

Report of the Auditor-General to the Limpopo Provincial Legislature and the council of the Greater Tzaneen Local Municipality

Report on the financial statements

Introduction

1. I have audited the financial statements of the Greater Tzaneen Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2014; the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget information with actual information for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA), Division of Revenue Act of South Africa, 2013 (Act No.02 of 2013) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on these separate financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements, and plan and perform the audit to obtain reasonable assurance about whether the separate financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the separate financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the separate financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the separate financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the separate financial statements.

5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for qualified opinion

Cash flow statement

6. GRAP 2, *Cash flow statements*, requires that the municipality summarises the entity's operating, investing and financing activities. The municipality did not correctly prepare and present the cash flow statement in accordance with GRAP 2, *Cash flow statements*. Consequently the cash flow statements was not properly prepared and presented as a result of the following:
 - Cash flow from operating activities includes non-cash items as "cash received from trade services and assessment rates" amounting to R399 366 132 (2013: R 357 386 419) represented by billed items not cash.
 - Interest income to the amount of R19 507 567 includes an unknown amount charged to water and sewerage debtors which is collected on behalf of Mopani District Municipality.
 - Cash received from agency fees, fines and sundry income include unquantified non-cash items.

Revenue

7. The municipality did not fully recognise revenue from fines issued amounting to R14 639 293 on a gross basis as required by IGRAP 1, *Applying probability test on initial recognition of revenue*. In addition, I have identified that fines for three months were not recorded in the municipality's traffic management system and rates charged for speeding fines were not in line with magistrate charge books. I was unable to obtain sufficient appropriate audit evidence by alternative means, to satisfy myself that all fines have been recorded and that the municipality is entitled to all fines recorded. Consequently, fines received amounting to R3 665 353 and receivables from non-exchange transactions amounting to R423 657 as disclosed in note 7 to the financial are misstated with an unquantifiable amount.

Receivables

8. The Standard of Generally Recognised Accounting Practice, GRAP 104, *financial instruments*, requires the municipality to assess whether a financial asset or a group of financial assets are impaired. The assessment should firstly be performed on individually significant financial assets and thereafter on a group of financial assets with similar credit risk characteristics. I could not obtain appropriate audit evidence that the municipality assessed individually significant receivables for impairment and, as a result I could not ascertain whether all receivables that should have been impaired are impaired. Consequently, I was unable to determine the correct of provision for impairment relating to consumer debtors of R160 557 340 (2013: R142 161 652) as disclosed in note 8 to the financial statements as it was impracticable to do so.
9. The municipality did not have adequate systems in place to maintain records of water and sewerage transaction services performed on behalf of Mopani District Municipality. My audit revealed that the receivable from the district municipality as per their financial

statements does not agree with payable balance disclosed by the district municipality in their 2013-14 financial statements. In addition, I have identified that the municipality did not account for all transactions receivable from the district municipality. I was unable to obtain sufficient appropriate audit evidence by alternative means. Consequently, the year-end debtors balance of R179 180 196 (2013: R185 703 876) as disclosed in note 6 to the financial statements was understated by R63 526 778.

Contingent Liabilities

10. The municipality did not submit appropriate audit evidence to substantiate contingent liabilities of R28 219 943 as disclosed in note 39 to the financial statements. I was unable to verify the reported amounts by alternative means. Consequently, I was unable to determine whether any adjustment to the financial statements was necessary.

Aggregation of Immaterial Uncorrected Misstatements

11. The financial statements as a whole are materially misstated due to the cumulative effect of numerous individually immaterial uncorrected misstatements in the following elements making up the statement of financial performance and financial position.
 - Debt impairments as R21 745 127 is overstated by R3 762 02;
 - Cash and cash equivalents reflected as R23 822 041 its overstated by R81 596;
 - Receivables from exchange transactions reflected as R194 302 064 is understated by R15 256 889;
 - Provisions reflected as R2 614 676 is overstated by R567 971;
 - Other financial liabilities stated as R12 014 682 is overstated by R1 354 999;
 - Property, plant and equipment amounting to R1 571 005 could not be physically verified;
 - Property, plant and equipment reflected as R1 693 376 434 is understated by R1 691
 - The movement in the staff leave provision reflected as R19 078 709 is overstated by R4 012 807;
 - Consumer deposits reflected as R18 436 179 is understated by R3 250 778;
 - Depreciation and amortisation reflected as R108 054 907 is understated by R4 462 661;
 - General expenses reflected as R57 574 447 139 is overstated by R3 042 641;
 - Investment property reflected as R810 377 000 is understated by R510 000;
 - Payables from exchange transactions reflected as R145 771 377 is overstated by R554 488;
 - Service charges reflected as R362.004 404 is understated by R1 748 470;
 - Donation revenue reflected as R155 300 000 is overstated by R1 200 000;
 - Employee cost reflected as R247 063 561 is overstated by R2 231 464;

In addition, I was unable to obtain sufficient appropriate audit evidence and to confirm the following items by alternative means:

- Interest income reflected as R19 507 567 includes an unknown amount of interest charged to water and sewerage debtors witch is collected on behalf of Mopani District Municipality;

- Journals posted in trade payables in exchange transactions and revenue amounting to R6 910 668;
- I was unable to verify the assets amounting to R2 721 528 recorded in the asset register without a physical location;

As a result, I was unable to determine whether any further adjustment to these items was necessary.

Opinion

12. In my opinion, except for the effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Tzaneen Municipality as at 30 June 2014 and its financial performance and cash flows for the year then ended, in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

13. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

14. As disclosed in note 48 to the financial statements, the corresponding figures for 30 June 2013 have been restated as a result of errors discovered during 2014 in the financial statements of the municipality at, and for the year ended, 30 June 2013.

Material underspending of conditional grants

15. With reference to note 18 to the financial statements, the municipality materially underspent its conditional grants by R44 079 480.

Material Uncertainty

16. With reference to note 39 to the financial statements, the municipality is the defendant in several lawsuits. The ultimate outcome of the matters cannot presently be determined and no provision for any liability that may result has been made in the financial statements.

Material Losses

17. As disclosed in note 49 to the financial statements, material losses of 75 262 387 units of electricity (20.39%) and (2013: 65 302 840 units 17.44%) were incurred as a result of electricity distribution losses.

Additional matter

18. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited supplementary schedules

19. 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.

Unaudited disclosure notes

20. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

Report on other legal and regulatory requirements

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

Predetermined objectives

22. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development objectives presented in the annual performance report of the Greater Tzaneen Municipality for the year ended 30 June 2014:
 - Objective x 1: Improve access to sustainable and affordable services on pages 27 to 35.
23. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
24. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned development objectives. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's Framework for managing programme performance information (FMPPi).
25. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
26. The material findings in respect of the selected development objectives are as follows:

Improve access to sustainable and affordable services

Usefulness of reported performance information

27. No reasons for variances between planned and actual achievements reported in the annual performance report were provided for 25% of the targets not achieved, as

required by the National Treasury's Guide for the preparation of the annual report. This was due to a lack of documented and approved internal policies and procedures to address reporting requirements and a lack of review of the presented annual performance report by management.

28. Performance targets must be measurable. I could not measure the required performance for 33% of the targets in relation to the selected development objectives.
29. Performance indicators/measures must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 33% of the indicators were not well defined.
30. Performance indicator/measures must be verifiable, meaning that it must be possible to validate the processes and systems that produced the indicator/measure. A total of 33% of the indicators/measures were not verifiable. This was due to the lack of monitoring and review of reported performance.

Reliability of reported performance information

31. The FMPPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. Significantly important targets were not reliable when compared to the source information or evidence provided. This was due to a lack of standard operating procedures for the accurate recording of actual achievements for the accurate measurement and monitoring of the completeness of source documentation in support of actual achievements and frequent review of the validity of reported achievements against source documentation.

Additional matter

32. Although I raised no material findings on the usefulness and reliability of the reported performance information for the selected development objectives, I draw attention to the following matters:

Achievement of planned targets

33. Refer to the annual performance report on page XX to XX for information on the achievement of the planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information for the selected development objectives reported in paragraphs XX to XX of this report.
34. The supplementary information set out on pages XX to XX does not form part of the annual performance report and is presented as additional information. I have not audited this schedule and, accordingly, I do not report thereon.

Compliance with laws and regulations

35. I performed procedures to obtain evidence that municipality had complied with legislation regarding financial matters, financial management and other related matters. Our findings on material non-compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Financial statements, performance and annual reports

36. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the Municipal Finance Management Act.
37. Material misstatements of non-current assets, current assets, liabilities, revenue and expenditure identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.

Audit committees

38. The audit committee did not submit, at least twice during the financial year, an audit report on the review of the performance management system to the council, as required by Municipal planning and performance management regulation 14(4)(a)(iii).
39. The audit committee did not review the municipality's performance management system and make recommendations to the council, as required by Municipal planning and performance management regulation 14(4)(a)(ii).
40. The audit committee did not review all the quarterly internal audit reports on performance measurement, as required by Municipal planning and performance management regulation 14(4)(a)(i).

Procurement and contract management

41. Awards were made to providers whose directors are in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulations 44. Similar awards were identified in the prior year and no effective steps were taken to prevent or combat the abuse of the SCM process in accordance with SCM regulation 38(1).

Expenditure management

42. Money owed by the municipality was not always paid within 30 days on an agreed period, as required by section 65(2)(e) of the Municipal Finance Management Act.
43. An effective system of expenditure control, including procedures for the approval of funds, was not in place, as required by section 65(2)(a) of the Municipal Finance Management Act.
44. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the Municipal Finance Management Act.

Budgets

45. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the Municipal Finance Management Act.

Internal control

46. We considered internal control relevant to our audit of the financial statements, annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for qualified opinion, the findings on the annual performance report and the findings on non-compliance with legislation included in this report.

Leadership

47. Oversight responsibility regarding financial and performance reporting and compliance and related internal controls was not exercised.

Financial and performance management

48. The financial statements and other information to be included in the annual report are not reviewed for accuracy and completeness by the accounting officer.
49. Controls over daily and monthly processing and reconciling of transactions were not implemented by the accounting officer.
50. Compliance with laws and regulations was not reviewed and monitored by the accounting officer.

Auditor-General

Polokwane

19 December 2014



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence