

REPORT OF THE AUDITOR-GENERAL TO THE FREE STATE LEGISLATURE AND THE COUNCIL ON DILABENG LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of Dihlabeng Local Municipality set out on pages xx to xx, which comprise the appropriation statement, the statement of financial position as at 30 June 2014, the statement of financial performance, statement of changes in net assets and cash flow statement 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 the 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 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 unqualified audit opinion.

Opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of Dihlabeng Local Municipality as at 30 June 2014 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

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 45 to the financial statements, the municipality incurred unauthorised expenditure of R34 392 693 (2013: R126 077 221) during the year under review due to expenditure in excess of the amounts provided for in the votes of the approved budget.

Fruitless and wasteful expenditure

9. As disclosed in note 46 to the financial statements, the municipality incurred fruitless and wasteful expenditure of R11 094 761 (2013: R6 388 788) during the year under review due to interest and penalties charged on overdue accounts.

Irregular expenditure

10. As disclosed in note 47 to the financial statements, Dihlabeng Local Municipality incurred irregular expenditure of R86 461 457 (2013: R48 405 743) during the year under review due to non-compliance with supply chain management (SCM). Of this amount, R54 153 457 relates to the previous year.

Financial sustainability

11. Note 6.1 of the accounting officer's report indicates that the Dihlabeng Local Municipality assessed its ability to continue in operation and meet its statutory and financial obligations for the foreseeable future. The assessment revealed the following concerns:
 - The recoverability of debtors is a problem, hence the large provision for doubtful debt.
 - The overdrawn cash book balance and short portion of long-term debt to operating revenue ratio showed an increase from 1,72% (2012-13) to 4,88% (2013-14).
 - Although the personnel costs are within the norm of 30%, the ratio is still too high due to the impairment of debt and the municipality should make all possible efforts to reduce it to at least 30% excluding impairment of debt in the next financial year to ensure that the municipality is able to meet all its financial obligations.
 - Unauthorised expenditure of 34 392 693 (2013: 126 077 221).

This may impact significantly on the delivery of services and the achievement of annual performance plan targets as set for the coming year.

Restatement of corresponding figures

12. As disclosed in note 41 to the financial statements, the corresponding figures for 30 June 2013 have been restated as a result of errors discovered during the 2013-14 financial year in the financial statements of the municipality at, and for the year ended, 30 June 2013.

Material losses/impairments

13. As disclosed in note 3 to the financial statements, material losses to the amount of R43 252 116 were incurred as a result of a write-off of irrecoverable trade debtors.
14. As disclosed in note 22 to the financial statements, the municipality incurred 42% as a result of water distribution losses.

Additional matters

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

Unaudited disclosure notes

16. 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

17. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings on the reported performance information against predetermined objectives for selected programmes presented in the annual performance report, compliance with legislation as well as 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

18. 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 local municipality for the year ended 30 June 2014:
- Development priority 1: Access to water and sanitation on pages x to x
 - Development priority 2: Access to roads and storm water management on pages x to x
 - Development priority 3: Access to electricity on pages x to x
 - Development priority 4: Human settlement and town planning on pages x to x
 - Development priority 5: Access to refuse removal and solid waste disposal on pages x to x
19. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
20. 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).
21. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
22. The material findings in respect of the selected development priorities are as follows:

Development priority 1: Access to water and sanitation

Usefulness of reported performance information

23. The FMPPI requires the following:

- Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 33% (>20%) of the targets were not specific.
- Performance targets must be measurable. We could not measure the required performance for 33% (>20%) of the targets.
- The period or deadline for delivery of targets must be specified. A total of 44% (>20%) of the targets were not time bound.

This was because management did not adhere to the requirements of the FMPPI due to a lack of proper systems and processes, and technical indicator descriptions.

Reliability of reported performance information

24. I did not raise any material findings on the reliability of the reported performance information for development priority 1: access to water and sanitation.

Development priority 2: Access to roads and storm water management

Usefulness of reported performance information

25. The FMPPI requires the following:

- Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 22% (>20%) of the targets were not specific.
- Performance targets must be measurable. We could not measure the required performance for 22% (>20%) of the targets.
- The period or deadline for delivery of targets must be specified. A total of 22% (>20%) of the targets were not time bound.
- Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 100% (>20%) of the indicators were not well defined.
- Performance indicator must be verifiable, meaning that it must be possible to validate the processes and systems that produced the indicator. A total of 100% (>20%) of the indicators were not verifiable.

This was because management did not adhere to the requirements of the FMPPI due to a lack of proper systems and processes and technical indicator descriptions.

Reliability of reported performance information

26. I did not raise any material findings on the reliability of the reported performance information for development priority 2: access to roads and storm water management.

Development priority 3: Access to electricity

Usefulness of reported performance information

27. The FMPPI requires the following:

- Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 38% (>20%) of the targets were not specific.

- The period or deadline for delivery of targets must be specified. A total of 38% (>20%) of the targets were not time bound.
- Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 100% (>20%) of the indicators were not well defined.
- Performance indicator must be verifiable, meaning that it must be possible to validate the processes and systems that produced the indicator. A total of 100% (>20%) of the indicators were not verifiable.

This was because management did not adhere to the requirements of the FMPPI due to a lack of proper systems and processes and technical indicator descriptions.

Reliability of reported performance information

28. I did not raise any material findings on the reliability of the reported performance information for development priority 3: access to electricity.

Development priority 4: Human settlement and town planning

Usefulness of reported performance information

29. The FMPPI requires the following:

- Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 33% (>20%) of the targets were not specific.
- Performance targets must be measurable. We could not measure the required performance for 33% (>20%) of the targets.
- The period or deadline for delivery of targets must be specified. A total of 33% (>20%) of the targets were not time bound.
- Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 100% (>20%) of the indicators were not well defined.
- Performance indicator must be verifiable, meaning that it must be possible to validate the processes and systems that produced the indicator. A total of 100% (>20%) of the indicators were not verifiable.

This was because management did not adhere to the requirements of the FMPPI due to a lack of proper systems and processes and technical indicator descriptions.

Reliability of reported performance information

30. I did not raise any material findings on the reliability of the reported performance information for development priority 4: human settlement and town planning.

Development priority 5: Access to refuse removal and solid waste disposal

Usefulness of reported performance information

31. The FMPPI requires the following:

- Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 25% (>20%) of the targets were not specific.
- Performance targets must be measurable. We could not measure the required performance for 25% (>20%) of the targets.

- The period or deadline for delivery of targets must be specified. A total of 25% (>20%) of the targets were not time bound.
- Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 100% (>20%) of the indicators were not well defined.
- Performance indicator must be verifiable, meaning that it must be possible to validate the processes and systems that produced the indicator. A total of 100% (>20%) of the indicators were not verifiable.

This was because management did not adhere to the requirements of the FMPPI due to a lack of proper systems and processes and technical indicator descriptions.

Reliability of reported performance information

32. I did not raise any material findings on the reliability of the reported performance information for development priority 5: access to refuse removal & solid waste disposal.

Additional matters

33. I draw attention to the following matters:

Achievement of planned targets

34. 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 usefulness and reliability of the reported performance information for the selected development priorities reported in paragraphs x to xx of this report.

Adjustment of material misstatements

35. I identified material misstatements in the annual performance report submitted for auditing on the reported performance information for development priority 1: access to water and sanitation, development priority 2: access to roads and storm water management, development priority 3: access to electricity, development priority 4: human settlement and town planning and development priority 5: access to refuse removal and solid waste disposal. As management subsequently corrected the misstatements, I did not raise any material findings on the reliability of the reported performance information. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness of the reported performance information.

Unaudited supplementary schedules

36. 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.

Audit findings in the auditor's report

37. We will report all the audit findings included under the basis for conclusion and additional matter sections of this report in the auditor's report.

Compliance with legislation

38. I performed procedures to obtain evidence that Dihlabeng Local 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

39. Measurable performance targets for the financial year with regard to each of the development priorities or objectives and key performance indicators were not set in the IDP, as required by section 41(1)(b) of the Municipal Systems Act and the Municipal planning and performance management regulation 12(1) and 12(2)(e).
40. The annual performance report for the year under review did not include a comparison with the previous financial year and measures taken to improve performance, as required by section 46 (1)(a)/(b)/(c) of the Municipal Systems Act.
41. The performance management system and related controls were not maintained as it did not describe and represent the processes of performance measurement and how it is conducted, organised and managed, as required by sections 38 of the Municipal Systems Act and regulation 7 of the Municipal planning and performance management regulations.

Budgets

42. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15/87(8) of the MFMA.

Financial statements, performance and annual reports

43. 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 of non-current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statement were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.
44. The oversight report, containing comments on the annual report, was not adopted by council within two months from the date on which the 2013/14 annual report was tabled, as required by section 129(1) of the MFMA.

Procurement and contract management

45. Quotations were not accepted from prospective providers who are not registered on the list of accredited prospective providers and did not meet the listing requirements prescribed by the SCM policy, in contravention of SCM regulation 16(b) and 17(b).
46. Invitations for competitive bidding were not always advertised for the minimum period of days, as required by SCM regulation 22(1) and 22(2).
47. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded only to bidders who submitted 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).

Consequence management

48. Unauthorised, irregular as well as fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person was liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.

Human resource management and compensation

49. Job descriptions were not established for all posts in which appointments were made in the current year, in contravention of section 66(1)(b) of Municipal Systems Act.
50. 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, regulation 14(2)(a).
51. The annual report of the municipality did not reflect information on compliance with prescribed minimum competencies as required by the Municipal regulations on minimum competency levels, regulation 14(2)(b)/14(3)

Expenditure management

52. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
53. 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.

Asset and liability management

54. Short-term debt was not repaid within the financial year, as required by section 45(4) of the MFMA.

Internal control

55. 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 on compliance with legislation included in this report.

Leadership

56. The accounting officer did not exercise oversight responsibility regarding compliance with laws and regulations and related internal controls due to the lack of a compliance evaluation system, which resulted in non-compliance, irregular expenditure as well as fruitless and wasteful expenditure.
57. There has been instability or vacancies in key positions due to resignations.
58. Management did not adequately monitor the implementation of action plans to address internal control deficiencies. This resulted in repeat findings being reported on compliance with laws and regulations.
59. There was a slow response to the message communicated by the AGSA to the administrative and political leadership.
60. Human resource management was not implemented to ensure that adequate and sufficiently skilled resources were in place and that performance was monitored.

Financial and performance management

61. The financial statements were not properly reviewed for completeness and accuracy prior to submission for auditing. This resulted in many findings relating to incorrect disclosure.

62. Management did not in all instances implement proper record keeping in a timely manner to ensure that complete, relevant and accurate information was accessible and available to support financial and performance reporting.
63. Management did not in all instances implement controls over daily and monthly processing and reconciling of transactions.

Governance

64. Management did not ensure that vacancies in the internal audit section were filled on time. The internal audit manager was acting and had two graduates reporting to him.
65. The audit committee did not evaluate and monitor the audit charter and annual audit plan as these were not approved on time.

OTHER REPORTS

Investigations

66. An investigation is been conducted by the Department of Corporative Governance and Traditional Affairs through the anti-corruption hotline. The investigation relates to allegations of irregularities in accepting kickbacks. The investigation was still ongoing and the report thereof was not ready at our reporting date.

AUDITOR-GENERAL

Bloemfontein

30 November 2014



AUDITOR - GENERAL
SOUTH AFRICA

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