

## **AUDITOR'S REPORT OF THE AUDITOR-GENERAL TO THE EASTERN CAPE PROVINCIAL LEGISLATURE AND THE COUNCIL ON SENQU MUNICIPALITY**

### **REPORT ON THE FINANCIAL STATEMENTS**

#### **Introduction**

1. I have audited the accompanying financial statements of the Senqu Municipality, which comprise the statement of financial position as at 30 June 2010, and the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information, and the accounting officer's report, as set out on pages ... to ....

#### **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 in the manner required by the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and Division of Revenue Act of South Africa, (DoRA). This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

#### **Auditor-General's responsibility**

3. As required by section 188 of the Constitution of South Africa, 1996 (Act No. 108 of 1996), section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and section 126(3) of the MFMA my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with International Standards on Auditing and *General Notice 1570 of 2009* issued in *Government Gazette 32758 of 27 November 2009*. 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.
5. 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.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

### **Opinion**

7. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Senqu Municipality as at 30 June 2010 and its financial performance and its cash flows for the year then ended, in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) described in note 1 to the financial statements and in the manner required by the MFMA and DORA.

### **Emphasis of matters**

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

### **Material losses**

9. As disclosed in note 40.4 to the financial statements, the municipality suffered a significant electricity loss of 9 million kilowatts amounting to R2.8 million.

### **Unauthorised and, fruitless and wasteful and irregular expenditure**

10. Unauthorised expenditure of R1.9 million is disclosed in note 40.1 to the financial statements. The unauthorised expenditure was incurred as a result of management's failure to effectively monitor the implementation of internal controls designed to prevent, detect and correct instances where expenditure exceeds the budget approved by the council.
11. As disclosed in note 40.2 to the financial statements, fruitless and wasteful expenditure to the amount of R2.8 million was incurred due to the excessive distribution loss experienced by the municipality.
12. Furthermore, note 40.3 to the financial statements disclosed irregular expenditure to the amount of R1.6 million relating to supply chain processes and procedures not being followed and non-compliance with the Municipal Systems Act 32 of 2000 (MSA) with respects to the payment of performance bonuses.

### **Additional matters**

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

### **Unaudited supplementary schedules**

14. 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 schedule(s) and accordingly I do not express an opinion thereon.

### **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

15. As required by the PAA and in terms of *General Notice 1570 of 2009* issued in *Government Gazette 32758 of 27 November 2009*, I include below my findings on the report on predetermined objectives, compliance with the following key laws and regulations including the Municipal Finance Management Act 56 of 2003 (MFMA) and the Municipal Systems Act (Act No. 32 of 2000) (MSA), and financial management (internal control).

**Predetermined objectives**

16. Material findings on the report on predetermined objectives, as set out on pages ... to ..., are reported below:

**Non-compliance with regulatory and reporting requirements****Submission of the IDP to the MEC for Local Government in the Province**

17. The municipality could not provide documentary evidence for proof of the submission of a copy of the IDP to the MEC for Local Government in the province within 10 days after the adoption of the IDP by the municipal council, as required by Section 32 of the Municipal Systems Act 32 of 2000 (MSA).

**Notice of IDP approval not given**

18. Notice of IDP approval was not given to the public within 14 days of the approval of the IDP, as required by Section 25 (4) (a) and (b) of the Municipal Systems Act 32 of 2000 (MSA).

**Performance agreements were not concluded within one month after the beginning of the financial year**

19. The municipality did not conclude performance agreements with the municipal manager and managers directly accountable to the municipal manager within one month after the beginning of the financial year, as required by Section 57 (2) (a) of the Municipal Systems Act 32 of 2000 (MSA).

**Performance evaluation of Municipal employees and suppliers was not performed**

20. Performance evaluations of municipal employees and suppliers was not performed for the year under review, as required by Section 41 of the Municipal Systems Act (Act No. 32 of 2000) (MSA).

**SDBIP not updated**

21. The SDBIP of the municipality relating to the 2009/2010 financial year was not updated as a number of performance measures and indicators presented were with respect to the 2008/09 financial year, which is not in compliance with Section 54(1) of the Municipal Finance Management Act 56 of 2003 (MFMA).

**Financial plan does not include a budget projection for the next three years**

22. The integrated development plan of the municipality does not include a budget projection for the next three years in the financial plan, as required by Section 26 (h) of the Municipal Systems Act (Act No. 32 of 2000) (MSA).

**Performance assessment of the Municipality not completed within prescribed time frame**

23. The performance assessment of the municipality was not submitted to the Council before 25 January 2010 and the municipality could not provide documentary evidence for the submission of the performance report assessment of the municipality to the mayor of the municipality, the National Treasury and the Provincial Treasury, as required by Section 72(1) of the Municipal Finance Management Act 56 of 2003 (MFMA).

### **The Integrated Development Plan (IDP) does not reflect performance targets**

24. Key performance targets are not disclosed in the IDP for the 2009/2010 financial year as required by Section 26(i) of the Municipal Systems Act 32 of 2000 (MSA).

### **SDBIP approval**

25. The municipality's SDBIP was not approved by the Mayor within 28 days after the approval of the budget as required by Section 53 (1) (c) (ii) of the Municipal Finance Management Act 56 of 2003 (MFMA).

### **Usefulness of reported performance information**

26. The following criteria were used to assess the usefulness of the planned and reported performance:
- Consistency: Has the municipality reported on its performance with regard to its objectives, indicators and targets in its approved integrated development plan] i.e. are the objectives, indicators and targets consistent between planning and reporting documents?
  - Relevance: Is there a clear and logical link between the objectives, outcomes, outputs, indicators and performance targets?
  - Measurability: Are objectives made measurable by means of indicators and targets? Are indicators well defined and verifiable, and are targets specific, measurable, and time bound?

The following audit findings relate to the above criteria:

27. The objectives in the service delivery budget implementation plan (SDBIP) are not measurable, as key performance indicators (KPI's) for the objectives do not measure the expected service delivery outcomes.
28. The objectives contained in the integrated development plan (IDP) outline broad strategies of the municipality which are not specific, measurable and time-bound.
29. The KPI's disclosed in the integrated development plan (IDP) are not in line with the KPI's disclosed in the SDBIP and the annual performance report. Furthermore, performance targets contained in the performance agreements for the managers accountable to the municipal manager and the annual performance report are disclosed as percentages and the basis for measurement of performance is not specific and time bound. Therefore, performance targets of the municipality do not measure the efficiency, effectiveness, quality and impact of the performance of the municipality.

### **Reliability of reported performance information**

30. The following criteria were used to assess the reliability of the planned and reported performance:
- Validity: Has the actual reported performance occurred and does it pertain to the entity i.e. can the reported performance information be traced back to the source data or documentation?
  - Accuracy: Amounts, numbers and other data relating to reported actual performance has been recorded and reported appropriately.
  - Completeness: All actual results and events that should have been recorded have been included in the reported performance information.

The following audit finding relates to the above criteria:

31. The performance management system of the municipality does not disclose detail on how performance information will be collated and included in the annual report. Furthermore, the performance management system does not disclose details of the official(s) responsible for the accurate collation, collection, recording, processing, monitoring and review of performance against pre-determined objectives and does not clarify the processes of implementing the performance management system within the framework of the service delivery objectives as contained in the SDBIP and the IDP.

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

Included below are findings related to material non-compliance with the acts as indicated.

### **Municipal Finance Management Act of South Africa, No 56 of 2003 (MFMA)**

#### **Material misstatements corrected in the financial statements**

32. In order for the financial statements to meet the requirements of section 122(1) of the MFMA, material misstatements identified during the audit were corrected by management.

#### **Expenditure was not paid within the parameters set by the applicable legislation**

33. Expenditure was not paid in all instances within the required 30 days from the receipt of an invoice, or such a period as prescribed for certain categories of expenditure as required by section 65(2)(e) of the Municipal Finance Management Act.

#### **Expenditure was incurred otherwise than in accordance with sections 15 and 11(3) of the MFMA resulting in unauthorised expenditure**

34. As disclosed in note 40.1 to the financial statements, expenditure was not incurred in accordance with the approved budget of the municipality and exceeded the limits of the amounts appropriated for the different votes in the approved budget of the municipality.

#### **Expenditure was incurred in contravention of or not in accordance with applicable legislation resulting in irregular expenditure**

35. As disclosed in note 40.3 to the financial statements, expenditure was not incurred in accordance with the requirements of the supply chain management policy of the municipality or municipal entity or the requirements of the municipality's by-laws giving effect to such policy as set out in section 1 the definition of "irregular expenditure" paragraph (d) of the MFMA.
36. As disclosed in note 40.3 to the financial statements, expenditure not was incurred in accordance with the requirements of the Municipal Systems Act as set out in section 1 the definition of "irregular expenditure" paragraph (b) of the MFMA.

#### **Expenditure incurred was made in vain or could have been avoided resulting in fruitless and wasteful expenditure**

37. As disclosed in note 40.2 to the financial statements, expenditure incurred was made in vain, and could have been avoided based on the fact that reasonable care had not been exercised, as set out in section1 the definition of "fruitless and wasteful expenditure" of the MFMA.



### **Capital Projects not considered by the Council in terms of section 19 of the MFMA**

38. The municipality does not comply with section 19 (2) of the Municipal Finance Management Act, in that the projected cost covering all financial years until capital projects are operational and the future operational costs and revenue on the projects, including municipal tax and tariff implications, are not considered by the council prior to the approval of the capital projects.

### **Municipal Systems Act 32 of 2000 (MSA)**

#### **Expenditure was incurred in contravention of or not in accordance with applicable legislation resulting in irregular expenditure**

39. Expenditure not was incurred in accordance with the requirements of the Municipal Systems Act as set out in section 1 the definition of "irregular expenditure" paragraph (b) of the MFMA.

### **INTERNAL CONTROL**

40. I considered internal control relevant to my audit of the financial statements and the report on predetermined objectives, but not for the purpose of expressing an opinion on the effectiveness of internal control.
41. The matters reported below are limited to the significant deficiencies regarding the findings on the report on predetermined objectives and the findings on compliance with laws and regulations.

#### **Leadership**

42. Management's philosophy is positive, however, oversight responsibilities over performance reporting, compliance with laws and regulations and internal control are not exercised and the accounting officer does not evaluate whether management has implemented effective internal controls, risk management and performance management.

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

43. Pertinent information is not always identified in a form and time frame to support financial and performance reporting and compliance with legislation.

#### **Governance**

44. No formal training and skills development was provided to the in-house internal auditor. Furthermore, the in-house internal audit did not discharge all their responsibilities for the year as per the annual internal audit plan as approved by the audit committee.

### **OTHER REPORTS**

#### **Investigations in progress**

45. The South African Police Service and Standard Bank are currently conducting an investigation into the unauthorised transfer of funds amounting to R600 000 from the municipality's bank account that occurred in June 2009. This fraudulent transaction was reported to the Executive Committee on 24th June 2009. An amount of R334 958 was recovered and the balance amounting to R265 041 was then disclosed as fruitless and wasteful expenditure in the financial statements.

**Investigations completed during the financial year**

46. The municipality dismissed a number of officials from the traffic services department following an investigation into the issue of motor vehicle licences by the said officials for no monetary consideration.

*Auditor General*

East London

29 November 2010



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SOUTH AFRICA

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