

Report of the auditor-general to the Northern Cape provincial legislature and the council on the Gamagara Local Municipality

Report on the financial statements

Introduction

1. I have audited the financial statements of the Gamagara Local Municipality set out on pages ... to ..., 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 the statement of comparison of budget and actual information 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 qualified audit opinion.

Basis for qualified opinion

Property, plant and equipment

6. The municipality did not assess impairment of property, plant and equipment for the current and prior year relating to community buildings and operational buildings, at each reporting date in accordance with the GRAP 17, Property, plant and equipment. I did not determine the correct net carrying amount of these assets as it was impracticable to do so. Additionally, there was a resultant impact on the surplus for the period and the accumulated surplus.
7. The municipality did not review the residual values and useful lives of property, plant and equipment relating to buildings, community assets and other assets at each reporting date for the current and prior year in accordance with the GRAP 17. I did not determine the correct net carrying amount of these assets as it was impracticable to do so. Additionally, there was a resultant impact on the surplus for the period and the accumulated surplus.
8. The municipality did not capitalise all items of property, plant and equipment in accordance with GRAP 17. Consequently, property, plant and equipment relating to land, infrastructure and other assets was understated for the current and prior year. I did not determine the correct net carrying amount of these assets as it was impracticable to do so. Additionally, there was a resultant impact on the surplus for the period and the accumulated surplus.
9. The municipality did not disclose property, plant and equipment in accordance with GRAP 17. Property, plant and equipment is overstated and investment property understated by R17 876 764, as land and buildings used for investment purposes was incorrectly classified as property, plant and equipment. Additionally, there was a resultant impact on the surplus for the period and on the accumulated surplus in the financial statements.
10. I was unable to obtain sufficient appropriate audit evidence for property, plant and equipment for the current and prior year relating to infrastructure as well as land and buildings. Additionally I was unable to obtain sufficient appropriate audit evidence for property, plant and equipment for the current year relating to community assets and other assets, as the municipality did not have adequate systems in place to maintain records of property, plant and equipment and the calculation of depreciation. I was unable to confirm the expenditure by alternative means. Consequently, I was unable to determine whether any adjustments to these items of property, plant and equipment stated in the financial statements were necessary.

Investment property

11. The municipality did not reflect market conditions in the value of investment property at reporting date, as required by GRAP 16 *Investment property*. I did not determine the correct net carrying amount of these assets as it was impracticable to do so. Additionally, there was a resultant impact on the surplus for the period and the accumulated surplus.

Expenditure

12. I was unable to obtain sufficient appropriate evidence for expenditure relating to general expenditure as well as repairs and maintenance for the current and prior year as the municipality did not have adequate systems in place to maintain records of expenditure and prior year corrections. I was unable to confirm the expenditure by alternative means. Consequently, I was unable to determine whether any adjustments to expenditure stated at R50 738 101 (2014: R38 975 804) in the financial statements were necessary.

Receivables from non-exchange transactions

13. I was unable to obtain sufficient appropriate evidence for the provision for impairment as the municipality did not have adequate systems in place to account for impairment. I was unable to confirm the impairment by alternative means. Consequently, I was unable to determine whether any adjustments to impairments stated at R64 820 632 noted 6 in the financial statements was necessary.

Receivables from exchange transactions

14. I was unable to obtain sufficient appropriate evidence for the provision for impairment as the municipality did not have adequate systems in place to account for impairment. I was unable to confirm the impairment by alternative means. Consequently, I was unable to determine whether any adjustments to impairments stated at R30 813 056 noted 5 in the financial statements was necessary.

Qualified opinion

15. 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 the Gamagara Local 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

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

Restatement of corresponding figures

17. As disclosed in note 58 to the financial statements, the corresponding figures for 30 June 2014 have been restated as a result of an error discovered during 2015 in the financial statements of the municipality at, and for the year ended, 30 June 2014.

Material losses

18. As disclosed in note 49 to the financial statements, material losses to the amount of R13 803 689 were incurred as a result of bulk electricity and water losses.

Irregular expenditure

19. As disclosed in note 47 to the financial statements, irregular expenditure incurred to the amount of R42 025 327. In addition, the full extent of the irregularities, as disclosed in note 47 to the financial statements, was still in the process of being determined

Additional matters

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

Unaudited supplementary schedules

21. 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 this schedule and, accordingly, I do not express an opinion thereon.

Unaudited disclosure notes

22. 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

23. 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

24. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2015:
 - Development priority (1): Basic service delivery and infrastructure investment on page 17
 - Development priority (5): Community safety, development and sustainable environment on pages 22
25. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
26. 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 priorities. 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).

27. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
28. The material findings in respect of the selected development priorities are as follows:

Basic service delivery and infrastructure investment

Usefulness of reported performance information

29. Section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) requires that the integrated development plan should form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. In total, 40% of the reported indicators were not consistent with those in the approved service delivery and budget implementation plan. This was due to a lack of an approved framework of properly documented processes and procedures that addressed the effective and efficient functioning of the performance management system.
30. Section 41(c) of the MSA requires actual achievements against all planned indicators and targets to be reported annually. The annual performance report submitted for audit purposes did not include the actual performance of 100% of all planned targets specified in the service delivery and budget implementation plan for the year under review. This was due to a lack of information systems recording and documenting actual achievements against targets.
31. Performance indicators should be well defined by having clear definitions so that data can be collected consistently and is easy to understand and use, as required by the FMPPI. In total, 100% of the indicators were not well defined.
32. The processes and systems that produced the indicator should be verifiable, as required by the FMPPI. In total, 100% of the indicators were not verifiable. This was because management did not adhere to the requirements of the FMPPI.
33. Performance targets should be specific in clearly identifying the nature and required level of performance as required by the FMPPI. A total of 100% of the targets were not specific.
34. Performance targets should be measurable as required by the FMPPI. We could not measure the required performance for 100% of the targets.

Reliability of reported performance information

35. 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 the reported performance information. This was due to the facts that the auditee could not provide sufficient appropriate evidence in support of the reported

performance information and that the auditee's records did not permit the application of alternative audit methods.

Community safety, development and sustainable environment

Usefulness of reported performance information

36. Section 41(c) of the MSA requires that the integrated development plan should form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. In total, 25% of the reported indicators were not consistent with those in the approved service delivery and budget implementation plan. This was due to a lack of an approved framework or properly documented processes and procedures that addressed the effective and efficient functioning of the performance management system.
37. Section 41(c) of the MSA requires actual achievements against all planned indicators and targets to be reported annually. The annual performance report submitted for audit purposes did not include the actual performance of 100% of all planned targets specified in the service delivery and budget implementation plan for the year under review. This was due to a lack of information systems recording and documenting actual achievements against targets.
38. Performance indicators should be well defined by having clear definitions so that data can be collected consistently and is easy to understand and use, as required by the FMPPI. In total, 100% of the indicators were not well defined.
39. The processes and systems that produced the indicator should be verifiable, as required by the FMPPI. In total, 100% of the indicators were not verifiable. This was because management did not adhere to the requirements of the FMPPI.
40. Performance targets should be specific in clearly identifying the nature and required level of performance as required by the FMPPI. A total of 100% of the targets were not specific.
41. Performance targets should be measurable as required by the FMPPI. We could not measure the required performance for 100% of the targets.

Reliability of reported performance information

42. 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 the reported performance information. This was due to the facts that the auditee could not provide sufficient appropriate evidence in support of the reported performance information and that the auditee's records did not permit the application of alternative audit methods.

Additional matters

43. I draw attention to the following matters:

Achievement of planned targets

44. Refer to the annual performance report on pages **x to x and 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 usefulness and reliability of the reported performance information for the selected development priorities reported in paragraphs **26 to 36** of this report.

Unaudited supplementary schedules and information

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

Compliance with legislation

46. 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:

Strategic planning and performance management

47. The performance management system did not provide for the monitoring, measuring and review of performance at least once per year, as required by section 41 of the Municipal Systems Act.
48. The performance management system did not provide for the monitoring, measuring and review of performance at least once per year, as required by section 41 of the Municipal Systems Act.
49. Key performance indicators, including input, output and outcome indicators, in respect of each of the development priorities and objectives were not set out in the IDP, as required by section 41(1)(a) of the Municipal Systems Act and the municipal planning and performance management regulations 1 and 9(1)(a).
50. The performance management system and related controls were inadequate as it did not describe and represent the processes of performance monitoring, measurement, review, reporting as well as improvement and how it is conducted, organised and managed, as required by sections 38 of the MSA and regulation 7 of the municipal planning and performance management regulations.
51. The performance management system did not provide for policies and procedures to take steps of improvement where performance targets were not met, as required by section 41 (1)(d) of the Municipal Systems Act.

52. The municipality did not establish mechanisms to monitor and review its performance management system, as required by section 40 of the Municipal Systems Act.
53. The KPIs set by the municipality did not include indicators on percentage of households with access to basic level of water, sanitation; electricity and solid waste removal were not set by the municipality as required by section 43(2) of the Municipal Systems Act and the municipal planning and performance management regulation 10(a).

Financial statements, performance and annual reports

54. 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 identified by the auditors in the submitted financial statements were not adequately corrected and/or the supporting records could not be provided subsequently, which resulted in the financial statements receiving a qualified audit opinion.
55. The annual performance report for the year under review did not include:
 - a comparison with the previous financial year as required by section 46 (1)(b) of the Municipal Systems Act.
 - measures taken to improve performance, as required by section 46 (1)(c) of the MSA.

Audit committees

56. The audit committee did not meet at least four times a year, as required by section 166(4)(b) of the MFMA.

Procurement and contract management

57. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations, as required by supply chain management (SCM) regulation 17(a) & (c).
58. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
59. Sufficient appreciation audit evidence could not be obtained that bid specifications were drafted by bid specification committees which were composed of one or more officials of the municipality, as required by SCM regulation 27(3).
60. Awards were made to providers who were in the service of other state institutions or whose directors/ principal shareholders were in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulation 44. Similar awards were identified in the prior year and no effective steps were taken to prevent or combat the abuse of the SCM process in accordance with SCM regulation 38(1).
61. Sufficient appropriate audit evidence could not be obtained that persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality to disclose such interest, as required by SCM regulation 46(2)(e).
62. A list of accredited prospective providers was not in place for procuring goods and services through quotations, as required by SCM regulation 14(1)(a).
63. Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).

64. Contracts were awarded to bidders based on preference points that were not calculated in accordance with the requirements of the Preferential Procurement Policy Framework Act and its regulations.
65. Invitations for competitive bidding were not always advertised for a required minimum period of days, as required by SCM regulation 22(1) & 22(2).
66. Quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
67. Quotations were awarded to providers whose tax matters had not been declared by the South African Revenue Service to be in order, as required by SCM regulation 43.

Human resource management and compensation

68. The municipality did not submit a report on compliance with prescribed competency levels to the National Treasury and relevant provincial treasury, as required by the municipal regulations on minimum competency levels 14(2)(a).
69. 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.

Expenditure management

70. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
71. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure, and fruitless and wasteful expenditure, as required by section 62(1) (d) of the MFMA.

Conditional grants received

72. The municipality did not evaluate its performance in respect of programmes funded by the Municipal Infrastructure Grant allocation, as required by section 12(5) of the DoRA.
73. The municipality did not evaluate its performance in respect of programmes or functions funded by the Municipal Systems Improvement Grant allocation, as required by section 12(5) of the DoRA.
74. The municipality did not evaluate its performance in respect of programmes or functions funded by the Local Government Financial Management Grant allocation, as required by section 12(5) of the DoRA.

Asset and liability management

75. An effective system of internal control for assets was not in place, as required by section 63(2) (c) of the MFMA.

Consequence management

76. Sufficient appropriate audit evidence could not be obtained that unauthorised, irregular as well as fruitless and wasteful expenditure incurred by the municipality was investigated to determine if any person was liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.

Internal control

77. 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 basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

Leadership

78. The accounting officer did not evaluate whether management had implemented effective internal controls by gaining an understanding of how senior management had met its responsibilities.
79. The leadership did not ensure adherence to the SCM policy at the municipality, which resulted in processes not preventing irregular expenditure and material non-compliance.
80. The municipality did not review and monitor compliance with applicable laws and regulations.
81. The accounting officer should develop and monitor the implementation of action plans to address internal control deficiencies prevailing in the supply chain management.

Financial and performance management

82. Quality was not understood by all staff to be a prerequisite and it was not embedded in the municipality's values, which led to various cases of non-compliance with legislation and material amendments to the financial statements.
83. The systems underlying the procurement processes at the municipality were inadequate to prevent and detect irregular expenditure on contracts entered into, resulting in irregular expenditure that was disclosed in the accounting records of the municipality. Effective and appropriate disciplinary steps were not taken against officials who made and permitted unauthorised, irregular, and fruitless and wasteful expenditure.
84. There were deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations and performance information.
85. The underlying systems and controls were inadequate to provide reliable and accurate evidence to support the reporting on predetermined objectives.
86. Senior management did not perform an adequate review of the actual performance against predetermined objectives reported. Therefore, the integrated development plan (IDP), service delivery and budget implementation plan (SDBIP) and the annual performance report (APR) were inconsistent.
87. The municipality did not have an adequate performance management system for the planning, collection, collation, monitoring, reviewing and reporting of performance information. The municipality did not have specific business processes which detailed how its performance management system worked, from the setting of objectives, indicators and targets through to reporting on objectives, indicators and targets.

Governance

88. The municipality utilised the shared internal audit division within the John Taolo Gaetsewe District Municipality. Performance information was not audited by the shared internal audit during the 2012-13 and 2013-14 financial years.
89. The municipality utilised the shared audit committee within the John Taolo Gaetsewe District Municipality. The audit committee did not review the performance management systems and did not make recommendations to the councils in this regard.

Kimberley

30 November 2015



Auditing to build public confidence