

**REPORT OF THE AUDITOR-GENERAL TO THE EASTERN CAPE PROVINCIAL  
LEGISLATURE AND THE COUNCIL ON THE UMZIMVUBU LOCAL MUNICIPALITY  
REPORT ON THE FINANCIAL STATEMENTS**

**Introduction**

1. I have audited the accompanying financial statements of the Umzimvubu Local Municipality, which comprise the statement of financial position as at 30 June 2011, and the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information as set out on pages XX to XX

**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 (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, 2010 (Act No.1 of 2010 as amended) (DoRA), as well as for such internal control as management determines 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. As required by section 188 of the Constitution of the Republic of South Africa, 1996 (Act No. 108 of 1996) and section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with International Standards on Auditing and *General notice 1111 of 2010* issued in *Government Gazette 33872 of 15 December 2010*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance that the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence for 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.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

**Opinion**

7. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Umzimvubu Local Municipality as at 30 June 2011, and its financial performance and cash flows for the year then ended in accordance with 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:

### **Significant uncertainties**

9. With reference to note 40 to the financial statements, contingent liabilities of R27 790 500 are disclosed as the municipality is the defendant in ongoing court proceedings. The ultimate outcome of the matters disclosed cannot presently be determined, and no provision for any liability that may result has been made in the financial statements.

### **Restatement of comparative figures**

10. As disclosed in note 29 to the financial statements, the comparative figures for 30 June 2010 have been restated. The restatement resulted from errors that have been discovered during the financial year ended 30 June 2011 in the financial statements of the municipality at, and for the year ended, 30 June 2010.

### **Unauthorised Expenditure**

11. The municipality incurred unauthorised expenditure of R 33 463 126 as a result of exceeding the total amount of the VOTE, as disclosed in note 32 of the annual financial statements.

### **Material Impairments**

12. In note 3 of annual financial statements the municipality has disclosed an impairment loss amounting to R5 727 567 (2010: R 3 626 829).The impairment results from debtor balances which are not recoverable as at 30 June 2011.

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

13. In accordance with the PAA and in terms of *General notice 1111 of 2010*, issued in *Government Gazette 33872 of 15 December 2010*, I include below my findings on the annual performance report as set out on pages ... to ... and material non-compliance with laws and regulations applicable to the municipality.

## **PREDETERMINED OBJECTIVES**

### **Presentation of information**

14. The following criterion is relevant to the finding below:

- Performance against predetermined objectives is reported using the National Treasury guidelines.

Audit finding

15. **Strategic objectives were not recorded on the annual performance report**

- The annual performance report submitted for audit purposes did not reflect any strategic objectives as required by the National Treasury guidelines.

### **Usefulness of information**

16. The following criteria are relevant to the findings below:

- Consistency: Objectives, indicators and targets are consistent between planning and reporting documents.

- Relevance: A clear and logical link exists between the objectives, outcomes, outputs, indicators and performance targets.
- Measurability: Indicators are well defined and/or verifiable, and targets are specific, and/or measurable and/or time bound.

#### Audit findings

#### 17. **Reported objectives and indicators are not complete when compared with the planned objectives and indicators**

The indicators relating to the budget and treasury programme, citizens and community services programme and infrastructure and planning programme were not completely reported on the annual performance report.

- For budget and treasury, 21% of indicators were not reported.
- For citizens and community services, 63% of indicators were not reported.
- For infrastructure and planning, 93% of indicators were not reported.

#### 18. **Annual performance report not complete**

- Twenty-six per cent of the planned and reported targets for programme 6: Department of Citizens and Community were not reported on in the annual performance report.

### **COMPLIANCE WITH LAWS AND REGULATIONS**

19. Included below are findings on material non-compliance with laws and regulations applicable to the municipality.

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

20. The accounting officer of the municipality did not, by 25 January, assess the performance of the municipality during the first half of the financial year, taking into account the municipality's service delivery performance during the first half of the financial year and the service delivery targets and performance indicators set in the service delivery and budget implementation plan, as required by section 72(1) (a)(ii) of the MFMA.

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

21. 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 capital assets, current assets and disclosure items identified by the auditors were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.

#### **Internal audit**

22. Internal audit did not report to the audit committee on matters relating to compliance with the MFMA, DoRA and other applicable legislation as required by section 165(2)(b) of the MFMA.

#### **Procurement and contract management**

23. The contract performance measures and methods whereby they are monitored were insufficient to ensure effective contract management, as per the requirements of section 116(2)(c) of the MFMA.

24. Awards were made to providers who are persons in service of the municipality, in contravention of SCM regulation 44. Furthermore, the providers failed to declare that he/she was in the service of the municipality, as required by SCM regulation 13(c).
25. Awards were made to providers who are persons in service of other state institutions, in contravention of the requirements of SCM regulation 44. Furthermore, the provider failed to declare that he/she is in the service of the state, as required by SCM regulation 13(c).
26. Persons in service of the municipality who 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).

#### **Expenditure management**

27. The accounting officer did not take reasonable steps to prevent unauthorised and irregular expenditure, as required by section 62(1)(d) of the MFMA.

#### **Revenue management**

28. Interest was not charged on all arrears accounts, as required by section 64(2)(g) of the MFMA.
29. Revenue received by the municipality was not always reconciled at least on a weekly basis, as required by section 64(2)(h) of the MFMA.
30. A credit control and debt collection policy was not implemented, as required by section 96(b) of the MSA.
31. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained a management, accounting and information system which accounted for debtors, as required by section 64(2)(e) of the MFMA.

#### **Asset management**

32. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained a management, accounting and information system which accounts for the assets of the municipality, as required by section 63(2)(a) of the MFMA.
33. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained an effective system of internal control for assets (including an asset register), as required by section 63(2)(c) of the MFMA.

#### **INTERNAL CONTROL**

34. In accordance with the PAA and in terms of *General notice 1111 of 2010*, issued in *Government Gazette 33872 of 15 December 2010*, I considered internal control relevant to my audit, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters reported below are limited to the significant deficiencies that resulted in the material audit adjustments, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

## **Leadership**

35. The accounting officer did not exercise oversight responsibilities regarding the financial-related controls, as evidenced by material misstatements in the transactions, balances, and disclosure line items that were identified during the audit process, that were subsequently adjusted by management. The accounting officer also did not have adequate monitoring controls to ensure adherence to the internal policies and procedures on performance reporting, resulting in significant control deficiencies identified during the audit process in the reporting and presentation of predetermined objectives.
36. Furthermore, the accounting officer's exercise of oversight over adherence to the SCM regulations was not effective, evidenced by non-adherence to SCM regulations identified during the audit process that resulted in irregular expenditure.

## **Financial and performance management**

37. The financial statements and report on predetermined objectives that were submitted for audit purposes contained misstatements and errors. This was mainly due to municipality staff not performing and implementing daily financial reporting controls throughout the financial year, including the daily processing of transactions, monthly reconciliations of accounting records, preparing monthly financial statements and service delivery reports. The monitoring of controls was not adequate to ensure that all transactions were accounted for accurately and completely.
38. Policies and procedures that will ensure that all transactions are accounted for, in terms of GRAP requirements, were not developed and communicated to staff members. As a result, there were material misstatements and errors not accounted for, in terms of GRAP, that were identified during the audit process.
39. Furthermore, established internal control practices were not effective as they did not detect or prevent non-compliance with laws and regulations that was identified during the audit process, resulting in the municipality incurring irregular expenditure.

## **Governance**

40. The municipality has an audit committee that promotes 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, and that has performed its work with due care and as per requirements of the MFMA. Furthermore, they have discharged their responsibilities as required by the MFMA.

41. However, audit committee interventions or mechanisms used were not appropriate and sufficient as they could not prevent and detect significant control deficiencies in the municipal internal control system, as evidenced by material misstatements that were identified during the audit process and subsequently corrected by management, weaknesses identified in reporting of predetermined objectives and non-compliance with SCM regulations. Furthermore, internal audit did not adequately monitor the implementation of its recommendations by management.

Auditor-General

East London

30 November 2011



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*