

# **REPORT OF THE AUDITOR-GENERAL TO THE FREE STATE LEGISLATURE AND THE COUNCIL ON THE MASILONYANA LOCAL MUNICIPALITY**

## **REPORT ON THE FINANCIAL STATEMENTS**

### **Introduction**

1. I have audited the financial statements of the Masilonyana Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2012, 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 the financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP), 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, 2011 (Act No. 6 of 2011) (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 judgment, 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. I was unable to obtain sufficient appropriate audit evidence regarding property, plant and equipment, as the descriptions in the asset register differed from the actual assets. I was unable to confirm the physical assets and the value thereof by alternative means. Consequently, I was unable to determine if any adjustments related to property, plant and equipment stated as R505 271 936 (2011: R887 969 017) as disclosed in note 11 to the financial statements was necessary.

### **Qualified opinion**

7. In my opinion, except for the possible effect of the matter described in the Basis for qualified opinion paragraph, the financial statements present fairly, in all material respects, the financial position of the Masilonyana Local Municipality as at 30 June 2012 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**

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

### **Restatement of corresponding figures**

9. As disclosed in notes 29 and 30 to the financial statements, the corresponding figures for 30 June 2011 have been restated as a result of correcting prior year audit findings during the current financial year in the financial statements of the municipality at, and for the year ended, 30 June 2011.

### **Fruitless and wasteful expenditure**

10. As disclosed in note 34.2 to the financial statements, fruitless and wasteful expenditure of R1 202 546 was incurred on interest and penalties, due to the late payment of outstanding accounts.

### **Irregular expenditure**

11. As disclosed in note 34.3 to the financial statements, irregular expenditure of R133 071 845 was incurred, due to supply chain management requirements not adhered to.

### **Unauthorised expenditure**

12. As disclosed in note 34.1 to the financial statements, unauthorised expenditure of R553 676 848 was incurred, due to the overspending of the budget.

### **Material losses**

13. As disclosed in note 34.4 to the financial statements, material losses of R24 704 158 (2011: R23 538 870) were incurred, due to distribution losses in the water and electricity network.

### **Additional matter**

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

### **Unaudited supplementary schedules**

15. 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 schedules and accordingly I do not express an opinion thereon.

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

### **Predetermined objectives**

16. I am unable to report findings on the usefulness and reliability of Masilonyana Local Municipality as it was not presented as required by section 46 of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) and section 121(3)(c) of the MFMA.

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

17. 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:

#### **Strategic planning and performance management**

18. The municipality did not afford the local community at least 21 days to comment on the final draft of its IDP before the plan was submitted to the council for adoption, as required by regulation 15(3) of the Municipal Planning and Performance Management Regulations.
19. The municipality did not establish a performance management system, as required by section 38(a) of the MSA.

#### **Budget**

20. The municipality incurred expenditure in excess of the limits of the amounts provided for in the votes in the approved budget, in contravention of section 15 of the MFMA.
21. Sufficient and appropriate audit evidence could not be obtained that the mayor submitted all quarterly reports to the council on the implementation of the budget and the financial state of affairs of the municipality within 30 days after the end of each quarter, as required by section 52(d) of the MFMA.

#### **Annual financial statements and annual report**

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. Material misstatements in non-current assets, current assets as well as disclosure identified by the auditors were subsequently corrected, but the uncorrected material misstatements were included in the basis for the qualified of audit opinion paragraphs.
23. The accounting officer did not submit the financial statements for auditing within two months after the end of the financial year, as required by section 126(1)(a) of the MFMA.

#### **Audit committee**

24. An audit committee was not in place, as required by section 166(1) of the MFMA.

#### **Internal Audit**

25. The internal audit unit was not established, as required by section 165(1) of the MFMA.

### **Procurement and contract management**

26. Goods and services with a transaction value above R200 000 were procured without inviting competitive bids, as per the requirements of supply chain management (SCM) regulations 19(a).
27. Goods and services with a transaction value below R200 000 were procured without obtaining the required price quotations as required by SCM Regulation 17(a) and (c).
28. Sufficient appropriate audit evidence could not be obtained that bid specifications for procurement of goods and services through competitive bids were drafted in an unbiased manner that allowed all potential suppliers to offer their goods or services, as per required by SCM regulation 27(2)(a).
29. Sufficient appropriate 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).
30. Sufficient appropriate audit evidence could not be obtained that invitations for competitive bidding were advertised for a required minimum period of days, as required by SCM regulation 22(1) and 22(2).
31. Sufficient appropriate audit evidence could not be obtained that bids were evaluated by bid evaluation committees which were composed of officials from the departments requiring the goods or services and at least one SCM practitioner of the municipality as required by SCM regulation 28(2).
32. Sufficient appropriate audit evidence could not be obtained that bid adjudication was always done by committees which were composed in accordance with SCM regulation 29(2).
33. Sufficient appropriate audit evidence could not be obtained that the preference point system was applied in all procurement of goods and services above R30 000 as required by section 2(a) of the Preferential Procurement Policy Framework Act, 2000 (Act No. 5 of 2000)(PPPFA) and SCM regulation 28(1)(a).
34. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
35. The contract performance and monitoring measures and methods were insufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA.
36. 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).
37. Sufficient appropriate audit evidence could not be obtained that contract and quotations were only awarded to providers whose tax matters have been declared by the South African Revenue Service to be in order as required by SCM regulation 43.

### **Expenditure management**

38. Money owing by the municipality was not always paid within 30 days of receiving an invoice or statement, as required by section 65(2)(e) of the MFMA.
39. Sufficient appropriate audit evidence could not be obtained that payments had been approved by the accounting officer or a properly authorised official as required by section 11(1) of the MFMA.

40. An effective system of expenditure control, including procedures for the approval, authorisation, withdrawal and payment of funds, was not in place as required by section 65(2)(a) of the MFMA.
41. The accounting officer did not take reasonable steps to prevent unauthorised, fruitless and wasteful and irregular expenditure, as required by section 62(1)(d) of the MFMA.
42. Unauthorised, irregular and fruitless and wasteful expenditure was not recovered from the liable person, as required by section 32(2) of the MFMA.

#### **Revenue management**

43. A credit control and debt collection policy was not implemented, as required by section 96(b) of the MSA and section 62(1)(f)(iii) of MFMA.

#### **Asset management**

44. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.
45. An effective system of internal control for assets (including an asset register) was not in place, as required by section 63(2)(c) of the MFMA.

#### **Environmental**

46. The municipality operated two of their waste disposal sites without a waste management license or permit, in contravention of section 20(b) of the National Environmental Management: Waste Act, 2008 (Act No. 59 of 2008) and section 20(1) of the Environmental Conservation Act, 1989 (Act No. 73 of 1989).

#### **INTERNAL CONTROL**

47. I considered internal control relevant to my audit of the financial statements, 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 basis for qualified opinion, the findings on the performance report and the findings on compliance with laws and regulations included in this report.

#### **Leadership**

48. Management did not implement effective internal controls by ensuring proper records management, maintaining of an asset register and the preparing the annual financial statements, due to a lack of proper tone-at-the-top.
49. Leadership did not prioritise the establishment of a SCM directorate, which resulted in non-compliance with applicable legislation and gave rise to irregular expenditure.
50. Effective oversight was not done to confirm the implementation of adequate controls to ensure compliance with laws, regulations and internally designed policies and procedures.

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

51. Effective performance systems, processes and procedures as well as the management thereof had not been adequately developed and implemented due to other priorities set by management.

52. The annual financial statements contained numerous inaccuracies, which are attributable to weaknesses in the design and implementation of internal control in respect of financial management, financial reporting and information systems.

**Governance**

53. An audit committee, internal audit and performance audit committee were not in place for the financial year due to management not prioritising these matters.

*Auditor-General*  
Bloemfontein

28 March 2013



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*