

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

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Letsemeng 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) 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, 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 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.

Basis for qualified opinion

Revenue

6. I was unable to obtain sufficient appropriate audit evidence as to the completeness, and accuracy of property rates to the amount of R5 350 022 (2011: R4 247 417) as disclosed in note 25 to the financial statements due to inadequate revenue reconciliations. I was unable to confirm the property rates by alternative means. Consequently, I was unable to determine whether any adjustments to property rates were necessary.

7. I was unable to obtain sufficient appropriate audit evidence as to the completeness, and accuracy of service charges to the amount of R24 542 385 (2011: R23 053 266) as disclosed in note 23 to the financial statements due to free basic services subsidy not applied in line with the indigent policy. I was unable to confirm the service charges by alternative means. Consequently, I was unable to determine whether any adjustments to service charges were necessary.

Expenditure

8. I was unable to obtain sufficient appropriate audit evidence on employee related cost of R24 513 913 (2011: R21 679 835), as disclosed in the statement of financial performance and note 31 to the financial statements. The municipality's records and information available did not permit the application of alternative procedures. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments to employee related cost were necessary.
9. I was unable to obtain sufficient appropriate audit evidence as to the accuracy and occurrence of repairs and maintenance to the amount of R4 716 889 (2011: R3 144 893), as disclosed in the statement of financial performance. I was unable to confirm the repairs and maintenance by alternative means. Consequently, I was unable to determine whether any adjustments to repairs and maintenance were necessary.
10. I was unable to obtain sufficient appropriate audit evidence as to the completeness and accuracy of other expenses to the amount of R21 392 665 (2011: R16 250 434), as disclosed in the statement of financial performance and note 37 to the financial statements. I was unable to confirm the other expenses by alternative means. Consequently, I was unable to determine whether any further adjustments to other expenses were necessary.

Trade and other payables from exchange transactions

11. The municipality did not have an effective system of control for trade and other payables from exchange transactions and as a result I was unable to obtain sufficient appropriate audit evidence as to the completeness, existence, valuation and allocation of, as well as the municipality's obligations to trade and other payables from exchange transactions to the amount of R12 821 642 (2011: R5 108 833) as disclosed in note 20 to the financial statements. I was unable to confirm the amount disclosed by alternative means. Consequently, I was unable to determine whether any further adjustments to trade and other payables from exchange transactions were necessary.

Irregular expenditure

12. I was unable to obtain sufficient appropriate audit evidence that management has properly identified, investigated and recorded all irregular expenditure during the current and prior year. Due to the limitations placed on my audit of expenditure and procurement management at the municipality and the lack of a proper system in place to account for and identify irregular expenditure, there were no satisfactory alternative audit procedures that I could perform to confirm the completeness of irregular expenditure of R40 953 956 (2011: R37 653 805), as disclosed in note 48 to the financial statements.

Qualified opinion

13. In my opinion, except for the possible effects of the matters described in the Basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Letsemeng 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 matter

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

Restatement of corresponding figures

15. As disclosed in note 42 and 43 to the financial statements, the corresponding figures for 30 June 2011 have been restated as a result of errors identified during 2011-12 in the financial statements of the Letsemeng Local Municipality at, and for the year ended 30 June 2011.

Additional matter

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

Unaudited supplementary information

17. 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

18. In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

19. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages XX to XX of the annual report.

20. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned development objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the *National Treasury Framework for managing programme performance information*.

The reliability of the information in respect of the selected development objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).

21. The material findings are as follows:

Usefulness of information

22. Section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) requires that the integrated development plan (IDP) should form the basis for the annual performance report, therefore requiring the consistency of objectives, indicators and targets between planning and reporting documents. A total of 85% (>20%) of the reported indicators and 79% (>20%) of the reported targets are not consistent with the objectives, indicators and targets as per the approved IDP. This is due to the lack of review procedures in place to ensure that the IDP and annual performance report is aligned.

23. The National Treasury *Framework for managing programme performance information (FMPPi)* requires that performance targets be specific in clearly identifying the nature and required level of performance. A total of 67% (>20%) of the targets of the selected program were not specific in clearly identifying the nature and the required level of performance. This was due to the fact that management was aware of the requirements of the *FMPPi* but did not receive the necessary training to enable application of the principles.
24. The National Treasury *Framework for managing programme performance information (FMPPi)* requires that performance targets be measurable. The required performance could not be measured for a total of 67% (>20%) for the targets of the selected program. This was due to the fact that management was aware of the requirements of the *FMPPi* but did not receive the necessary training to enable application of the principles.
25. The National Treasury *Framework for managing programme performance information (FMPPi)* requires that indicators should have clear, unambiguous data definitions so that data is collected consistently and is easy to understand and use. A total of 89% (>20%) for the indicators of the selected program were not well defined in that clear, unambiguous data definitions were not available to allow for data to be collected consistently. This was due to the fact that management was aware of the requirements of the *FMPPi* but did not receive the necessary training to enable application of the principles.
26. The National Treasury *Framework for managing programme performance information (FMPPi)* requires that it must be possible to validate the processes and systems that produce the indicator. A total of 89% (>20%) for the indicators of the selected program were not verifiable in that valid processes and systems that produce the information on actual performance did not exist. This was due to the fact that management was aware of the requirements of the *FMPPi* but did not receive the necessary training to enable application of the principles.

Compliance with laws and regulations

27. 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:

Annual financial statements, performance and annual reports

28. The accounting officer did not make the 2010-11 annual report public immediately after the annual report was tabled in the council, as required by section 127(5)(a) of the MFMA.
29. The council did not adopt in good time, a process set out in writing to guide the planning, drafting, adoption and review of its IDP, as required by section 28(1) of the MSA.
30. The municipality did not establish a performance management system, as required by section 38(a) of the MSA.

Revenue management

31. A tariff policy on the levying of fees for municipal services provided by the municipality was not implemented, as required by section 74(1) of the MSA and section 62(1)(f)(i) of MFMA.
32. 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.
33. A policy on the levying of rates on rateable property within the municipality was not implemented, as required by section 3(1) of the Local Government: Municipal Property Rates Act, 2004 (Act No.6 of 2004) and section 62(1)(f)(ii) of MFMA.
34. Sufficient audit evidence could not be obtained that revenue had been reconciled on a weekly basis, as required by 64(2)(h) of the MFMA.

Expenditure management

35. The accounting officer did not take reasonable steps to prevent unauthorised, irregular and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.
36. Unauthorised, irregular, and fruitless and wasteful expenditure was not recovered from the liable person, as required by section 32(2) of the MFMA.

Liability management

37. An effective system of internal control for liabilities (including a liability register) was not in place, as required by section 63(2)(c) of the MFMA.

HR Management

38. Sufficient appropriate audit evidence could not be obtained that appointments were only made in posts which were provided for in the approved staff establishment of the municipality, as required by section 66(3) of MSA.
39. 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 MSA.
40. Sufficient appropriate audit evidence could not be obtained that the appointment of senior managers directly accountable to the municipal manager were approved by municipal council as required by 56(1)(a) of MSA.

Financial misconduct

41. Investigations were not instituted into all allegations of financial misconduct against officials of the municipality, as required by section 171(4)(a) of the MFMA due to the fact that irregular and fruitless and wasteful expenditure was incurred but not investigated.

Waste management legislation

42. The municipality operated some 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

43. 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

44. The leadership did not evaluate whether management had implemented effective internal controls. They did not gain a comprehensive understanding of how senior management members had met their responsibilities in terms of ensuring proper record management in respect of preparing the annual financial statements.
45. The leadership of the municipality neglected to develop, implement and monitor internal control procedures to ensure that quarterly financial statements are prepared and subjected to review. This oversight resulted in the challenges faced to submit financial statements to audit that are fully compliant to the SA Standards of GRAP and necessitated the amendment of financial statements provided for audit purposes.
46. The leadership failed to implement adequate controls to ensure compliance with laws, regulations and internally designed policies and procedures. As a result, significant non-compliance issues were noted.

Financial and performance management

47. Effective performance systems, processes and procedures as well as the management thereof had not been adequately developed and implemented.
48. Due to oversight on the part of the accounting officer, the regular review and monitoring of compliance to laws and regulations were not sufficiently prioritised in the municipality. As a result, significant non-compliance issues were noted that could have been prevented.
49. The staff within the finance directorate of the municipality lacked the appropriate skill and competence and this necessitated the municipality to make use of consultants to supplement such constraints. Consultants assisted with the preparation of an asset register and the preparation of the financial statements.
50. Due to time pressure brought about by the fact that the process of preparing the financial statements were only started late in the financial year, when appointment of the consultants were finalised sufficient time was not available to the chief financial officer to properly review such statements for completeness and accuracy prior to submission thereof for auditing. This resulted in many findings relating to incorrect disclosure which were subsequently corrected.
51. Staff within the finance directorate of the municipality had an insufficient understanding of the accounting framework. This contributed towards the numerous errors that were subsequently corrected in the financial statements of the municipality.

Governance

52. The internal audit unit was not sufficiently staffed and effective during the year.

OTHER REPORTS

53. Investigations are being conducted by South African Police Services on request of the municipality. The investigations were initiated based on allegations of prepaid electricity expenditure. The investigations were still in progress at the reporting date.

Auditor - General

Bloemfontein

30 November 2012



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence