

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

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of Xhariep District Municipality set out on pages XX to XX, which comprise the statement of financial position as at 30 June 2013, the statement of financial performance, statement of changes in net assets and the cash flow statement for the year then ended, and 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, 2012 (Act No. 5 of 2012) (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 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 financial statements are free from material misstatements.
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 qualified audit opinion.

Basis for qualified opinion

Property, plant and equipment

6. SA Standard of GRAP 17 states that "the useful life of an asset shall be reviewed at least at each reporting date and, if expectations differ from previous estimates, the change shall be accounted for as a change in an accounting estimate in accordance with the Standard of GRAP on Accounting Policies, Changes in Accounting Estimates and Errors. I was unable to obtain sufficient appropriate audit evidence regarding movable tangible assets, as the municipality did not account for the review of useful lives in the asset register submitted for audit. I was unable to confirm the carrying amount of Property, Plant and Equipment and depreciation by alternative means. Consequently I was unable to determine whether any adjustments relating to movable tangible assets stated at R 20 082 803 and depreciation stated at R3 370 483 in the financial statements were necessary.

Commitments

7. I was unable to obtain sufficient appropriate audit evidence that management has properly accounted for all commitments for the current and prior year due to the status of the accounting records. I was unable to confirm the commitments by alternative means. Consequently, I was unable to determine whether any adjustment to commitments stated at R 1 328 470 (2012: R 4 843 658) in the financial statements was necessary.

Opinion

8. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of Xhariep District Municipality as at 30 June 2013 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.

Emphasis of matters

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

Irregular expenditure

10. As disclosed in note 36 to the financial statements, the municipality incurred irregular expenditure of R 17 774 097 (2012: R 12 817 074) as proper procurement processes had not been followed as required by the supply chain management (SCM) regulations. The full extent of the irregular expenditure of R 17 774 097 is disclosed in note 36 to the financial statements.

Unauthorised expenditure

11. As disclosed in note 34 to the financial statements, the municipality incurred unauthorised expenditure of R 11 151 137 (2012: R 5 483 481) due to inadequate budgetary control measures.

Restatement of corresponding figures

12. As disclosed in note 33 to the financial statements, the corresponding figures for the year ended 30 June 2012 have been restated as a result of errors discovered during the year ended 30 June 2013 in the financial statements of Xhariep District Municipality at, and for the year ended, 30 June 2012.

Financial sustainability

13. The financial statements included in the annual report on page #to# indicates that the Xhariep District Municipality incurred a deficit of R 29 390 104 during the year ended 30 June 2013 and, as of that date, the municipality's unspent conditional grants and a receipt of R1 992 053 exceeds the cash balance held by the municipality of R1 819 068. The net cash flow from operating activities is negative by an amount of R11 886 257 and the current liability of R8 520 540 exceed the current asset of R3 729 369. These conditions, along with other matters as set forth in the note 41, indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern.

REPORT ON OTHER LEGAL AND REGULATORY 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

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 ... to ... 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's annual reporting principles and whether the reported performance is consistent with the planned development 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*.
17. 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).
18. There were no material findings on the annual performance report concerning the usefulness and reliability of the information.

Additional matter

19. Although no material findings concerning the usefulness and reliability of the performance information were identified in the annual performance report, I draw attention to the following matter below. This matter does not have an impact on the predetermined objectives reported above.

Achievement of planned targets

20. Of the total number of 133 targets planned for the year, 47 of targets were not achieved during the year under review. This represents 35% of total planned targets that were not achieved during the year under review.

Compliance with laws and regulations

21. 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:

Annual financial statements, performance and annual reports

22. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA.

Expenditure management

23. The accounting officer did not take reasonable steps to prevent unauthorised, irregular and fruitless and wasteful expenditure, as required by section 62(1) (d) of the MFMA.
24. Unauthorised, irregular and fruitless and wasteful expenditure was not investigated and as a result it was not recovered from the liable person, as required by section 32(2) of the MFMA.
25. Money owing by the municipality was not always paid within 30 days or an agreed period, as required by section 65(2)(e) of the MFMA.

Procurement and contract management

26. Sufficient appropriate audit evidence could not be obtained that bids were evaluated by bid evaluation committees which were composed of officials from the municipality requiring the goods or services and at least one SCM practitioner of the municipality as required by SCM regulation 28(2).

Conditional Grants received

27. The municipality did not submit the evaluation to the transferring national officer within two months after the end of the financial year, as required by section 12(5) of DoRA.

Budgets

28. Monthly budget statements were not submitted on time to the Mayor and the relevant Provincial Treasury as required by section 71(1) of the MFMA.
29. 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.

Revenue management

30. An effective system of internal control for debtors was not in place, as required by section 64(2) of the MFMA.
31. Interest was not charged on all accounts in arrears, as required by section 64(2) (g) of the MFMA.

Asset Management

32. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the Municipal Finance Management Act.

Consequences management

33. Unauthorised, irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in accordance with the requirements of section 32(2) of the MFMA.

Internal control

34. I considered internal control relevant to my audit of the 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 compliance with laws and regulations included in this report.

Leadership

35. The leadership of Xhariep District Municipality neglected to evaluate whether management had implemented effective internal controls. They did not gain a comprehensive understanding of how senior management members had met their responsibilities in terms of ensuring proper record management for preparing the financial statements and monitoring compliance to laws and regulations.
36. The leadership neglected to take appropriate action to address the lack of discipline in the finance and SCM directorates; this resulted in non-compliance matters reported above which in turn gave rise to the high level of irregular expenditure incurred in the financial statements.
37. The leadership of the municipality neglected to develop, implement and monitor internal control procedures to ensure that financial statements are prepared and subject to review. This oversight resulted in the challenge faced to submit financial statements to audit that are fully compliant to the SA Standards of GRAP and necessitated the amendment of financial statements provided for audit purposes and a qualified audit opinion.

Financial and performance management

38. Due to inadequate oversight on the part of senior management of the district municipality the regular review and monitoring of compliance to laws and regulations were not sufficiently prioritised. As a result, material non-compliance issues were noted that could have been prevented.
39. The municipality did not have the human resource capacity throughout the financial year to adequately address prior year issues and weaknesses identified in the financial and control systems of the district municipality. This necessitated the municipality to make use of consultants to supplement such constraints.
40. Due to time pressure brought about by the fact that the process of preparing the financial statements was only started late in the financial year, sufficient time was not available to the Accounting Officer to properly review such statements for completeness and accuracy prior to submission thereof for auditing. This resulted in numerous findings relating to different account balances, classes of transactions and disclosures.
41. Staff within the finance and SCM directorate of the district municipality has insufficient understanding of the accounting framework and the SCM regulations. This contributed towards the misstatements identified in the financial statements and non-compliance with laws and regulations.

Bloemfontein

30 November 2013



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence