

Report of the auditor-general to the Free State Legislature and the council on the Dihlabeng Local Municipality

Report on the financial statements

Introduction

1. I have audited the financial statements of Dihlabeng 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 appropriation 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 this 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 consolidated and separate 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 audit opinion.

Opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Dihlabeng 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

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

Irregular expenditure

8. As disclosed in note 53 to the financial statements, irregular expenditure of R25 094 237 (2014: R86 461 006) was incurred, which was mainly due to non-compliance with supply chain management requirements in respect of procurement transactions.

Going concern

9. As disclosed in note 49 to the financial statements, the municipality is experiencing financial difficulties as current liabilities exceed current assets, consumer debtors are not recovered timeously and the inability to settle accounts payable within an acceptable period. These conditions, along with other matters as set forth in note 49, indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern.

Material losses

10. As disclosed in note 23 to the financial statements, the municipality incurred a loss of 13,25% (2014: 7,41%) as a result of electricity distribution losses.

Material impairment

11. As disclosed in note 7 to the financial statements, a provision for impairment of debtors amounting to R530 625 336 (2014: R412 526 763) has been made with regard to irrecoverable receivables.

Restatement of corresponding figures

12. As disclosed in note 46 to the financial statements, the corresponding figures for 30 June 2014 have been restated as a result of errors discovered during the 2014-15 financial year in the financial statements of the municipality at, and for the year ended, 30 June 2014.

Additional matter

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

Unaudited disclosure notes

14. 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.

Supplementary explanations of budget variances presented outside the financial statements

15. The supplementary explanations of budget variances contained in the accounting officer's report, as referred to in note 55, do not form part of the financial statements. I have not audited these explanations and accordingly I do not express an opinion thereon.

Report on other legal and regulatory requirements

16. 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 key performance areas (KPA) 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

17. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected key performance area presented in the annual performance report of the municipality for the year ended 30 June 2015:
 - KPA 1: Accelerated service delivery and infrastructure development on pages x to x
18. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
19. 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 key performance areas. 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).
20. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
21. The material findings in respect of the selected key performance are as follows:

KPA 1: Accelerated service delivery and infrastructure development

Usefulness of reported performance information

22. The period or deadline for delivery of targets should be specified as required by the FMPPI. A total of 25% 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.

Additional matters

23. I draw attention to the following matters:

Achievement of planned targets

24. 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 of the reported performance information for the selected key performance area reported in paragraph 22 of this report.

Adjustment of material misstatements

25. I identified material misstatements in the annual performance report submitted for auditing on the reported performance information for KPA 1: accelerated service delivery and infrastructure development. As management subsequently corrected only some of the misstatements, I identified material findings on the usefulness of the reported performance information.

Compliance with legislation

26. 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

27. Measurable performance targets for the financial year were not set in the integrated development plan (IDP), for each of the key performance indicators and with regard to each of the development priorities or objectives, as required by section 41(1)(b) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) and the Municipal planning and performance management regulations 12(1) and 12(2)(e).
28. The service delivery and budget implementation plan (SDBIP) for implementing the municipality's delivery of municipal services and annual budget did not indicate:
- projections for each month of the revenue to be collected, by source and
 - the operational and capital expenditure, by vote, as required by section 1 of the MFMA.
29. 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 MSA and regulation 7 of the municipal planning and performance management regulations.

Financial statements and annual reports

30. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the Municipal Finance Management Act. Material misstatements of non-current assets, revenue and disclosure items identified by the auditors in the submitted financial statement were subsequently corrected or the supporting records were provided subsequently, resulting in the financial statements receiving an unqualified audit opinion.
31. The annual report and oversight report for the year 2013-14 was not filed with the provincial legislature within seven days after adoption of the oversight report by the council as required by MFMA 132 (1) and (2).
32. 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.

Audit committee

33. The audit committee did not advise the council on matters relating to internal financial control and internal audits on performance management as required by section 166(2)(a) of the MFMA.
34. The audit committee did not advise the council on matters relating to the adequacy, reliability and accuracy of financial reporting and information, as required by section 166(2)(a)(iv) of the Municipal Finance Management Act.
35. The audit committee did not advise the council on matters relating to compliance with legislation, as required by section 166(2)(a)(vii) of the MFMA.
36. The audit committee did not submit, at least twice during the financial year, an audit report on the review of the performance management system to the council, as required by Municipal planning and performance management regulation 14(4)(a)(iii).
37. The audit committee did not respond to the council on the issues raised in the audit reports of the Auditor-General, as required by section 166(2)(c) of the MFMA.
38. The audit committee did not review the municipality's performance management system and make recommendations to the council as required by Municipal planning and performance management regulation 14(4)(a)(ii).

Procurement and contract management

39. Quotations were accepted from prospective providers who are not registered on the list of accredited prospective providers and do not meet the listing requirements prescribed by the SCM policy in contravention of SCM regulation 16(b) and 17(b).

40. Awards were made to providers who are in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulations 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).
41. Persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM regulation 46(2)(e).

Human resource management and compensation

42. 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 the MSA.
43. The municipality did not timeously 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) .
44. The competencies of head of supply chain, financial and supply chain management officials were not assessed in a timely manner in order to identify and address gaps in competency levels as required by Municipal Regulations on Minimum Competency Levels 13.

Expenditure management

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

Conditional grants

47. 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.

Consequences management

48. Unauthorised, Irregular, Fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a)(ii) of the Municipal Finance Management Act.

Internal control

49. 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 opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

Leadership

50. The municipality did not continuously exercise its oversight responsibility regarding compliance and related internal controls due to the instability in key positions resulting in inadequate reviewing of the system of internal control.
51. Processes to prevent and detect unauthorised, irregular, fruitless and wasteful expenditure were not established. This was due to leadership not taking adequate action to address weaknesses identified.

Financial and performance management

52. Management did not in all instances implement proper record keeping in a timely manner to ensure that complete, relevant and accurate information is accessible and available to support financial and performance reporting.
53. The financial statements were not properly reviewed for completeness and accuracy prior to submission for auditing due to the instability in key positions and vacancies. This resulted in findings relating to incorrect disclosure and non-disclosure on property plant and equipment, investment property, revenue, commitments, and irregular expenditure which resulted in audit adjustments having to be passed on the financial statements initially submitted.

Governance

54. Management did not in all instances ensure that there is an adequate resourced and functioning internal audit unit as the function was outsourced and a majority of the vacancies in the unit were not filled at year end.

AUDITOR - GENERAL

Bloemfontein

30 November 2015



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence