Auditing to build public confidence

AUDITOR-GENERAL
SOUTH AFRICA

FINAL MANAGEMENT REPORT

KAROO HOOGLAND LOCAL MUNICIPALITY

30 June 2017

Communicated to the accounting officer on: 30 November 2017

MANAGEMENT REPORT

KAROO HOOGLAND LOCAL MUNICIPALITY

30 June 2017

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MANAGEMENT REPORT TO THE ACCOUNTING OFFICER ON THE AUDIT OF THE KAROO HOOGLAND LOCAL MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2017

INTRODUCTION

1. The purpose of the management report is to communicate audit findings and other key audit observations to the accounting officer and does not constitute public information. This management report includes audit findings arising from the audit of the financial statements, performance information and compliance with legislation for the year ended 30 June 2017.

2. These findings were communicated to management and the report details management's response to these findings. The report includes information on the internal control deficiencies that we identified as the root causes of the matters reported. Addressing these deficiencies will help to improve the audit outcome.

3. In accordance with the terms of engagement, our responsibility in this regard is to:

   - express an opinion on the financial statements
   - express a conclusion in the management report on the usefulness and reliability of the reported performance information for selected development priorities, and report the material findings in the auditor's report
   - report on material findings raised on compliance with specific requirements in key applicable legislation, as set out in the general notice issued in terms of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA).

   Our engagement letter sets out our responsibilities and those of the accounting officer in detail.

4. This management report consists of the overall message arising from the audit, summary of key findings and observations, annexures containing the detailed audit findings, annexures to the report on the audit of performance information as well as the annexure to internal control deficiencies reported.

5. The auditor's report is finalised only after the management report has been communicated. All matters included in this report that relate to the auditor's report remain in draft form until the final auditor's report is signed. In adherence to section 50 of the PAA, we do not disclose any information obtained during the audit and contained in this management report.

6. This management report consists of the overall message arising from the audit, summary of key findings and observations, annexures containing the detailed audit findings, annexures to the report on the audit of performance information as well as the annexure to internal control deficiencies reported.

7. The auditor's report is finalised only after the management report has been communicated. All matters included in this report that relate to the auditor's report remain in draft form until the final auditor's report is signed. In adherence to section 50 of the PAA, we do not disclose any information obtained during the audit and contained in this management report.

8. The **figure** that follows provides a pictorial summary of the audit results and our key messages on how to improve the audit outcomes with the focus on the following:

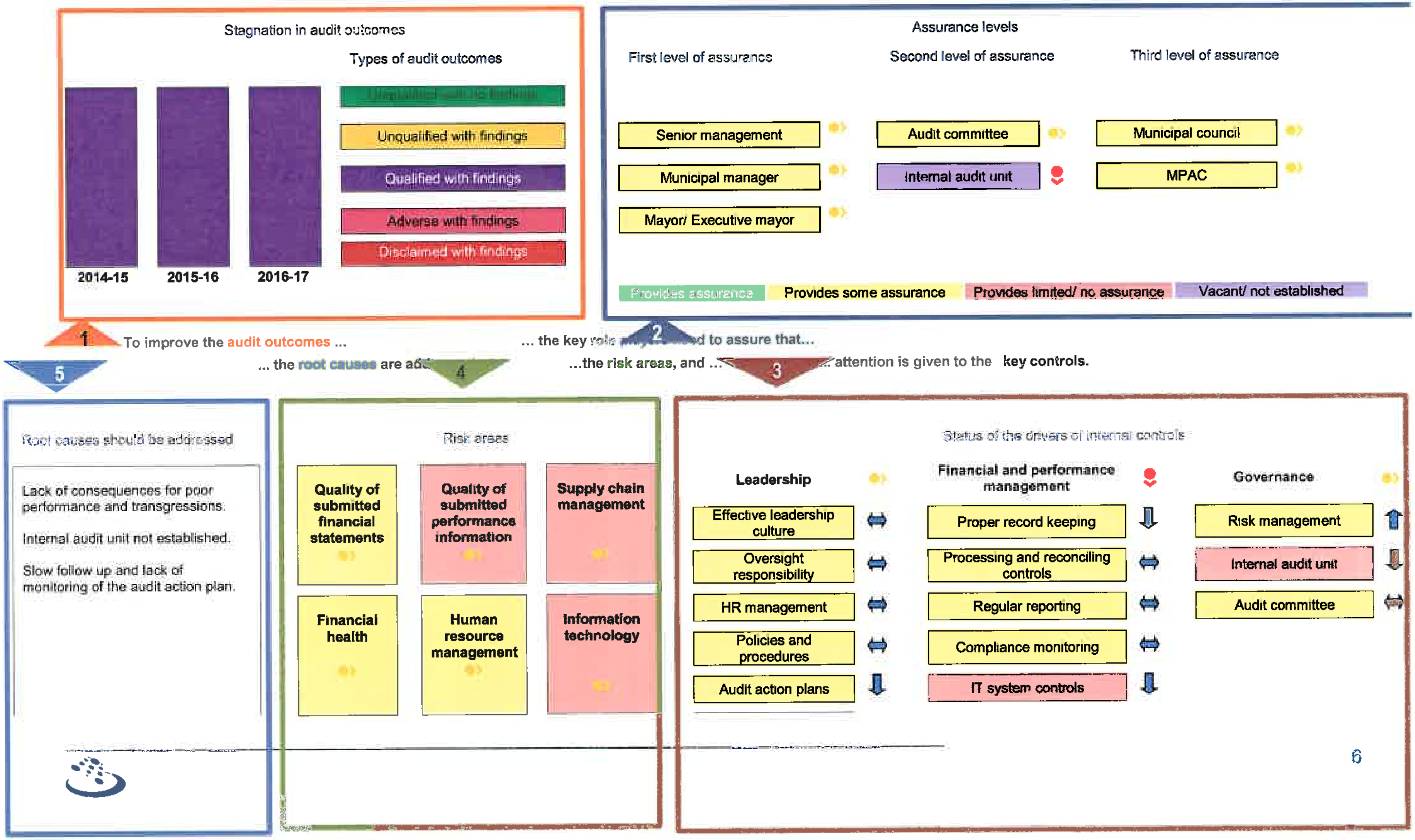
   - Status of the audit outcomes
   - Status of the level of assurance provided by key role players
   - Status of the drivers of internal controls
   - Status of risk areas
   - Root causes to be addressed

The tick mark or legends on the figure mean the following:

/ ⇧ Improved

/ ⇔ Unchanged/slight improvement/slight regression

/ ⇩ Regressed


Stagnation in audit outcomes
Types of audit outcomes
Unqualified with no findings
Unqualified with findings
Qualified with findings
Adverse with findings
Disclaimed with findings
2014-15
2015-16
2016-17
Assurance levels
First level of assurance
Second level of assurance
Third level of assurance
Senior management
Municipal manager
Mayor/ Executive mayor
Audit committee
Internal audit unit
Municipal council
MPAC
Provides assurance
Provides some assurance
Provides limited/ no assurance
Vacant/ not established
1
To improve the audit outcomes ...
2
... the key role
d to assure that...
5
... the root causes are ad
4
...the risk areas, and ...
3
attention is given to the key controls.
Root causes should be addressed
Lack of consequences for poor performance and transgressions.
Internal audit unit not established.
Slow follow up and lack of monitoring of the audit action plan.
Risk areas
Quality of submitted financial statements
Quality of submitted performance information
Supply chain management
Financial health
Human resource management
Information technology
Status of the drivers of internal controls
Leadership
Effective leadership culture
Oversight responsibility
HR management
Policies and procedures
Audit action plans
Financial and performance management
Proper record keeping
Processing and reconciling controls
Regular reporting
Compliance monitoring
IT system controls
Governance
Risk management
Internal audit unit
Audit committee

				IT governance			
	Good	Concerning	Intervention required	Good	Concerning	Intervention required	

OVERALL MESSAGE

9. Karoo Hoogland Local Municipality has maintained a qualified opinion with findings.

10. Management submitted financial statements that were not prepared in accordance with the prescribed financial reporting framework, financial statements contained material misstatements in property, plant and equipment, work-in-progress, commitments, employee costs, provisions, accruals and expenditure. Some material statements have not been corrected resulting in the financial statements receiving a qualified audit opinion.

11. The review of quarterly financial statements was not adequate as it did not detect potential areas of misstatements in the financial statements, and as a result, misstatements were not addressed timeously.

12. The financial health of the municipality is concerning as the entity is in a net current liability position with adverse ratios for debtor's collections period and creditor's payment period. Its current liabilities exceeded its current assets by R 1 923 521. The entity has made appropriate disclosure in the annual financial statements of these events or conditions on the municipality's ability to continue as a going concern and the measures in place to mitigate these. The Municipality continues to implement measures to improve on collections for outstanding debts and obtains funding from National Treasury.

13. Management did not implement internal controls designed for the appropriate monitoring of compliance with laws and regulations resulting in repeat findings of non-compliance in the current year.

14. The municipality does not have a performance management system in place. No polices were developed and implemented to govern performance management.

SECTION 1: Interactions with stakeholders responsible for oversight and governance

15. During the audit cycle, we met with the following key stakeholders responsible for oversight and governance to communicate matters relating to the audit outcome of the municipality:

Key stakeholder	Purpose of interaction	Number of interactions
Mayor	Roll out of audit outcome for 15/16 and discussion of audit progress	1
Municipal manager	Provide status update on the audit; discuss audit findings and status of requests for information.	3
Audit committee	Present Audit Strategy document for the 2016/17 financial year audit, discuss draft annual financial statements and annual performance report and obtain a status update on the operations of the municipality.	1

16. At these interactions, we shared the following key matters affecting audit outcomes and the auditee:

- Significant risks identified during audit planning and our planned response to these risks
- Key focus areas
- Challenges regarding the audit of performance information as there is no performance management system in place.
- Absence on internal audit
- Audit progress
- Audit findings raised, including misstatements identified during the audit process
- Concerns of management and the auditors

17. All stakeholders made commitments to implement initiatives that can improve the audit outcome. The commitments given and the progress of previous commitments are included in section 3.2, which deals with the assessment of assurance providers.

SECTION 2: Matters relating to the auditor's report

2.1 AUDIT OF THE FINANCIAL STATEMENTS

18. We identified material misstatements in the financial statements during the audit. These misstatements were not prevented or detected by the municipality's system of internal control. These material misstatements also constitute non-compliance with section 122 of the Municipal Finance Management Act (MFMA).

19. The misstatements that were not corrected form the basis for the qualified opinion on the financial statements.

Material misstatement			Impact	Impact
Financial statement item	**Finding**	**Occurred in prior year** (Insert Yes/No)	**R** current year	**R** previous year
Material misstatements not corrected				
Property, plant and equipment				
	PPE: Land registered in the name of the Municipality that was not included in the asset register.	No	Unknown	0
	PPE: Land not registered in the name of the municipality that was recorded in the asset register	No	Unknown	0
Disclosures				
Commitments	Limitation of scope- contracts not provided for audit	No	Unknown	0
Material misstatements corrected				
Non-current assets				
Property, plant and equipment	**Misclassification of property plant and equipment**			
	DR Community assets	No	2 493 570	0

Material misstatement			Impact	Impact
Financial statement item	**Finding**	**Occurred in prior year (Insert Yes/No)**	**R current year**	**R previous year**
	CR Land and buildings	No	(2 493 570)	0
Property, plant and equipment	PPE: Failure to disclose projects on hold in notes to the financial statements	No	3 091 728	0
Work-in-Progress	**Work-in-progress not separately disclosed**			
	DR Infrastructure assets	No	7 111 434	0
	CR Work-in-progress	No	(7 111 434)	0
Current assets				
Receivables	Allowance for impairment note does not cast	No	3 338 503	No
Current liabilities				
Provisions	**Incorrect classification of leave accrual**			
	Dr Provisions	No	1 270 075	892 196
	Cr Payables – Leave accrual	No	(1 270 075)	(892 196)
Expenditure				
Repairs and maintenance	**Incorrect classification of expenses**			
	DR Inventory	No	3 181 587	0
	Prepayments	No	46 540	0
	General expenses	No	23 736	0
	Intangible assets	No	106 065	0
	CR Repairs and maintenance	No	(3 357 928)	0
Disclosures				
Irregular expenditure	Irregular expenditure not disclosed	No	5 191 981	0

2.2 MATTERS TO BE BROUGHT TO THE ATTENTION OF USERS

Emphasis of matter paragraphs

20. The following emphasis of matter paragraphs will be included in our auditor's report to draw the users' attention to matters presented or disclosed in the financial statements:

Restatement of corresponding figures

21. As disclosed in note 38 to the financial statements, the corresponding figures for 30 June 2016 have been restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2017.

Material losses

22. As disclosed in note 31 to the financial statements, material losses to the amount of R4 544 683 (2016: R2 417 304) were incurred as a result of write off and impairment of trade receivables.

23. As disclosed in note 44 to the financial statements, material electricity losses to the extent of 15.72% (2016: 16.76%) were incurred as a result of technical losses, faulty meters, and illegal connections.

Other matter paragraphs

24. The following other matter paragraphs will be included in our auditor's report to draw the users' attention to matters regarding the audit, the auditor's responsibilities and the auditor's report:

Unaudited disclosure notes

25. 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."

Unaudited supplementary schedules

26. 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.

2.3 AUDIT OF THE ANNUAL PERFORMANCE REPORT

27. In terms of the AG directive the opinion on the audit of reported information will be included in the management report. The report is included below to enable management and those charged with governance to see what the report will look like once it is published in the auditor's report. I will report all the audit findings included under the basis for opinion and the other matter sections of this report in the auditor's report.

Introduction and scope

28. I was engaged to undertake a reasonable assurance engagement on 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 2017:

Development priorities	Pages in annual performance report	Opinion	Movement
KPA 1 – Basic Service Delivery	30 – 37	Disclaimer of opinion	
KPA 2 – Local Economic Development	30 – 37	Disclaimer of opinion	

KPA 1 – Basic Services Delivery

Disclaimer of opinion

29. I do not express an opinion on the reported performance information for KPA 1 – Basic Services Delivery of the municipality. Because of the significance of the matters described in the basis for disclaimer of opinion section of my report, I have not been able to obtain sufficient appropriate evidence to provide a basis for an opinion on the reported performance information of the development priority.

Basis for Disclaimer of opinion

30. I was unable to obtain sufficient appropriate evidence for all indicators relating to this development priority. This was due to limitations place on the scope of my work. I was unable to confirm the reported achievements by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements of all the indicators.

KPA 2 – Local Economic Development

Disclaimer of opinion

31. I do not express an opinion on the reported performance information for KPA 2 – Local economic development of the municipality. Because of the significance of the matters described in the basis for disclaimer of opinion section of my report, I have not been able to obtain sufficient appropriate evidence to provide a basis for an opinion on the reported performance information of the development priority.

Basis for Disclaimer of opinion

32. I was unable to obtain sufficient appropriate evidence for all indicators relating to this development priority. This was due to limitations place on the scope of my work. I was unable to confirm the reported achievements by alternative means. Consequently, I was unable to

determine whether any adjustments were required to the reported achievements of all the indicators.

Other matter

Achievement of planned targets

33. Refer to the annual performance report on pages x to x for information on the achievement of planned targets for the year and explanations provided for the under/overachievement of a significant number of targets. This information should be considered in the context of the disclaimer of opinions expressed on the usefulness and reliability of the reported performance information in paragraph 32 and 34 of this report.

Responsibilities of the accounting officer for the reported performance information

34. The accounting officer is responsible for the preparation of the annual performance report in accordance with the prescribed performance management and reporting framework, as set out in annexure D to this report and for such internal control as the accounting officer determines is necessary to enable the preparation of performance information that is free from material misstatement in terms of its usefulness and reliability.

Auditor-general's responsibilities for the reasonable assurance engagement on the reported performance information

35. My objectives are to obtain reasonable assurance about whether the reported performance information in the annual performance report for the selected development priorities is free from material misstatement, in accordance with International Standard on Assurance Engagements, ISAE 3000: *Assurance engagements other than audits or reviews of historical financial information* and to issue a management report that includes my opinion. However, because of the matter described in the basis for disclaimer of opinion section of my report, I was not able to obtain sufficient appropriate evidence to provide a basis for an audit opinion on the selected development priorities.

36. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) together with the ethical requirements that are relevant to my audit. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.

2.4 AUDIT OF COMPLIANCE WITH LEGISLATION

37. Included below are material findings on compliance with selected specific requirements of applicable legislation, as set out in the general notice issued in terms of the PAA.

Budgets

38. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R11 699 778, as disclosed in note 47 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by increase in repairs and maintenance costs.

Annual financial statements, performance reports and annual reports

39. 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, current assets, liabilities, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

40. The annual performance report for the year under review did not include measures taken to improve performance, as required by section 46(1)(c) of the MSA.

Expenditure management

41. Effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R256 676, as disclosed in note 42 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by interest and penalties charged on late payments to suppliers.

42. Effective steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The value of R5 801 360 as disclosed in note 43, is not complete as management was still in the process of quantifying the full extent of the irregular expenditure. The majority of the irregular expenditure was caused by goods and services procured without inviting competitive bids.

43. Money owed by the municipality was not always paid within 30 days as required by section 65(2)(e) of the MFMA.

Asset Management

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

Strategic planning and performance management

45. The SDBIP for the year under review did not include the service delivery targets and performance indicators for each quarter as required by section 1 of the MFMA.

46. Amendments to the IDP were made without consultation with the district municipality as required by municipal planning and performance management regulations 3(6)(a).

47. A performance management system was not established as required by section 38(a) of the MSA and municipal planning and performance management regulation 8.

48. The performance management system and related controls were not maintained as it did not describe how the performance planning, monitoring, measurement, review, reporting, improvement processes should be conducted, as required by municipal planning and performance management regulation 7(1).

Procurement and contract management

49. Some of the quotations were accepted from prospective providers who were not on the list of accredited prospective providers and did not meet the listing requirements prescribed by the SCM policy, in contravention of SCM regulations 16(b) and 17(b).

50. Some of the quotations were accepted from 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). Similar non-compliance was also reported in the prior year.

51. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1). Similar non-compliance was also reported in the prior year.

52. Some of the construction contracts were awarded to contractors that were not registered with the CIDB in accordance with section 18(1) of the CIDB Act. This non-compliance was identified in the procurement processes for the Sutherland construction of road Jupiter Single project.

53. The performance of the contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA. Similar non-compliance was also reported in the prior year.

54. Awards were made to providers whose directors / principal shareholders were in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulation 44.

Human resource management

55. Appropriate systems and procedures to monitor, measure and evaluate performance of staff were not developed and adopted as required by section 67(1)(d) of the MSA.

Consequence management

56. Irregular fruitless and wasteful expenditure incurred by the municipality were not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the Municipal Finance Management Act.

57. Unauthorised 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) of the Municipal Finance Management Act.

2.5 OTHER INFORMATION

58. The Karoo Hoogland Local Municipality accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report and those selected development priorities presented in the annual performance report that have been specifically reported in the auditor's report.
59. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.

60. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

61. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the

other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and re-issue an amended report as appropriate, however, if it is corrected this will not be necessary.

2.6 INTERNAL CONTROL

62. The significant deficiencies in internal control which led to our overall assessment of the status of the drivers of key controls, as included in the figure in paragraph x, is described below. The detailed assessment of the implementation of the drivers of internal control in the areas of financial statements, performance reporting and compliance with legislation is included in annexure F.

Leadership

Oversight responsibility

63. The municipality did not have sufficient monitoring controls to ensure the proper implementation of the overall process of planning, budgeting, implementation and reporting.
64. The Accounting Officer did not adequately perform oversight responsibility over financial reporting resulting in material misstatements being identified during the audit.
    - Detailed reviews of the financial statements, supporting working papers and calculations prior to submission for audit were not performed by the Chief Financial Officer. This impacted the accuracy and quality of the financial statements submitted on 31 August 2017 to the extent that the submission contained errors, omissions and misstatements. Refer to table of identified material misstatements.

Human resource management

Human resource planning and organisation

65. A human resource plan based on the strategic plan of the municipality was not in place.

Performance management

66. There is no performance management system in place for employees other than senior managers.

Action plans to address internal control deficiencies

67. The municipality developed a plan to address external audit findings, but the appropriate level of management did not monitor adherence to the plan in a timely manner to ensure that the control deficiencies relating to prior year were adequately addressed resulting in instances of non-compliance with laws and regulations being identified.

Policies and procedures

68. The municipality does not have a performance management system in place. No polices were developed and implemented to govern performance management

69. The internal policies and procedures of the municipality did not adequately address the processes pertaining to the planning, monitoring, managing and reporting of performance information at an overall performance management level and at an objective level

- The municipality did not have documented and approved internal policies and procedures to address the process of collection, recording, processing, monitoring and reporting of performance information
- The accounting officer of the municipality did not develop, implement and monitor sufficient and appropriate internal controls to mitigate the risk of material misstatement in the preparation of the annual financial statements; and
- Several policies were identified that were not approved, implemented and monitored for the year under review.

Information technology governance framework

70. IT Service level agreements were not monitored due to the municipality not having sufficient IT skilled staff who was assigned the responsibilities of monitoring the service level agreements.

Financial and performance management

Proper record keeping

71. The municipality did not have a proper record management system to maintain information that supported the reported performance in the annual performance report. This included information that related to the collection, collation, verification, storing and reporting of actual performance information.
72. The municipality could not provide signed employment contracts for some employees.

Daily and monthly processing and reconciling of transactions

73. Management did not implement the following daily and monthly controls designed for the municipality's business processes:
    - Asset reconciliations of the municipality are not performed and reviewed on a monthly basis.
    - The municipality did not implement an effective and efficient system of internal control to respond to unauthorised, irregular and fruitless and wasteful expenditure
    - The municipality did not ensure that compliance checklists were prepared to identify and prevent instances of non – compliance with relevant laws and regulations

Regular, accurate and complete financial and performance reports

74. As indicated in section 2.1, the financial statements contained material misstatements. This was mainly due to a lack of adequate review and weakness in the implementation of internal controls in respect of financial management and financial reporting.

Compliance monitoring

75. Non-compliance with laws and regulations could have been prevented had the municipality designed, implemented and monitored a system of compliance with relevant laws and regulations.

76. Municipal officials are not aware of legislative requirements, resulting in various instances of non-compliance with laws and regulations.

Information technology systems

77. Deficiencies reported in the prior year audit on Information Technology (IT) environment and controls were not addressed by the municipality.

78. The weaknesses surrounding IT security management, user account management, EFT management, program change management and IT service continuity were due to the municipality not having sufficient IT skilled staff to implement adequate controls.

Governance

Internal audit

79. Management did not ensure that is an adequately resourced and functioning internal audit unit that identifies internal control deficiencies and make recommendations for corrective action to be taken was established.

Audit Committee

80. The audit committee did not consist of at least three persons with appropriate experience.

81. The audit committee did not advise the council / accounting officer on matters relating to performance management and performance evaluation.

82. The audit committee did not respond to the council on the issues raised by the Auditor-General in the audit report.

83. The Audit Committee did not review the municipality's performance management system and did not make any recommendations in this regard.

84. The audit committee members were not appointed by the council.

Summary

85. The matters above, as they relate to the basis for the qualified opinion, findings on the annual performance report and findings on compliance with legislation, will be summarised in the auditor's report as follows:

86. The Accounting officer did not exercise adequately perform oversight responsibility over the preparation of the annual financial statements, performance reporting, compliance with laws and regulations and internal control. Leadership did not implement adequate processes to ensure that reviews took place before information was submitted. This was evidenced by the material misstatements in the financial statements, non-compliance with laws and regulations and internal control deficiencies noted throughout the audit process. Furthermore, action plans were not adequately monitored to ensure that the control deficiencies relating to prior year were adequately addressed resulting in instances of non-compliance with laws and regulations being identified.

87. Senior management did not adhere to internal controls, which resulted in various instances of irregular, fruitless and wasteful and unauthorised expenditure being incurred and other material misstatements in the financial statements, not detected by management.

88. The portfolio of evidence for the annual performance report was not submitted for audit. This was due to staff members within the reporting units not fully understanding the performance information requirements for audit purposes.

89. Management did not review the financial statements, to ensure the achievement of fair

presentation; this resulted in material misstatements being identified in the financial statements.

2.7 OTHER REPORTS

90. There were no engagements conducted by various parties that have or could potentially have an impact on the municipality's financial statements, reported performance information and compliance with applicable legislation and other related matters.

SECTION 3: Assurance providers and status of implementation of commitments and recommendations

3.1 ASSESSMENT OF ASSURANCE PROVIDERS

91. The annual report is used to report on the financial position of auditees, their performance against predetermined objectives and overall governance. One of the important oversight functions of the municipal council is to consider auditees' annual reports. To perform this oversight function, they need assurance that the information in the annual report is credible. To this end, the annual report includes our auditor's report, which provides assurance on the credibility of the financial statements and the annual performance report, as well as on the auditee's compliance with legislation.

92. Our reporting and oversight processes reflect on past events, as they take place after the end of the financial year. However, management, the leadership and those charged with governance contribute throughout the year to the credibility of financial and performance information and compliance with legislation by ensuring that adequate internal controls are implemented.

93. We assess the level of assurance provided by these assurance providers based on the status of internal controls (as reported in section 2.6) and the impact of the different role players on these controls. We provide our assessment for this audit cycle below.

First level of assurance

Senior management: provides some assurance

94. All four controls of proper record keeping, regular reporting, compliance monitoring and IT system controls are not properly developed, implemented and monitored by senior management.

Accounting officer: provides some assurance

95. The accounting officer has been visible throughout the audit however the municipality has remained stagnant from the previous year

Mayor: provides some assurance

96. The mayor is available to interact with the audit team however the municipality remains fairly stagnant from the prior year.

Second level of assurance

Internal audit unit: provides no assurance

97. Legislation in South Africa requires the establishment, roles, and responsibilities of internal audit units. Internal audit units form part of the internal control and governance structures of the municipality and play an important role in its monitoring activities. Internal audit provides an independent assessment of the municipality's governance, risk management and internal control processes.

98. The internal audit unit of a municipality's must prepare a risk-based audit plan and internal audit programme for each financial year. It must advise the accounting officer and report to the audit committee on implementing the internal audit plan and matters relating to internal audit; internal controls; accounting procedures and practices; risk and risk management; performance management; loss control and compliance with the MFMA. The internal audit unit must also perform such other duties as may be assigned by the accounting officer.

99. There was no internal audit unit established during the year under review.

Audit committee: provides some assurance

100. The audit committee is an independent advisory body to the accounting officer and the management and staff of the municipality on matters relating to internal financial control and internal audits; risk management; accounting policies; the adequacy, reliability and accuracy of financial reporting and information; performance management; effective governance; the MFMA and any other applicable legislation; performance evaluation; and any other issues.

101. The audit committee is also expected to review the annual financial statements to provide an authoritative and credible view of the municipality, its efficiency and effectiveness and its overall level of compliance with the applicable legislation.

102. The audit committee is not comprised of the minimum number of members as required by MFMA Act.

103. The audit committee did not provide adequate reports to Council regarding performance management.

Third level of assurance

Municipal council: provides some assurance

104. The council has convened several meetings to discuss critical issues however the municipality has remained fairly stagnant from the prior year.

Municipal public account committee (MPAC): provides some assurance

105. The extent to which the council adopted the MPAC guides has been considered in the assessment of MPAC as an assurance provider.

106. The municipality's audit outcome has remained stagnant from the prior year

3.2 STATUS OF IMPLEMENTING COMMITMENTS AND RECOMMENDATIONS

107. Below is our assessment of the progress in implementing the commitments made by the municipality to address the previous and current years' audit findings.

No	Commitment	Made by	Date	Status
1	To reduce a number of material misstatements	CFO	July 2016	Ongoing
2	To reduce incurrence of irregular and fruitless and wasteful expenditure	CFO	July 2016	Ongoing
3	Compliance with laws and regulations will be monitored	CFO	July 2016	Ongoing
4	To reconstruct the asset register that is GRAP 17 compliant	CFO	July 2016	Asset register was reconstructed during the year under review.
5	To obtain a better audit outcome regarding predetermined objectives	CFO	July 2016	Ongoing

108. 43 audit recommendations accepted by management in the previous year on matters included in the auditor's report and other important matters were implemented, or alternative actions were taken to resolve the finding.

109. 15 recommendations are still being implemented and 1 has not been addressed, or very limited progress has been made.

110. Details on the status of implementing the previous year's recommendations are provided in section 10, which summarises the detailed audit findings.

SECTION 4: Focus areas

4.1 FINANCIAL VIABILITY

111. Our audit included a high-level overview of the municipality's financial viability as at year-end. The financial viability assessment provides useful information for accountability and decision-making purposes and complements the financial statements by providing insights and perspectives. The financial viability assessment is expected to enhance timely remedial decision-making and policy reforms where financial viability may be at risk. It will also highlight to management those issues that may require corrective action and the urgency and magnitude of the reforms and decisions necessary to maintain operations. The information should be used to complement, rather than substitute, management's own financial assessment.

Financial viability assessment			
(Limitation = unable to obtain sufficient appropriate information to assess the indicator)		As at 30 June 2017	As at 30 June 2016
Expenditure management			
1.1	Creditor payment period	81.9 Days	203 Days
Revenue management			
2.1	Debt-collection period (after impairment)	708.3 Days	57 Days
2.2	Debt impairment provision as a percentage of accounts receivable	-84 %	83%
	• Amount of debt impairment provision • *Amount of accounts receivable	R 23 414 000R 27 863 000	R 19 601 695 R 23 5756 089
Asset and liability management			
3.1	A deficit for the year was realised (total expenditure exceeded total revenue)	No	No
	• Amount of the surplus/(deficit) for the year	R 2 089 993	R 1 994 032
3.2	A net current liability position was realised (total current liabilities exceeded total current assets)	Yes	Yes
	• Amount of net current assets/(liability) position	(R 1 519 000)	R 30 594 084
3.3	A net liability position was realised (total liabilities exceeded total assets)	No	No
	• Amount of net asset/(liability) position	R 161 167 000	R 204 182 310
Cash management			
4.1	The year-end bank balance was in overdraft	No	No

Financial viability assessment			
(Limitation = unable to obtain sufficient appropriate information to assess the indicator)		As at 30 June 2017	As at 30 June 2016
	• Amount of year-end bank balance (cash and cash equivalents)/(bank overdraft)	R 3 520 000	R 6 503 433
4.2	Net cash flows for the year from operating activities were negative	No	No
	• Amount of net cash in/(out) flows for the year from operating activities	R 10 302 000	R 10 826 029
4.3	Creditors as a percentage of cash and cash equivalents	141.8%	152.8%
	• Amount of creditors (accounts payable) • Amount of cash and cash equivalents/(bank overdraft) at year-end	R 10 302 000 R 3 520 000	R 10 885 955 R 6 503 433
Overall assessment			
		Yellow (Concerning)	Yellow (Concerning)
* *This (these) amount(s) has (have) been adjusted for uncorrected misstatements that resulted in the modification of the audit opinion and will therefore not agree to the financial statement amounts*			

High-level comments

112. Creditor payment days exceed the norm, which can result in penalty and interest charges being levied against the municipality and further non-compliance with laws and regulations.
113. Debtors' collection period is above the norm, resulting in significant cash flow problems and non-compliance with laws and regulations.
114. Significant provision for debt impairment, indicate poor debt recovery and significant financial losses, impacting on the going concern of the municipality.
115. Current liabilities exceed current assets, indicating that the municipality will not be able to pay short term debt when it becomes due within the next 12 months.

4.2 PROCUREMENT AND CONTRACT MANAGEMENT

Irregular expenditure

116. R 3 874 862 (100%) of irregular expenditure incurred in the current financial year was as a result of the contravention of SCM legislation. The root causes of the lack of effective prevention and detection are inadequate training of supply chain management officials and a lack of review and monitoring of compliance with applicable legislation.

Awards to persons in the service of the state

117. Regulation 44 prohibits awards to persons in the service of the auditee (i.e. employees and councilors), persons in the service of any other state institution and entities owned/managed by them. The audit included the identification of such prohibited awards. Further testing was also performed to determine whether the legislated requirements with regard to declarations of interest were adhered to.

118. The findings were as follows :

Finding	Number and value of awards made	Number and positions of official/ councillor identified	Number of suppliers identified	Further non-compliance or irregularities regarding the awards			
				Supplier did not submit declarations of interest	Supplier did not declare interest (false declaration)	Official/ councillor or did not declare interest	Official/ councillor was involved in awarding the contract/ quotation
Awards made to officials of the municipality	1 R195 520 (prior year)	1 Clerk: Credit Control Officer	1	1	0	1	0
Awards to persons in the service of other state institutions	1 R134 831	2	2	0	2		

Procurement processes

119. The table below is a summary of findings identified on procurement processes:

	Total		Quotations		Contracts	
	Number	Value	Number	Value	Number	Value
Awards selected for testing	*36*	*32 027 277*	*24*	*1 348 827*	*12*	*30 678 450*
Expenditure incurred on selected awards – current year		*14 915 195*		*1 223 749*		*13 691 446*
Awards on which non-compliance was identified	*14*	*6 033 095*	*6*	*255 187*	*8*	*5 777 908*
Irregular expenditure	*16*	*5 153 421*	*14*	*1 149 408*	*2*	*4 005 013*

Identified						

Procurement processes – general.

- 3 awards with a value of R 33 605 were procured without inviting at least the minimum prescribed number of written price quotations from prospective suppliers, and the deviation was approved even though it was possible to obtain the quotations.
- 3 quotations with a total value of R 102 087 were accepted from prospective providers who were not registered on the list of accredited prospective providers or the National Treasury's central suppliers database and did not meet the listing requirements prescribed by the SCM policy.
- 1 quotation to the value of R 14 488 was procured from suppliers whose tax matters had not been declared by the South African Revenue Services to be in order.
- 1 contracts with a value of R 3 265 483 were procured without inviting competitive bids, and the deviations were approved even though it was practical to invite competitive bids.
- 12 quotations were awarded to bidders who did not submit a declaration of whether they were employed by the state or connected to any person employed by the state.

Construction contracts

- 1 construction contract with a total value of R 1 168 202 was awarded to contractors who were not registered with the Construction Industry Development Board (CIDB).
- The performance of 6 contractors or providers was not monitored monthly. The total value of related contracts was R 6 151 907.

Internal control deficiencies

120. The accounting officer did not exercise adequate oversight responsibility over compliance with laws and regulations as well as internal controls which resulted in:
    - A construction contract being awarded to a contractor who is not registered on CIDB.
    - Quotations being awarded without obtaining the minimum prescribed number of written quotations
    - SCM officials are not implementing the approved policies and procedures under all circumstances

4.3 FRAUD AND CONSEQUENCE MANAGEMENT

121. The primary responsibility for preventing and detecting fraud rests with management and those charged with governance. We are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error, and to issue an auditor's report that includes our opinion. Due to the inherent limitations of an audit, there is a risk that some material misstatements, including fraud, may not be detected.

122. No findings were identified.

123. The MFMA and its regulations clearly stipulate that matters such as incurring unauthorised, irregular and fruitless and wasteful expenditure; the possible abuse of the SCM system (including fraud and improper conduct); and allegations of financial misconduct should be investigated. Disciplinary steps should be taken based on the results of the investigations. Our audits included an assessment of the municipality's management of consequences. The significant findings are provided below:

Measures to manage consequences

124. The following measures were not implemented to ensure that the environment is conducive to effective consequence management:

- The municipality did not adopt systems (policies) to investigate allegations of misconduct; and disciplinary procedures.
    - A disciplinary board was established but did not function during the year to investigate allegations of financial misconduct and monitor the institution of disciplinary proceedings against an alleged transgressor,

125. The table below provides a summary of transgressions from the previous year that were either not investigated or proper disciplinary steps were not taken after investigation.

Unauthorised, irregular, fruitless and wasteful expenditure

Finding	Number of instances	Value
Unauthorised expenditure		
Unauthorised expenditure identified in the previous year was not investigated to determine whether any person was liable for the expenditure	[redacted]	R85 127 558
Irregular expenditure		
Irregular expenditure identified in the previous year was not investigated to determine if any person was liable for the expenditure		R27 105 403
Fruitless and wasteful expenditure		
Fruitless and wasteful expenditure identified in the previous year was not investigated to determine whether any person was liable for the expenditure		R2 067 166

126. Unauthorised, irregular, fruitless and wasteful expenditure disclosed in note 42, 43 and 47 to the financial statements must be investigated to determine whether any official is liable for losses incurred as a result of this expenditure. Disciplinary steps must be taken against officials who caused or permitted the unauthorised, irregular, fruitless and wasteful expenditure and losses incurred must be recovered from the person liable.

4.4 USE OF CONDITIONAL GRANTS

127. For the financial year under review, the audit included an assessment of the effectiveness of the municipality's use of the following conditional grants received:

- Municipal Infrastructure grant
- Integrated national electrification programme.

- The following compliance findings were raised on the use of selected grants:
- For each of the grants tested as per the table above, we selected key projects funded by the grant and audited the use of grants on the project. Listed below are the audit findings raised on each project.

Key projects/initiatives funded by the grant				
Summary of selected key project and result of testing	**Details**	**Details**	**Details**	**Details**
Name of grant	**MIG**	**MIG**	**MIG**	**INEP**
Project/initiative funded by the grant	**SUTHERLAND BULK WATER**	**SUTHERLAND REBELSKOP AREA STORMWATER**	**SUTHERLAND SPORT FACILITIES**	**Fraserburg Electricity Network Upgrade Phase 1**
Audit findings				
Planned targets/key milestones for the selected project were not achieved	Limitation of scope	Limitation of scope	Limitation of scope	Limitation of scope
Reported performance/achievement of targets as per the project evaluation report was inaccurate	Limitation of scope	Limitation of scope	Limitation of scope	Limitation of scope
The municipality did not evaluate performance of the project	No findings were identified	No findings were identified	No findings were identified	No findings were identified
Findings were identified on the procurement of goods and services for the project	Yes	Yes	Yes	Yes
Misstatements were identified on the accounting for the expenditure	No misstatements identified	No misstatements identified	No misstatements identified	No misstatements identified
Payments were made for goods/services not received	No misstatements identified	No misstatements identified	No misstatements identified	No misstatements identified

4.5 PUBLIC PARTICIPATION

128. As part of the audit of predetermined objectives we audit compliance with the provisions of the Municipal Systems Act relevant to community participation. The following findings were raised:

- No ward level improvement plans were developed.

4.6 USE OF CONSULTANTS

129. The audit included an assessment of the effective use of consultants. In the local government environment, the partnership between the private and public sectors has become important in driving strategic goals.

130. The total expenditure on consultants was R 4 190 528.

131. A summary of the significant findings from the audit is as follows:

Performance management and monitoring

132. Measures applied to monitor consultancy projects were insufficient and could not ensure effective contract management.

133. A comparison of the consultant's services rendered and the deliverable to the initial project objectives and needs was not evaluated.

134. Material misstatements were identified or findings were raised by the auditors on the work performed by the consultant or in areas of the consultants' responsibilities. Some of the misstatements were subsequently corrected.

Internal control deficiencies

135. A policy should be developed to manage consultancy and assist in skills transfer to build internal capacity.

4.7 WATER AND SANITATION

136. The audit included an assessment of the water and sanitation service delivery objective of the municipality. We focused on the following:

- Management of grant funding for water and sanitation infrastructure
- Management processes for water and sanitation infrastructure projects
- Maintenance of water infrastructure
- Water losses

Water losses

137. The municipality disclosed water losses to the extent of 5.45%.

4.8 ROADS INFRASTRUCTURE

138. The audit included an assessment of the roads infrastructure service delivery objective. Procedures were performed in relation to the following:

- New and refurbished projects, including planning, project management and commissioning
- Maintenance of roads infrastructure
- Follow-up on the previous year's findings

139. A summary of the significant findings from the audit are as follows:

- No approved priority list of roads infrastructure exists for the renewal and routine maintenance projects which is used as a basis for the Roads Maintenance Plan (RMP). The reason for this was due to management not being aware of the requirements.

SECTION 5: Using the work of internal audit

140. The auditing standards allow external auditors the optional use of the work of internal audit for external audit purposes and for direct assistance.

141. There was no internal audit unit in place during the year under review.

SECTION 6: Emerging risks

6.1 Accounting, performance management/reporting and compliance matters

New pronouncements

Standards of GRAP

142. The ASB has issued the following GRAP pronouncements, with effective dates as indicated:

GRAP pronouncement	Effective date
Conceptual framework for general purpose financial reporting	Applicable once published
GRAP 20, *Related party disclosures*	To be determined
GRAP 32, *Service concession arrangements: grantor*	To be determined
GRAP 34, *Separate financial statements*	To be determined
GRAP 35, *Consolidated financial statements*	To be determined
GRAP 36, *Investments in associates and joint ventures*	To be determined
GRAP 37, *Joint arrangements*	To be determined
GRAP 38, *Disclosure of interests in other entities*	To be determined
GRAP 108, *Statutory receivables*	To be determined
GRAP 109, *Accounting by principals and agents*	To be determined
GRAP 110, *Living and non-living resources*	To be determined
IGRAP 17, *Service concession arrangements where a grantor controls a significant residual interest in an asset*	To be determined
IGRAP 18, *Recognition and de-recogntion of land*	1 April 2019
IGRAP 19, *Liabilities to pay levies*	1 April 2019
Directive 12, *The selection of an appropriate reporting framework by public entities*	1 April 2018
Guideline on accounting for housing arrangements	Applicable once published

Municipal SCOA

143. The municipality has implemented measures to implement the mSCOA requirements and have appointed a consultant through the transversal IT contract. The project is currently on-going and has not been fully implemented.

6.2 Audit findings on the annual performance report that may have an impact on the audit opinion in future

For the 2016-17 cycle, the planned and reported performance information of selected development priorities was audited against additional criteria as developed from the Performance Management Reporting Framework.

Audit findings in relation to the additional criteria do not have an impact on the audit opinion for 2016-17 (reported in the management report); however, going forward findings arising from the audit against the additional criteria may have an impact on the audit opinion.

SECTION 7: Ratings of detailed audit findings

For the purposes of this report, the detailed audit findings included in annexures A to C have been classified as follows:

- Matters to be included in the auditor's report: these matters should be addressed as a matter of urgency.
- Other important matters: these matters should be addressed to prevent them from leading to material misstatements of the financial statements or material findings on the performance report and compliance with legislation in future.
- Administrative matters: these matters are unlikely to result in material misstatements of the financial statements or material findings on the performance report and compliance with legislation.

SECTION 8: Conclusion

The matters communicated throughout this report relate to the three fundamentals of internal control that should be addressed to achieve sustained clean administration. Our staff remains committed to assisting in identifying and communicating good practices to improve governance and accountability and to build public confidence in government's ability to account for public resources in a transparent manner.

Yours faithfully

Orlando Fredericks

Senior Manager: Northern Cape

30 November 2017

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