42. The accounting officer did not take reasonable steps to prevent unauthorised and irregular expenditure as required by section 62(1)(d) of the MFMA.

### **Revenue management**

43. A credit control and debt collection policy was not implemented, as required by section 96(b) of the MSA and section 62(1)(f)(iii) of MFMA.

### **Internal control**

44. I considered internal control relevant to my audit of the consolidated financial statements, 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 findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

### **Leadership**

45. The accounting officer did not evaluate whether management had fulfilled their responsibilities of planning, directing and control on key business processes of procurement and management of performance information so as take corrective action where appropriate.
46. The accounting officer did not take timely and adequate action to address weaknesses in the supply chain management directorate, which resulted in non-compliance with applicable legislation and gave rise to unauthorised, and irregular expenditure.
47. The accounting officer did not take decisive action to address external audit findings previously reported in a timely manner. The municipality failed to properly analyse the control weaknesses and implement appropriate follow-up actions that adequately addressed the

root cause. This resulted in the audit findings in the prior year report being recurring in the current year.

48. Leadership failed to implement adequate controls to ensure compliance with laws, regulations and internally designed policies and procedures. As a result, significant non-compliance issues were noted.

#### **Financial and performance management**

49. The accounting officer did not ensure that the municipality implements appropriate processes and procedures to collect, collate, verify, store and report on performance information. This resulted in limitation of scope on the audit of performance information.
50. The accounting officer did not ensure that procurement of goods and services was made in accordance with Supply Chain Management regulations and possible conflict of interest with suppliers or related parties was avoided resulting in the municipality incurring irregular expenditure that could have been prevented.

#### **Governance**

51. The internal audit function did not fully perform its responsibilities. As a result internal control deficiencies were not timely identified and corrective actions and recommendations effectively implemented.
52. The accounting officer did not implement appropriate risk management activities to ensure that regular risk assessments, including information technology risks and fraud prevention, are conducted and that a risk strategy to address the risks is developed and monitored.

Bloemfontein

30 November 2012



**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*