

# **Report of the auditor-general to the Free State Legislature and the council on the Tokologo Local Municipality**

## **Report on the financial statements**

### **Introduction**

1. I have audited the financial statements of the Tokologo Local Municipality set out on pages x to x, 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 the statement of comparison of budget and 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 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 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 unqualified 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 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.

## **Restatement of corresponding figures**

8. As disclosed in note 42 to the financial statements, the corresponding figures for 30 June 2014 have been restated as a result of errors discovered during 2014-15 in the financial statements of the municipality at, and for the year ended, 30 June 2014.

## **Material impairment**

9. As disclosed in note 4 to the financial statements, provision for debt impairment to the amount of R 70 789 856 (2014: R 56 609 924) has been made with regards to consumer debtors amounting to R 74 964 497 (2014: R 63 485 989).

## **Material losses**

10. As disclosed in note 49 to the financial statements, material electricity losses to the extent of 49% (2014: 33%) were incurred as a result of distribution losses as a result of line losses, theft and vandalism.

## **Going concern**

11. Note 44 to the financial statements indicates that the municipality incurred a net deficit of R 18 057 667 during the year ended 30 June 2015 and, as of that date, the municipality's current liabilities exceeded its current assets by R17 628 412. These conditions, along with other matters as set out in the note 44, indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern.

## **Irregular expenditure**

12. As disclosed in note 48 to the financial statements, the municipality incurred irregular expenditure of R 20 598 865 (2014: R10 300 938) during the year under review. This was mainly due to non-compliance with supply chain management requirements.

## **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.

## Report on other legal and regulatory requirements

15. 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 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

16. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected key performance areas presented in the annual performance report of the municipality for the year ended 30 June 2015:
- Key performance area 2: Service delivery and infrastructure development on pages x to x
  - Key performance area 5: Financial viability and management on pages x to x
17. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
18. 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).
19. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
20. The material findings in respect of the key performance areas are as follows:

## **Key Performance area 2: Service delivery and infrastructure development**

### Usefulness of reported performance information

21. Section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) requires the integrated development plan (IDP) and the service delivery agreement to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 91% of the reported objectives were not consistent with those in the approved IDP. A total of 100% of the reported indicators/measures were not consistent with those in the approved service delivery agreements. A total of 96% of the reported targets were not consistent with those in the approved service delivery agreements. This was as a result of a lack of oversight from management in ensuring that the service delivery agreement, IDP and the annual performance reports correlates to one another.
22. The FMPPI requires that 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 50% of the indicators were not well defined.
23. The period or deadline for delivery of targets should be specified as required by the FMPPI. A total of 35% of the targets were not time bound.

The above was due to a lack of proper systems and processes for predetermined objectives.

### 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.

## **Key performance area 5: Financial viability and management**

### Usefulness of reported performance information

25. Section 41(c) of the MSA requires the 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 95% of the reported objectives were not consistent with those in the approved IDP. A total of 90% of the reported indicators/measures were not consistent with those in the approved service delivery documents. A total of 75% of the reported targets were not consistent with those in the approved service delivery agreements. This was due to a lack of frequent review of the validity of reported achievements against source documentation.
26. Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 25% of the targets were not measurable.

27. 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 45% of the indicators were not well defined.
28. The period or deadline for delivery of targets should be specified as required by the FMPPI. A total of 35% of the targets were not time bound.

The above was due to a lack of proper systems and processes for predetermined objectives.

### Reliability of reported performance information

29. The FMPPI requires auditees to 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. Significantly important targets were not reliable when compared to the source information or evidence. This was due to a lack of frequent review of the validity of reported achievements against source documentation.

### Additional matter

30. I draw attention to the following matter:

#### Achievement of planned targets

31. Refer to the annual performance report on page x to x; x for information on the achievement of planned targets for the year. This information should be considered in the context of the material findings on usefulness and reliability of the reported performance information for the selected key performance areas in paragraph 24 to 32 of this report.

### Compliance with legislation

32. 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:

### Annual financial statements

33. 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 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.

### Audit committees

34. 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).

## **Procurement and contract management**

- 35. 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) and (c).
- 36. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).
- 37. Invitations for competitive bidding were not always advertised for a required minimum period of days, as required by SCM regulation 22(1) and 22(2).
- 38. Contracts were awarded to bidders who did not submit 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).

## **Human resource management and compensation**

- 39. The competencies of 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 the Municipal Regulations on Minimum Competency Levels reg 13.

## **Expenditure management**

- 40. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
- 41. 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 management**

- 42. 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.
- 43. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

## **Consequences management**

- 44. Unauthorised, 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.

## **Internal control**

- 45. 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 the findings on compliance with legislation included in this report.

## Leadership

46. Leadership did not always take prompt and adequate action to address weaknesses in internal control which resulted in non-compliance with applicable legislation and gave rise to unauthorised, irregular expenditure and fruitless and wasteful expenditure

## Financial and performance management

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

## Governance

48. The audit committee did not promote effective oversight by ensuring consequences for transgressing legal requirements as well as advising council on the implementation of a functional performance management system.

*Auditor General.*  
Bloemfontein

30 November 2015



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*