

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

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Tokologo Local Municipality set out on pages ... to ... 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 and the statement of comparison of budget information with actual amounts 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 the 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 Division of Revenue Act of South Africa, 2013 (Act No. 2 of 2013) (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 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 qualified audit opinion.

Opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Tokologo Local Municipality as at 30 June 2014 and its financial performance and cash flows for the year then ended, in accordance with the 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:

Restatement of corresponding figures

8. As disclosed in note 42 to the financial statements, the corresponding figures for 30 June 2013 have been restated as a result of errors discovered during 2013-14 in the financial statements of the Tokologo Local Municipality at, and for the year ended, 30 June 2013.

Material impairments

9. As disclosed in note 4 to the financial statements, a provision for a decrease in value to the amount of R56 609 924 (89%) (2013: R54 724 980) (97%) was made with regard to amounts owing to the municipality in respect of services rendered by the municipality.

Material losses

10. As disclosed in note 49 to the financial statements, material losses to the extent of 32,58 % (2013: 17,00%) were incurred as a result of distribution losses incurred on electricity purchases. **(Ex.122)**

Significant uncertainty

11. With reference to note 40 to the financial statements, the municipality is the defendant various lawsuits. The municipality is opposing the claims. The ultimate outcome of the matter cannot presently be determined and no provision for any liability that may result has been made in the financial statements.

Financial sustainability / Going concern

12. Note 44 to the financial statements indicates that as at 30 June 2014 the municipality's current liabilities exceeded its current assets. This condition, along with other matters as set forth in the note indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern.

Unauthorised, irregular and fruitless and wasteful expenditure

13. As disclosed in notes 46, 48 and 47 to the financial statements respectively, the municipality incurred Unauthorised expenditure of R16 559 006 (2013: R38 587 715), irregular expenditure of R52 729 751 (2013: R47 582 909) and fruitless and wasteful expenditure of R1 225 697 (2013: R1 348 808) during the year under review, due to non-compliance with supply chain requirements.

Additional matter

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

Unaudited disclosure notes

15. 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

16. In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives for selected development priorities presented in the annual performance report, compliance with laws and regulations 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

17. 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 2014:
 - Municipal financial viability and management on pages XX to XX
 - Service delivery and infrastructure development on pages XX to XX
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 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).
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 development priorities are as follows:

Municipal financial viability and management

Usefulness of reported performance information

Measurability

22. Section 41(c) of the Municipal Systems Act requires the integrated development plan (IDP) to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 100% of the reported objectives were not consistent with those in the approved IDP. This was due to the fact that management was not aware of the requirements of the FMPPI (ex.62).
23. The FMPPI requires the following:
 - Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 40% (>20%) of the targets were not specific. (ex.113)
 - 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. (ex.111)

Reliability of reported performance information

24. The FMPPI requires that institutions should 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. The reported performance information was not valid, accurate and complete when compared to the source information or evidence provided. This was due to a lack of frequent review of the validity of reported achievements against source documentation. (ex.112)

Service delivery and infrastructure development

Usefulness of reported performance information

Measurability

25. Section 41(c) of the MSA requires the integrated development plan (IDP) to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 100% of the reported objectives were not consistent with those in the approved IDP. This was due to the fact that management was not aware of the requirements of the FMPPI (ex.160).
26. The FMPPI requires the following:
- Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 92% (>20%) of the targets were not specific. (Ex.172)
 - Performance targets must be measurable. I could not measure the required performance for 72% (>20%) of the targets. (ex.172)
 - The period or deadline for delivery of targets must be specified. A total of 33% (>20%) of the targets were not time bound. (ex.172)
 - 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. (ex.171, 172)

Reliability of reported performance information

27. The FMPPI requires that institutions should 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. The reported performance information was not valid, accurate and complete when compared to the source information or evidence provided. This was due to a lack of frequent review of the validity of reported achievements against source documentation. (ex.141)**Additional matter**

28. I draw attention to the following matter:

Achievement of planned targets

29. Refer to the annual performance report on pages **XX to XX** 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 objectives reported in paragraphs XX to XX of this report.

Compliance with laws and regulations

30. I performed procedures to obtain evidence that the municipality 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

31. The municipality did not give effect to its integrated development plan as required by section 36 of the MSA, section 21(2)(a) of the MFMA and Municipal planning and performance management regulation 6. **(ex.35)**.

32. The annual performance report for the year under review did not include the performance of the municipality and each external service provider and a comparison of the performance with set targets and a comparison with the previous financial year and measures taken to improve performance, as required by section 46 (1)(a), (b) and (c) of the MSA. **(ex.36)**
33. 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 MSA and the Municipal planning and performance management regulation 1 and 9(1)(a). **(ex.35 Audit comments)**

Annual financial statements, performance and annual reports

34. 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, current assets, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently resulting in the financial statements receiving an unqualified audit opinion.

Budget

35. 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 of the MFMA. **(ex.70)**

Audit committees

36. The audit committee did not advise the council or accounting officer on matters relating to compliance with legislation, as required by section 166(2)(a)(vii) of the MFMA. (ex.40)
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.(ex:13)
38. The audit committee did not review the quarterly internal audit reports on performance measurement, as required by Municipal planning and performance management regulation 14(4)(a)(i). (ex.39)
39. The audit committee did not review the municipality's performance management system or make recommendations to the council, as required by MPPMR 14(4)(a)(ii). (ex.41)
40. 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 MPPMR 14(4)(a)(iii). (ex.42)

Procurement and contract management

41. The prospective providers list for procuring goods and services through quotations was not updated at least quarterly to include new suppliers that qualify for listing, and prospective providers were not invited to apply for such listing at least once a year as per the requirements of SCM regulation 14(1)(a)(ii) and 14(2). (ex.142)
42. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulation 17(a) & (c). (ex.45)
43. 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). (ex.45)
44. 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. (ex.45)

Human resource management and compensation

45. 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 Regulations on Minimum Competency Levels reg14(2)(a).(ex:120)

Expenditure management

46. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA. (ex.51)
47. An effective system of expenditure control, including procedures for the approval of funds, was not in place, as required by section 65(2)(a) of the MFMA. (ex.25)
48. 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. (ex. 21, 45)

Revenue management

49. Interest was not charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA. (ex.165)

Asset management

50. 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. (ex.17, 18, 19, 61, 73, 74, 75, 76, 77, 78, 79, 80, 81, 82, 98, 115, 118, 119, 130, 134, 135, 140, 150, 151, 152, 153, 154, 167, 168)
51. 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. (ex.17, 75)

Consequences management

52. Unauthorised, Irregular and 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 MFMA. (ex.21, 45)

Internal control

53. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

54. Leadership did not always take timeous and adequate action to address weaknesses in internal control and vacancies in key positions in the finance and supply chain management component, which resulted in non-compliance with applicable legislation and gave rise to unauthorised, irregular expenditure and fruitless and wasteful expenditure..

Financial and performance management

55. Effective performance systems processes and procedures as well as the management thereof had not been adequately developed and implemented as a result of slow response to audit findings and a lack of capacity.

Governance

56. The audit committee did not promote accountability and service delivery through evaluating and monitoring responses to risks and providing oversight over the effectiveness of the internal control environment, including financial and performance reporting and compliance with laws and regulations.

Bloemfontein

30 November 2014



A U D I T O R - G E N E R A L
S O U T H A F R I C A

Auditing to build public confidence