



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence

FINAL MANAGEMENT REPORT
Thembelihle Local Municipality

30 June 2020

Communicated to the accounting officer on: 31 March 2021





Management report

Thembelihle Local Municipality

30 June 2020

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Management report to the accounting officer on the audit of the Thembelihle Local Municipality for the year ended 30 June 2020


INTRODUCTION




1. The purpose of the management report is to communicate audit findings and other key audit observations to the accounting officer. The report 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 2021.
2. These findings were communicated to management. The report details management's response to these findings and 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 an opinion in the management report on the usefulness and reliability of the reported performance information for selected development priority 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 25 of 2004 (PAA).
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. Please note that the information contained in these documents is confidential, privileged and only for the information of the intended recipient(s). It may not be used, published or redistributed without the prior written consent of the Auditor-General of South Africa (AGSA). Any form of reproduction, dissemination, copying, disclosure, modification, distribution and/or publication of this material is strictly prohibited. Should the information be used or processed in a manner that contravenes any laws in the Republic of South Africa, the AGSA is fully indemnified from liability that may arise from such contravention.
7. 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



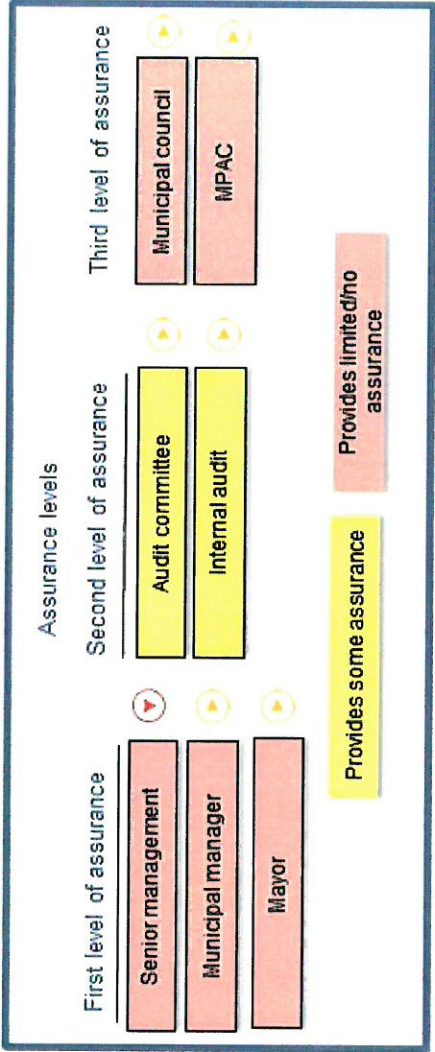
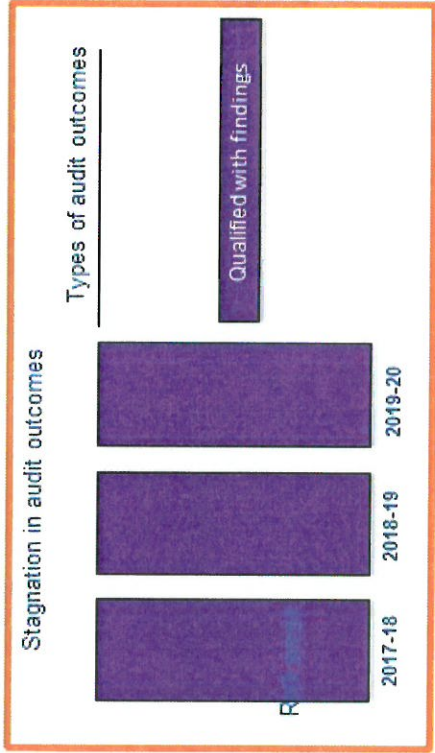
- Status of the level of assurance provided by key role players
- Status of the drivers of internal controls
- Status of risk areas
- Root causes to be addressed

Movement from the previous year is depicted as follows:

 / Improved

   / Unchanged / slight improvement / slight regression

 / Regressed



1 To improve/maintain the audit outcomes ...

2 ... the key role players need to assure that ...

5 ... the root causes are addressed ...

4 ... the risk areas and ...

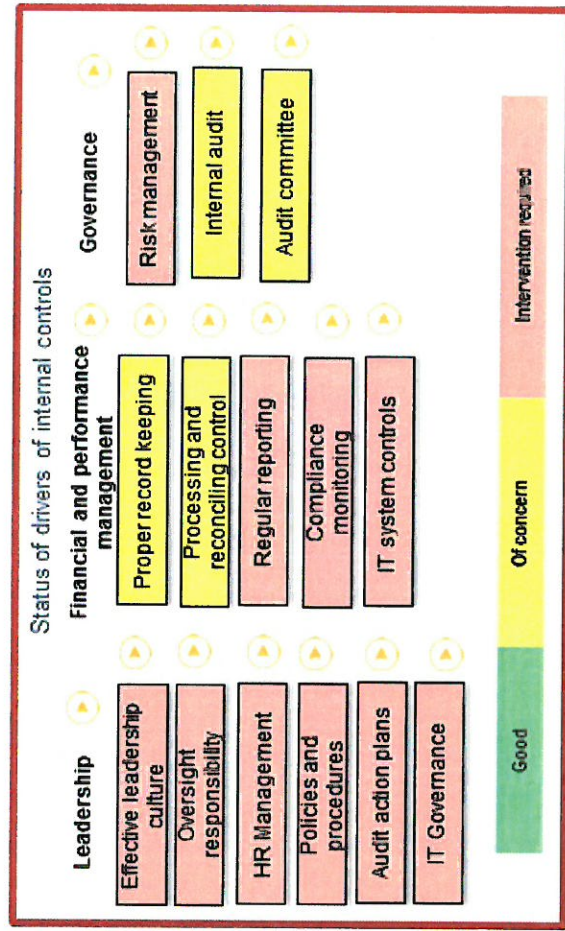
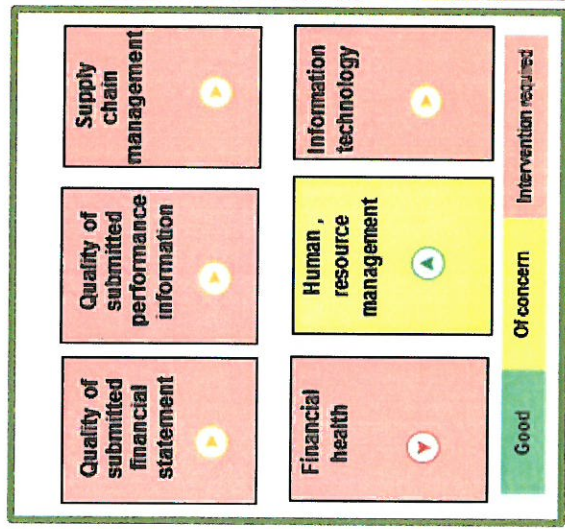
3 ... attention is given to the key controls and ...

... the best practices are maintained.

Root causes should be addressed

Slow progress by management (poor leadership and oversight) leading to financial misstatements and no movement with regards to performance recording.

Lack of consequence management to address the material misstatements and compliance findings.



OVERALL MESSAGE

8. The audit opinion of the municipality has been stagnant from prior year to current year due to slow to no response from management of their planned action plan to address issues previously highlighted. This has led to repeat material and compliance findings in the current year under audit.
9. Material misstatements and also material non-compliance with applicable legislation and standards were identified in the annual financial statements that were submitted for audit.
10. The municipality's ability to provide auditors with the requested information as per the engagement letter was also an issue that led to the stagnation in the audit opinion as four cut-off letters were issued to the municipality.
11. The municipality still incurs high level of irregular expenditure and this is mostly relating to non-compliance with the SCM regulations.
12. The financial health of the municipality has deteriorated from that of previous year as now it requires intervention. (refer to section 4)

SECTION 1: Interactions with stakeholders responsible for oversight and governance

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

Key stakeholder	Purpose of interaction	Number of interactions
Municipal manager	Discussion of the audit progress, audit findings identified and any fraud identified during the audit.	4
Audit committee	Discussion of audit progress, engagement strategy, engagement letter and any possible fraud known, discussion of the draft audit report.	2
Senior Management	Discussion of the audit progress, audit findings, management responses and any fraud identified during the audit.	6

14. At these interactions, we shared the following key matters affecting audit outcomes and the auditee:
 - Audit strategy and engagement letter
 - Progress of the audit
 - Discussion of audit findings
 - Audit fees
 - Discussion of final management report and audit report
15. Some 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, which deals with the assessment of assurance providers.

SECTION 2: Matters relating to the auditor's report

Audit of the financial statements

16. 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).
17. The misstatements that were not corrected form the basis for the qualification of opinion on the financial statements.

Material misstatement				
Financial statement item	Finding	Occurred in prior year	Impact R current year	Impact R previous year
Material misstatements not corrected				
Current assets				
Statutory receivable from non-exchange transactions: Traffic fines	[ISS.82] Limitation on Receivables: Traffic fines. Limitation of Receivable from non-exchange transactions.	Yes	R1 675 760	R4 547 621
	[ISS.112] Limitation - VAT statutory receivable	No	-R 3 182 341	-
Current liabilities				
Provision of landfill sites	[ISS.130] Limitation on Provision of Landfill sites and the data affecting the landfill sites not considered	No	R11 664 614	-

Material misstatement				
Financial statement item	Finding	Occurred in prior year	Impact R current year	Impact R previous year
Payables from exchange transactions: Trade payables	[ISS.115] Differences between creditors schedule and AFS amount(COMAF 18)	Yes	R1 958 552	R86 291 414
Retention fess	[ISS.54] FIN-Payables from exchange-Limitation. Overstatement of Payables from exchange transactions.	Yes	R1 368 046	R1 368 046
Revenue				
Revenue from exchange				
Rental of facilities	[ISS.33] Revenue: Limitation of scope(Revenue)	No	R411 563	
Service charges: Sale of electricity	[ISS.90] Revenue completeness issues : Sale of metered electricity	Yes	Unknown	Unknown
Service charges: Sale of water	[ISS.48] Revenue Completeness issues : Sale of water	Yes	Unknown	Unknown
Service charges: refuse removal	[ISS.50] Revenue: Differences between the auditors recalculation and amount recorded	No	R202 767	-
Commission received	[ISS.05] Commission from motor car registration is not accurately disclosed [ISS.89] No Contract obtained to agent principle transaction	No	R906 855	-
Interest received: investments	[ISS.78] Revenue from exchange transaction : Interest received	No	R50 195	-

Financial statement item	Material misstatement		Impact R current year	Impact R previous year
	Finding	Occurred in prior year		
Availability charges	[ISS.90] Availability charges incorrectly disclosed	No	Unknown	-
Disclosure				
Prior-year adjustments	[ISS.84] Journals not supported by source documents: Property, plant and equipment	No	R2 488 927	
	[ISS.84] Journals not supported by source documents: Investment property	No	R412 039	-
	[ISS.84] Journals not supported by source documents: Depreciation	No	R 5 392	-
	[ISS.84] Journals not supported by source documents: Licence and permits (non-exchange)	No	R576 594	-
	[ISS.84] Journals not supported by source documents: General expenditure - project maintenance cost	No	R3 116 477	-
	[ISS.84] Journals not supported by source documents: Surplus (deficit) for the year	No	R3 764 306	-
Commitments	[ISS.41] The municipality did not maintain records of the contractual information used to determine commitments.	Yes	R 4 254 579	-
	[ISS.95] Difference between commitments amount disclosed and auditor's recalculation	Yes	R4 484 903	-
	[ISS.103] Differences of contract values between contract and commitments register.	No	R23 209 51	-
Cash flow statement	[ISS.88] Presentation and Accuracy of the cash flow from and to the municipality and the accuracy of it.	No	R 8 786 605	-

Material misstatement				
Financial statement item	Finding	Occurred in prior year	Impact R current year	Impact R previous year
Unauthorised Expenditure	[ISS.111] Unauthorised expenditure not calculated correctly. Understatement of Disclosure.	No	R24 849 487	-
	[ISS.53] Incorrect Unauthorised expenditure amount disclosed	Yes	Amount absorbed under issue 111	R34 352 239
Irregular Expenditure	[ISS.22] Irregular expenditure opening balance	No	R133 683 484	-
Irregular Expenditure	L1.5. Completeness issue on irregular expenditure	Yes	R1 861 395	-
Distribution losses	Consequential impact of the water and electricity qualification	Yes	Unknown	-
Material misstatements corrected				
Non-current liabilities				
Long service awards	[ISS.81] Differences noted in variable used by expert for Long service awards	No	Unknown	-

Matters to be brought to the attention of users

Emphasis of matter paragraphs

18. 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:

Material impairment- Receivables

19. As disclosed in note 5 of the financial statements, material losses of R59 538 677 (2019: R51 025 377) were incurred as a result of impairment in current and non-current debtors.

Material uncertainty relating to going concern

20. We draw attention to the matter below. Our opinion is not modified in respect of this matter.
21. We draw attention to note 53 to the financial statements, which indicates that the municipality incurred a deficit of R33 491 097 during the year ended 30 June 2020 and, as of that date the municipality's current liabilities exceeded its current assets by R123 311 364. As stated in note 53, these events or conditions, along with other matters as set forth in note 53 indicate that a material uncertainty exists that may cast significant doubt on the municipality's ability to continue as a going concern.

Other matter paragraphs

22. 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

23. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. 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 (ISA 700.53)

24. 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 on them.

Performance information reporting

25. In terms of the general notice issued in terms of the PAA, the opinion on the audit of reported information will be included in the management report.



26. We were unable to audit and report on the usefulness and reliability of the reported performance information as the municipality's annual performance report was not prepared as required by section 46 of the Municipal Systems Act and section 121(3)(c) of the MFMA.

Responsibilities of the accounting officer for the reported performance information

27. The accounting officer is responsible for the preparation of the annual performance report in accordance with the prescribed performance management and reporting framework 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

28. Our objectives are to obtain reasonable assurance about whether the reported performance information for the selected development priority presented in the annual performance report is free from material misstatement, and to issue a management report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that the assurance engagement conducted in accordance with the relevant assurance standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if they could reasonably be expected to influence the relevant decisions of users taken on the basis of the reported performance information.
29. Our procedures address the usefulness and reliability of the reported performance information, which must be based on the approved performance planning documents of the municipality. We have not evaluated the appropriateness of the performance indicators established and included in the planning documents. Our procedures do not examine whether the actions taken by the municipality enabled service delivery. Our procedures also do not extend to any disclosures or assertions relating to planned performance strategies and information relating to future periods that may be included as part of the reported performance information. Accordingly, our opinion does not extend to these matters.

Audit of compliance with legislation

30. 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.

Annual financial statements and annual report

31. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of non-current liabilities, non-current asset, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and or the supporting records were provided subsequently, but the uncorrected material misstatements and or supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.
32. The 2018/2019 annual report was not tabled in the municipal council after the end of the financial year, as required by section 127(2) of the MFMA.

Expenditure management

33. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
34. Expenditure was incurred in excess of the approved budget, in contravention of section 87(8) of the MFMA.
35. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The full extent of the irregular expenditure could not be quantified as indicated in the basis for qualification paragraph. The majority of the disclosed irregular expenditure was caused by non-compliance with SCM requirements.
36. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R7 729 633, as disclosed in note 56 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 non-payment of creditors which resulted in interest being charged on late payments.
37. Reasonable steps were not taken to prevent unauthorised expenditure, as required by section 62(1)(d) of the MFMA. The full extent of the unauthorised expenditure could not be quantified as indicated in the basis for qualification paragraph. The majority of the disclosed unauthorised expenditure was caused by overspending of the vote.

Revenue Management

38. An effective system of internal control for revenue was not in place, as required by section 64(2)(f) of the MFMA.
39. Revenue due to the municipality was not calculated on a monthly basis, as required by section 64(2)(b) of the MFMA.

Strategic planning and performance management

40. A performance management system was not established, as required by section 38(a) of the MSA.
41. The performance management system and related controls were not maintained and inadequate 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 reg 7(1).

Procurement and Contract Management

42. Some of the goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations, in contravention of by SCM regulation 17(1)(a) and (c). Similar non-compliance was also reported in the prior year.
43. 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).
44. The performance of some 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.

Consequences Management

45. 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 MFMA.
46. Irregular, 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)(b) of the MFMA.
47. Cases of financial misconduct which constitute a crime committed by officials were not always reported to the South African Police Service, as required by the municipal regulations on financial misconduct procedures and criminal proceedings 10(1).
48. Allegations of theft which exceeded R100 000 were not reported to the South African Police Service, as required by section 34(1) of the PRECCA.



Other information

49. The 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.
50. Our opinion on the financial statements and compliance with legislation do not cover the other information and we do not express an audit opinion or any form of assurance conclusion on it.
51. In connection with our audit, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements, or our knowledge obtained in the audit, or otherwise appears to be materially misstated.
52. The following paragraphs will be included in the auditor's report to highlight to the users whether any inconsistencies in the other information exist:
53. 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.

Internal controls

54. The significant deficiencies in internal control that led to our overall assessment of the status of the drivers of key controls, as included in the figure in paragraph x, are 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

Effective leadership culture

55. Management does not take recommendations from independent evaluators and addressed them in a timely manner (Slow progress on action plan).

Oversight responsibility

56. The finance committee, Corporate services committees and Development & Technical services committee, as well as all the oversight committees do not have terms of reference in place
57. The committee members did not sign an annual declaration of interest
58. During the financial year end of 2019/20 audit the municipality the municipality did not submit the annual performance report as required by MSA to the auditors as legislated within two months after the end of the financial year



59. Money owed by the municipality was not always paid within 30 days

Human resource management

60. The municipality has a concerning vacancy rate

61. The organogram is not reviewed and updated on a regular basis

62. The municipality did not take any disciplinary actions for non-compliance with the code of conduct (In the case of Mr. E Struis).

63. There is no regularly evaluation of employees skills and competencies in order to establish whether they are still relevant and adequate to carry out the entity's objectives.

64. The Organisational structure is Outdated

65. The municipality does not have in place a process to reward and retain employees who are performing well.

66. Management do not regularly reviews and evaluates the organisational structure for continued relevance and effectiveness and efficiency in support of internal controls

Policies and procedures

67. The Municipality do not have Policies and procedures that reflect expectations of competency necessary to support the achievement of the entity's objectives are in place

68. The Municipality does not have policies for promotion, training, evaluation , counselling and termination.

69. The municipality does not have a policy for performance management

70. No policy for investigations in place to implement consequence management

71. SCM Policy not inline with regualtions

Action plans to address internal control deficiencies

72. Management does not address internal control deficiencies timely

73. The risk management strategy on how to respond to identified risk is not implemented timeously.

74. The municipality does not have a formal process in place for employees who are directly involved in carrying out the entity's internal control to communicate breakdowns in the system of internal control.

75. The Municipality did not consider findings from the external audit, as only three were completed and addressed.(slow progress in action plan to address issues previously identified by auditors)



Information technology governance framework

76. During the audit of ICT Entity level controls, the auditor identified that the municipality does not have the following in place:

- Approved IT Governance framework
- Approved IT strategic plan
- IT Steering Committee
- IT Risk/Control Assessment/Register
- Approved IT security policy
- Patch management software
- Approved disaster recovery plan

Financial and performance management

Proper record keeping

77. The municipality did not formulate and implement a record management policy and related procedures to ensure that all documentation was properly controlled.

Daily and monthly processing and reconciling of transactions

78. Management did not ensure that bank reconciliations are prepared timeously.

Regular, accurate and complete financial and performance reports

79. Management did not ensure that all information disclosed in AFS is accurate

Compliance monitoring

80. A list of disposals submitted for the year ended 30 June 2020 was not supported by evidence that council approved disposal of capital assets

81. Non-compliance with legislation was not properly reviewed, monitored and prevented.

Information technology systems

82. There is no training in place for updated systems

83. A Formally approved IT Service continuity controls plan has not been established to ensure the availability and recoverability of financial and performance information systems in instances of data loss or disaster.

Governance

Internal audit

84. only one quarterly internal audit report was submitted and reported to audit committee.

Audit committee

85. Audit committee did not meet at least 4 times in the year under audit

Summary

86. 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:

87. Management did not take appropriate action with regards to lack of controls in the finance and supply chain management unit, resulting in the re-occurrence of the material misstatements and compliance issues.

88. Leadership did not adequately exercise appropriate oversight over financial and performance reporting, compliance monitoring and related internal controls, which led to matters being repeatedly raised from the prior year to the current year

89. There was no proper system in place to collate all the required support to enable the municipality to compile a proper annual performance report.

90. Management did not timeously monitor adherence to the audit action plan resulting in the re-occurrence of some of the compliance, financial and annual report issues

91. The situation on human resources, information technology, oversight and internal controls remained stagnant, hence the audit opinion also remained stagnant.

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

Assessment of assurance providers

92. 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.



93. 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.

94. 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 limited assurance

- The annual financial statements of the municipality were submitted on time however material misstatements and material non compliances with the applicable legislation and standard were identified. Some of these findings are repeat finding from prior year. Senior management must design and communicate processes that enable accurate reporting and be determined to address any deviations thereof. These processes, that should have been effective throughout the year, should produce reporting that is supported by the underlying records. During the audit the senior managers were visible however there were some instances management failed to provide the required information.

Accounting officer: provides limited assurance

- The accounting officer was visible during the audit and and provided assistance were needed, however there were issues of lack of management oversight that were identified in which the accounting authority failed to identify. The visibility of the accounting officer did not culminate to an improvement to the audit outcome

Mayor: provides limited assurance

- The mayor provided limited assurance and no interaction were held with the auditors to discuss any milestones or challenging matter that were identified. No consequence management was implemented for the year as a result repeat findings and no compliance matter were identified. The Mayor should commit in assisting the municipality more in ensuring proper implementation of controls and also affect consequence management oversight by ensuring that consequence management was implemented during the year.

Second level of assurance

Internal audit unit: provides some assurance

- Legislation in South Africa requires the establishment of, and provides for, the roles and responsibilities of internal audit units. Internal audit units must form part of the internal control and governance structures of the municipality and must play an important role in its monitoring

activities. Internal audit must provide an independent assessment of the municipality governance, risk management and internal control processes.

- The internal audit unit of a municipality 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 implementation of 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.
- The municipality is using a well capacitated and resourced internal audit unit. Internal auditors are independent from the operational divisions that they audit and act objectively. The internal audit unit did perform internal audits during the financial year however meet once to discuss matters of the municipality. Recommendations were included in the internal report that was submitted to the municipality. The internal audit unit also committed themselves to assist the municipality by performing internal audits on the progress made on action plans and annual financial statements prior to it being submitted to the AGSA.

Audit committee: provides some assurance

- The audit committee must be 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.
- 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.
- The audit committee members are well balanced with regards to skills and public sector experience and have a good understanding of major accounting practices and public sector reporting requirements. The audit committee report directly to council as required by the MFMA and influenced good governance and clean administration within the municipality, however material misstatements and instances of non-compliance were identified.

Third level of assurance

Municipal council: provides limited assurance

- There were no interactions held between the auditors and council. Council should however be more involved in the audit and also provide support to management at operation level so as to improve the state of affairs of the municipality. Material misstatements in the financial statements and also with compliance were identified in which they could have been avoided if proper support from the oversight committees was given

Municipal public account committee (MPAC): provides limited assurance

- There was limited assurance provided by the MPAC committee. The committee failed to investigate all unauthorised, irregular, fruitless and wasteful expenditure identified and reported in the prior period

Status of implementing commitments and recommendations

95. No specific commitments were recorded on the significant deficiencies in internal controls we raised in the 2018/19 financial year.

SECTION 4: Specific focus areas**Financial viability**

96. 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 thereon. 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

FINANCIAL VIABILITY ASSESSMENT			
		As at 30 June 2020	As at 30 June 2019
Expenditure management			
1.1	Creditor-payment period	1069 Days	1095 Days
Revenue management			
2.1	Debt-collection period (after impairment)	56 Days	48 Days
2.2	Debt-impairment provision as a percentage of accounts receivable	94%	93%
	• Amount of debt-impairment provision	R59 538 677	R51 052 337
	• Amount of accounts receivable	R63 599 384	R54 794 017
Asset and liability management			
3.1	A deficit for the year was realised (total expenditure exceeded total revenue)	Yes	Yes
	• Amount of the surplus / (deficit) for the year	R33 49111 097	R4 038 605

FINANCIAL VIABILITY ASSESSMENT			
		As at 30 June 2020	As at 30 June 2019
3.2	A net current liability position was realised (total current liabilities exceeded total current assets)	Yes	Yes
	• Amount of the net current assets / (liability) position	R123 311 364	R90 340 336
3.3	A net liability position was realised (total liabilities exceeded total assets)	No	No
	• Amount of the net asset / (liability) position	R136 130 928	R169 721 025
Cash management			
4.1	The year-end bank balance was in overdraft	Yes	No
	• Amount of year-end bank balance (cash and cash equivalents) / (bank overdraft)	R2 749 084	R2 590 629
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	R9 289 842	R29 093 147
4.3	Creditors as a percentage of cash and cash equivalents	Bank in overdraft	3329%
	• Amount of creditors (accounts payable)	R108 756 732	R86 231 311
	• Amount of cash and cash equivalents / (bank overdraft) at year-end	(R2 749 084)	R2 590 629
4.4	Current liabilities as a percentage of next year's budgeted resources **	No current liabilities/ 414%	No current liabilities/ 304%
	• Amount of current liabilities	R133 041 563	R110 299 974
	• Amount of next year's budgeted income **	R32 143 000	R36 328 000
Overall assessment			
Overall, the financial viability is assessed as:		Red (unfavourable – intervention required)	Red (unfavourable – intervention required)
* 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 with the financial statement amounts.			

FINANCIAL VIABILITY ASSESSMENT		
	As at 30 June 2020	As at 30 June 2019
<p>** This amount excludes the portion of next year's budgeted resources that is budgeted to be spent on employee costs and remuneration of councillors.</p>		

High-level comments

97. The financial analysis of the municipality performed indicated that the municipality financial viability is concerning and intervention is required due to the following:
98. Creditors payment period exceed the norm of 30 days, which can result in interest and penalties levied against the municipality.
99. Debtor impairment provision accounts for 94% of the total receivables. This indicates that the municipality is experiencing dire challenges with debtor collection which might result in cash flow difficulties, this may also have a possible negative impact on effective and efficient service delivery.
100. The municipality realised deficit in financial year ended 30 June 2020 of R 33 491 097 which increased by R25 512 649 as comparison to prior year.
101. A net current liability position was realised with current liabilities exceeding current assets by R123 311 364. This is due to serious financial constraints and may result in municipality inability to finance short term debts such as funds to be surrendered or payables to suppliers.
102. The non-payment of these payables can result in equitable share withholding that impacts on operational effectiveness and interest and penalties being levied against the municipality further increasing non-compliance with laws and regulations.
103. This high level summary shows that the municipality may not be adequately managing debtors and creditors, and that effective financial management controls are not in place to ensure prompt payments and collections. In addition, this is indicative of or may lead to going concern and financial viability difficulties.

Procurement and contract management

104. The audit included an assessment of procurement processes, contract management and the related controls in place. These processes and controls must comply with legislation to ensure a fair, equitable, transparent, competitive and cost-effective supply chain management (SCM) system and to reduce the likelihood of fraud, corruption, favouritism and unfair and other irregular practices. A summary of the findings from the audit are as follows:

Irregular expenditure

105. R 7 715 091 (5%) of the irregular expenditure incurred in the current financial year was as a result of the contravention of SCM legislation. The root cause of the lack of effective prevention and detection is lack of management oversight over monitoring of controls and compliance with laws and regulations.

Awards to persons in the service of the state

106. Regulation 44 prohibits awards to persons in the service of the auditee (i.e. employees and councillors), 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.

107. The findings were as follows:

Nature of finding	Number and value of awards made	Number and position s of officials/ councillors 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/ accepting the quotation
Awards made to officials of the [municipality]	R5 625	1	1	0	0	1	0
Awards to persons in the service of other state institutions	0	0	0	0	0		

Procurement processes

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

	Total		Quotations		Contracts	
	Number	Value R	Number	Value R	Number	Value R
Awards selected for testing	48	R78 972 776	29	R1 479 853	19	R77 492 923
Expenditure incurred on selected awards – current year		R 40 540 351		R 1139548.18		R 39 400 802
Limitations – awards selected but could not be tested	0	0	0	0	0	0
Awards where non-compliance was identified	9	R10 820 433	3	R 72 897	6	R 10 747 536
Irregular expenditure identified	4	R 546 900	3	R 72 897	1	R 474 003
Instances of irregular expenditure where goods/services were not received	0	0	0	0	0	0

Procurement processes – general

- 3 awards to the value of R72 897 were procured without inviting at least the minimum prescribed number of written price quotations from prospective suppliers and the deviation was not approved by a properly delegated official.
- 1 contract to the value of R 474 003 were procured without inviting competitive bids, and the deviations were approved even though it was practical to invite competitive bids.

- 1 contract awarded to the value of R 270 000 were not approved by an appropriately delegated official/committee.

Contract management

- The performance of 3 contractors or providers was not monitored monthly. The total value of related contracts was R 10 007 492,49.
- The contract performance and monitoring measures and methods applied in monitoring 3 contracts to the value of R 10 007 492,49 were insufficient to ensure effective contract management.

Internal control deficiencies

109. The following project/ contract relates to continued needs of the auditee, and the contracts for the current service providers are ending with the next 6 months and no procurement process has been started for the appointment of a new service provider:

Tender number	Project	Supplier	Contract end date	Contract amount
TLM02/2015	Internet services	PC World	01-Dec-20	2 094 708,56
TLM S32 - 02/2018/19	Compilation Of Fixed Asset Register	Shai Consulting	30-Nov-20	1 776 750,00
				3 871 458,56

110. During the audit of SCM (local content) it was noted that for the following awards under local content Department of trade industry was not notified of the awards made.

1	Dimphororo Consulting (Pty) Ltd	R74 846
2	Manemk	R308 898

111. The following contracts are open ended and do not have expiry dates:

Tender number	Project	Supplier	Details	Contract amount
TLM03/2017/2018	Provision Of Professional Services For The Construction Of Outfall Sewer Line And Upgrading Of Pump Station	BVI CONSULTING	Contract states that agreement will be discharged when the consultant has completed its services.	772 783,20

TLM05/2019/20	Provison For Training Services For 200 Members	INAFRICA GENERAL TRADING	Contract states that the duration of the skills program will be for a period culminating successful completion of the learnership/ skills programme	1 440 000,00
				2 212 783,20

Fraud and consequence management

112. 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 for issuing 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.

113. Below is a summary of fraud risk factors identified during the audit that should be addressed to ensure that sufficient measures/controls are in place to prevent material misstatement/ non-compliance due to fraud.

- Long outstanding reconciling items were identified in the year under review which relate to cash and cash equivalents amounting to R38 428. These relate to revenue that was generated however was never banked. These relate as far back as in 2014. No further action has been taken with regards to the matter.

114. 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

115. 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.
- The municipality did not have a fraud prevention plan.

- A disciplinary board was not established to investigate allegations of financial misconduct and monitor the institution of disciplinary proceedings against an alleged transgressor.
- The disciplinary board was not properly constituted in accordance with the provisions of the Financial Misconduct Regulations.
- There was no hotline or similar process/mechanism for reporting financial misconduct/transgressions that are committed by officials and suppliers of the municipality.
- There was a lack of proper record keeping to ensure that complete, relevant and accurate information is accessible and available to support the processes followed for financial misconduct/transgressions committed by officials and suppliers of the municipality.

Failure to deal properly with allegations reported in the previous year

116. 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	Value R
Unauthorised expenditure	
Unauthorised expenditure identified in the previous year was not investigated to determine whether any person was liable for the expenditure	R122 121 742
Irregular expenditure	
Irregular expenditure identified in the previous year was not investigated to determine whether any person was liable for the expenditure	R133 683 484
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	R30 000 065

Allegations of financial misconduct, fraud and improper conduct in SCM

Finding	Number of instances
Allegations against officials other than senior managers of municipalities	

Finding	Number of instances
Allegations of financial misconduct against officials of the municipality were not investigated	1

117. Unauthorised, irregular, fruitless and wasteful]expenditure disclosed in note 55,56,57 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.

Conditional grants

118. 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
- Finance Management Grant
- Expanded Public works grant
- Integrated National Electricity Programme
- Library Grant

119. No findings were noted with regards to conditional grants

SECTION 5: Using the work of internal auditors

120. The auditing standards allow external auditors the option to use the work of internal audit for external audit purposes and for direct assistance. We have used internal audit as follows:

- The audit team received internal audit reports which were used for risk assessment during the planning phase of the audit. The internal audit unit prepares quarterly reports, all of which were used for risk identification. The scope of the internal audit reports included mainly compliance matters although performance management was also included.
- The scope for financial statements was limited and therefore could not be used for further external audit purposes.

SECTION 6: Emerging risks

Accounting, performance management/reporting and compliance matters

New pronouncements

Standards of Generally Recognised Accounting Practice (GRAP)

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



GRAP pronouncement	Effective date
GRAP 18 on <i>Segment reporting</i>	1 April 2020
GRAP 34 on <i>Separate financial statements</i>	1 April 2020
GRAP 35 on <i>Consolidated financial statements</i>	1 April 2020
GRAP 36 on <i>Investments in associates and joint ventures</i>	1 Apr 2020
GRAP 37 on <i>Joint arrangements</i>	1 April 2020
GRAP 38 on <i>Disclosure of interests in other entities</i>	1 April 2020
GRAP 104 on <i>Financial instruments</i> (revised)	To be determined
GRAP 110 on <i>Living and non-living resources</i>	1 April 2020
IGRAP 20 on <i>Accounting for adjustments to revenue</i>	1 April 2020
Guideline on <i>Accounting for landfill sites</i>	To be determined
Guideline on <i>Application of materiality to financial statements</i>	Voluntary*
* The guideline was issued in April 2019. The guideline is available for immediate consideration to assist entities to apply the concept of materiality when preparing financial statements in accordance with Standards of GRAP. Although the application of the guideline is voluntary, application is encouraged.	

Legislation change

Division of Revenue Act

- Section 33 of the 2019 DoRA states that expenditure of a municipal allocation contrary to the DoRA is irregular expenditure in terms of the MFMA, except if it results in unauthorised expenditure in terms of the MFMA. Municipalities have been disclosing contraventions with section 17(1) of the 2019 DoRA as irregular expenditure in the 2018-19 and 2019-20 financial statements however, National Treasury recently indicated that this should have been disclosed as unauthorised expenditure from the 2018-19 year due to a change in DORA during that year. National Treasury agreed that the irregular expenditure treatment should be accepted for the 2019-20 financial year to remain consistent, however they will be issuing guidance in 2021 to municipalities on how to treat non-compliance findings with section 17(1) of the DORA for the 2020-21 financial year going forward."

Accounting, performance management/reporting and compliance matters

Provision for post-retirement medical aid benefits

- Medical scheme subsidies for retired employees as a condition of service were not covered in the bargaining council collective agreements. We therefore want to inform the municipality of the *Nel & Groenewald v Gariep Local Municipality et al* Case No 2512/2102 Eastern Cape Division of the High Court of South Africa delivered on 13 June 2014 that may create a legal obligation for the municipality based on the



matching arrangement as stipulated in this judgement. Whilst this judgment is binding in the Eastern Cape province only, it will have persuasive authority in the Northern Cape High Court, as this arrangement was in place and applicable when the Eastern Cape province and the Northern Cape province prior to 1994 were part of the greater Province of the Cape of Good Hope, and such matching arrangement are then also be applicable in the successors-in-law. The municipality should assess the impact of the matching arrangement in this judgement on their provision for post-retirement medical aid benefits and where needed adjustments must be made. It is then further recommended that the municipality should ensure that it has a council policy in place that is in line with the matching arrangement and the council policy should also clearly state if senior managers are eligible for this benefit as they are excluded from the bargaining council collective agreements.

- As this is a complex legal and technical matter the municipality should get an opportunity to assess the impact of the legal aspects on their provision. The timing of this matter does not allow sufficient time for the municipality to assess the legal impact and make adjustments where needed during the 2019-20 audit. Furthermore, consistent treatment in the province should be ensured and therefore this matter will be followed up during the next audit cycle.

Subsequent events

121. There were no subsequent events that were identified.

SECTION 7 : Ratings of detailed audit findings

122. 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.

Separate annexure will be issued separately once also issues have been finalized.

SECTION 8 : Conclusion

123. 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 remain 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 sincerely



Sizwe Buthelezi

Senior Manager: Northern Cape Business Unit

31 March 2021

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Audit committee
Head of internal audit unit
Executive authority

Annexure D: Performance management and reporting framework

The performance management and reporting framework (PMRF) consists of the following:

- Legislation applicable to performance planning, management and reporting, which includes the following:
 - MFMA
 - Municipal Systems Act 32 of 2000 (MSA)
 - Regulations for planning and performance management, 2001, issued in terms of the MSA.
 - Municipal performance regulations for municipal managers and managers directly accountable to municipal managers, 2006, issued in terms of the MSA.
- The Framework for Managing Programme Performance Information (FMPPI), issued by the National Treasury. This framework is applicable to all spheres of government, excluding Parliament and provincial legislatures.
- Circulars and guidance issued by the National Treasury regarding the planning, management, monitoring and reporting of performance against predetermined objectives.

Annexure D – Criteria developed from the performance management and reporting framework

Criteria	References to PMRF per institution	
	Municipalities	Municipal entities
Consistency: Objectives, performance indicators and targets are consistent between planning and reporting documents.		
1. Reported strategic or development objectives are consistent or complete when compared to planned objectives.	Section 121(3)(f) of the MFMA Sections 41(a) – (c) & 46 of the MSA	Section 121(4)(d) of the MFMA
2. Changes to strategic or development objectives are approved	Section 25(2) of the MSA	Section 54(1)(c) of the MFMA
3. Reported indicators are consistent or complete when compared to planned indicators	Section 121(3)(f) of the MFMA Sections 41(a) – (c) & 46 of the MSA	Section 121(4)(d) of the MFMA
4. Changes to indicators are approved	Section 25(2) of the MSA	Section 54(1)(c) of the MFMA
5. Reported targets are consistent or complete compared to planned targets	Section 121(3)(f) of the MFMA Sections 41(a) – (c) & 46 of the MSA	Section 121(4)(d) of the MFMA
6. Changes to targets are approved	Section 25(2) of the MSA	Section 54(1)(c) of the MFMA
7. Reported achievements are consistent with the planned and reported indicator and target	Section 121(3)(f) of the MFMA	Section 121(4)(d) of the MFMA
Measurability: Performance indicators are well defined and verifiable, and targets are specific, measurable and time bound		




Criteria	References to PMRF per institution	
	Municipalities	Municipal entities
1. A performance indicator is well defined when it has a clear, unambiguous definition so that data will be collected consistently and is easy to understand and use.	Chapter 3.2 of the FMPPi	
2. A performance indicator is verifiable when it is possible to validate or verify the processes and systems that produce the indicator.	Chapter 3.2 of the FMPPi	
3. A target is specific when the nature and required level of performance of the target are clearly identifiable.	Chapter 3.3 of the FMPPi	
4. A target is measurable when the required performance can be measured.	Chapter 3.3 of the FMPPi	
5. A target is time bound when the timeframes for achievement of targets are indicated.	Chapter 3.3 of the FMPPi	
Relevance: Performance indicators relate logically and directly to an aspect of the institution's mandate and the realisation of its strategic goals and objectives		
1. The performance indicator and target relate logically and directly to an aspect of the institution's mandate and the realisation of its strategic goals and objectives.	Chapter 3.2 of the FMPPi	
Presentation and disclosure: Performance information in the annual performance report is presented and disclosed in accordance with the requirements contained in the legislation, frameworks, circulars and guidance		

Criteria	References to PMRF per institution	
	Municipalities	Municipal entities
1. Actual performance compared to planned targets and prior year performance is disclosed in the annual performance report	Section 46 of the MSA	Section 46 of the MSA
2. Measures taken to improve performance are disclosed in the annual performance report	Section 46 of the MSA	Section 46 of the MSA
3. Measures taken to improve performance are corroborated with audit evidence	Section 46 of the MSA	Section 46 of the MSA
Reliability: Recording, measuring, collating, preparing and presenting information on actual performance achievements is valid, accurate and complete.		
1. Reported performance occurred and pertains to the reporting entity.	Section 45 of the MSA	Section 45 of the MSA
2. Amounts, numbers and other data relating to reported performance are recorded and reported correctly.	Chapter 5 of the FMPPI	Chapter 5 of the FMPPI
3. All actual performance that should have been recorded is included in the reported performance information.		




Annexure F: Assessment of internal controls




Below is our assessment of the implementation of drivers of internal control based on significant deficiencies identified during our audit of the financial statements, the [annual performance report/ insert name of performance report] and compliance with legislation. Significant deficiencies occur when internal controls do not exist, are not appropriately designed to address the risk, or are not implemented. These either had caused, or could cause, the financial statements or the [annual performance report/ insert name of performance report] to be materially misstated, and material instances of non-compliance with legislation to occur.





































The internal controls were assessed as follows:

	The required preventative or detective controls were in place.
	Progress was made on implementing preventative or detective controls, but improvement is still required, or actions taken were not or have not been sustainable.
	Internal controls were not in place, were not properly designed, were not implemented or were not operating effectively. Intervention is required to design and/or implement appropriate controls.







The movement in the status of the drivers from the previous year-end to the current year-end is indicated collectively for each of the three audit dimensions under the three fundamentals of internal control. The movement is assessed as follows:

	Improved
	Unchanged
	Regressed

	Financial statements		Performance reporting		Compliance with legislation	
	Current year	Prior year	Current year	Prior year	Current year	Prior year
Leadership						
Overall movement from previous assessment						

	Financial statements		Performance reporting		Compliance with legislation	
	Current year	Prior year	Current year	Prior year	Current year	Prior year
• Provide effective leadership based on a culture of honesty, ethical business practices and good governance, and protecting and enhancing the best interests of the entity						
• Exercise oversight responsibility regarding financial and performance reporting and compliance as well as related internal controls						
• Implement effective human resource management to ensure that adequate and sufficiently skilled resources are in place and that performance is monitored						
• Establish and communicate policies and procedures to enable and support the understanding and execution of internal control objectives, processes and responsibilities						
• Develop and monitor the implementation of action plans to address internal control deficiencies						
• Establish and implement an information technology governance framework that supports and enables the business, delivers value and improves performance						
Financial and performance management						
Overall movement from previous assessment						

	Financial statements		Performance reporting		Compliance with legislation	
	Current year	Prior year	Current year	Prior year	Current year	Prior year
• Implement proper record keeping in a timely manner to ensure that complete, relevant and accurate information is accessible and available to support financial and performance reporting	☹	☹	☹	☹	☹	☹
• Implement controls over daily and monthly processing and reconciling transactions	☹	☹	☹	☹	☹	☹
• Prepare regular, accurate and complete financial and performance reports that are supported and evidenced by reliable information	☹	☹	☹	☹	☹	☹
• Review and monitor compliance with applicable legislation	☹	☹	☹	☹	☹	☹
• Design and implement formal controls over information technology systems to ensure the reliability of the systems and the availability, accuracy and protection of information	☹	☹	N/A	N/A	N/A	N/A
Governance						
Overall movement from previous assessment						
• Implement appropriate risk management activities to ensure that regular risk assessments, including the consideration of information technology risks and fraud prevention, are conducted and that a risk strategy to address the risks is developed and monitored	☹	☹	☹	☹	☹	☹

	Financial statements		Performance reporting		Compliance with legislation	
	Current year	Prior year	Current year	Prior year	Current year	Prior year
• Ensure that there is an adequately resourced and functioning internal audit unit that identifies internal control deficiencies and recommends corrective action effectively						
• Ensure that the audit committee promotes accountability and service delivery through evaluating and monitoring responses to risks and overseeing the effectiveness of the internal control environment, including financial and performance reporting and compliance with legislation	