



General report on the local government audit outcomes of the **EASTERN CAPE**



EASTERN CAPE MFMA 2013-14

Our reputation promise/mission

The Auditor-General of South Africa has a constitutional mandate and, as the Supreme Audit Institution (SAI) of South Africa, exists to strengthen our country's democracy by enabling oversight, accountability and governance in the public sector through auditing, thereby building public confidence.



The information and insights presented in this flagship publication are aimed at empowering oversight structures and local and provincial government leaders to focus on those issues that will result in reliable financial statements, credible reporting on service delivery and compliance with legislation.

This publication also captures the commitments that leaders have made to improve audit outcomes.

I wish to thank the audit teams from my office and the audit firms that assisted with the auditing of local government for their diligent efforts towards fulfilling our constitutional mandate and the manner in which they continue to strengthen cooperation with the leadership of the province.

Auditor-General

Kimi Makwetu
Auditor-General



**AUDITOR - GENERAL
SOUTH AFRICA**

HIGHLIGHTS

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The Sarah Baartman district and Senqu are the first two municipalities to achieve clean audits in the province (4%) (Section 1)

A total of 27% of municipalities received unqualified audit opinions by correcting the material misstatements found in their financial statements during the audit process (Section 2)



Non-compliance with key legislation remains high (Section 5)

Very few municipalities have good financial viability indicators (Section 9)



The quality of the annual performance reports has regressed (Section 4)

Municipalities continue to rely on consultants, and their management of this resource is weak (Section 7)



The political and administrative leadership are slow to address the root causes of poor audit outcomes (Sections 13 - 14)

The auditor-general reflects on the importance of clean administration as a catalyst to drive service delivery

EASTERN CAPE CLEAN AUDITS 2013-14



MUNICIPALITY

Sarah Baartman district
Senqu



MUNICIPAL ENTITY

Mandela Bay Development Agency

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FOREWORD

FOREWORD

It is my pleasure to present to the legislature and municipal councils of the Eastern Cape my general report on the audit outcomes of the Eastern Cape local government for the year ended 30 June 2014.

On launching operation clean audit in September 2009, the then Minister of Cooperative Governance and Traditional Affairs used the 2007-08 financial year as a baseline. Operation clean audit entailed all municipalities achieving unqualified audits by 2014. While it is acknowledged that 33% of the municipalities in the province attained this milestone, there is still a long way to go before all municipalities achieve an unqualified audit outcome. My definition of clean audit elevated that of operation clean audit to unqualified audit outcomes without findings on compliance and performance reporting. Only the Sarah Baartman and Senqu municipalities have reached this milestone.

The province has made some strides towards improving its audit outcomes over the last seven years and has recorded a net improvement in 19 municipal audit outcomes. I am, however, concerned that these positive movements have been negated by perpetual regressions. Almost all municipalities in the province were still not able to submit credible and reliable financial statements, which then required material amendments during the audit process. These municipalities manage 99% of the provincial budget, creating a risk that funds may not be used in an economical, effective and efficient manner that enhances return on investment. Of particular concern within this group are the two metros, which administer a combined budget of R15 billion that represents 44% of the total provincial municipal budget

Another critical function of local government is to plan, monitor and report on service delivery to communities. However, municipalities have not positioned themselves to appropriately perform this function. As a result, the majority of annual performance reports are not credible.

In addition, the province is still plagued by irregular and unauthorised expenditure of R3,36 billion and R2,1 billion respectively, which the leadership is unable to prevent. I am particularly concerned about the high level of supply chain management transgressions driven by uncompetitive or unfair procurement processes, conflicts of interests and internal control failures. This not only translates into high irregular expenditure, but also provides very little assurance that value for money was received from the acquisition of goods and services.

I am also concerned about council's failure to adequately investigate this expenditure and establish the necessary accountability, as required by legislation. All levels of leadership should set the tone by dealing decisively with transgressions of applicable legislation. This will build the ethical culture required to ensure sustained compliance with legislation and the economical, effective and efficient delivery of services to the citizens of the Eastern Cape.

The weak information technology controls highlighted in this report not only increase the risk of fraud at municipalities in the province, but also threaten to undermine the sustainability of the improved audit outcomes experienced by the local government sector in the province. These controls require urgent attention.

Only three municipalities in the province had positive financial viability risk indicators. The poor financial viability of municipalities can have a negative impact on their ability to respond to the service delivery needs of the communities that

they serve. Urgent leadership attention is required to place these municipalities on a path to financial viability and sustainability.

The control weaknesses in all the key areas referred to above are exacerbated either by the lack of action or the lack of real impact where actions have commenced. It is evident that most municipalities often directed their efforts at addressing the symptoms or isolated risks that are raised by the audit rather than the root causes of audit outcomes. At the heart of this, evidenced by the status of the drivers of internal controls, is a lack of decisive action and monitoring of various improvement plans.

The leadership is reminded of the following characteristics common to those auditees that have achieved a clean audit status in both the provincial and local government spheres. These characteristics have enabled effective oversight:

- a. Accounting officers were proactive in driving action plans to improve the financial control environment and to instil a culture of good financial governance and compliance with legislation.
- b. Executive authorities and accounting officers set a tone of zero tolerance for non-performance and held staff accountable.
- c. Robust and proactive audit committees and internal audit units dealt effectively with matters regarding implementing and monitoring action plans to address recurring findings and the commitments made.
- d. Accounting officers and senior management successfully implemented basic internal controls and disciplines by preparing regular and accurate financial statements and performance reports.

- e. Stability is maintained at senior management level and within finance units, with the required level of technical competence and experience.

Notably, these characteristics were observable in less than a handful of municipalities in the province. A significant effort is required to turn this situation around.

The challenge remains for the province to build a public service characterised by transparent financial and performance reporting. This should be led by municipal managers with the councils' support and oversight. Municipal managers must appreciate ethical and professional behaviour; and have zero tolerance towards the indecisive execution of controls and deviation from legislation. In support, the Office of the Premier must strengthen intergovernmental relations to ensure that all public institutions that have a role to play within local government are adequately coordinated. This would include the oversight of the two coordinating departments, the Department of Cooperative Governance and Traditional Affairs and the provincial treasury, which have a direct bearing on municipalities' functions.

We are encouraged by the commitments received from the political leadership in the province to improve the audit outcomes in the local government sector. These commitments include the province working closely, mentoring and collaborating with municipalities and improving coordination among all role players in provincial initiatives. The leadership has also committed to focus on capacitating district municipalities to improve their own and their local municipalities' audit outcomes and providing funding for focused assistance to poor performing municipalities.

My staff and I remain committed to working with the municipal and provincial leadership to further improve governance and accountability, so as to build public confidence in the local government sector and in the province's ability to account for public resources in a transparent manner.

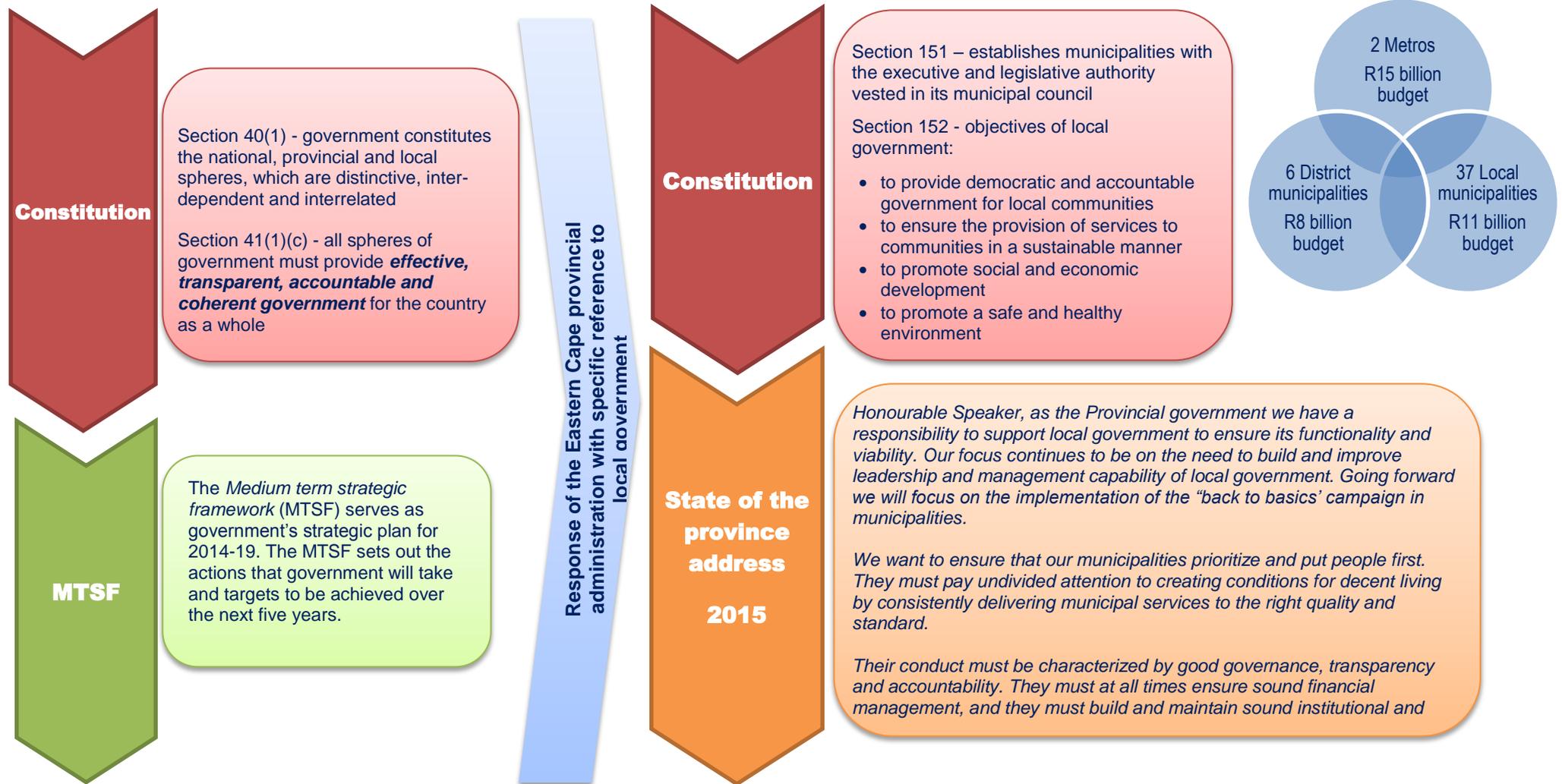
I wish to thank all the teams from my office and the audit firms that assisted us for their diligent efforts towards fulfilling our constitutional mandate and the manner in which they continue to strengthen cooperation with the leadership of the province.

Auditor-General
Pretoria
8 June 2015

INTRODUCTION 9

The government and its strategies

The Constitution of South Africa is the supreme law of the country. It provides the legal foundation for the existence of the republic, sets out the rights and duties of its citizens, and defines the structure of the government. The spirit and aim of the Constitution is best summarised in the preamble, where it pronounces the ultimate goal - **Improve the quality of life of all citizens and free the potential of each person**. This foundation of our society, the Constitution, appoints government as the facilitator and enabler of this goal. The illustration depicts the basic operations of government that give effect to the Constitution.



Historical overview of local government initiatives

Operation clean audit 2014

On 22 September 2009, responding to the findings of a government study into the problem areas of service delivery, *leadership*, *financial management*, and matters of governance, the Minister of Cooperative Governance and Traditional Affairs (CoGTA) launched operation clean audit 2014.

During his address to Parliament, the minister highlighted the particular focus on local government as the closest to the coalface of service delivery. He summarised the pre-2009 status as follows:

The then DPLG, did not support provincial departments. As a result, the link and support between municipalities and provinces was weak and not sustainable. Thus, service delivery, governance and financial management were severely affected. Technically, when a system of governance and financial management is poor due to lack of support, without a doubt service delivery will be negatively affected. More importantly, in some provincial departments and municipalities, there is lack of both administrative and political leadership.

The initiative aimed at ensuring that by 2014, all municipalities and provincial government departments in South Africa achieve clean audits on their financial statements and that they further **maintain systems for sustaining quality financial statements and management information**. In this address the following milestones were set:

- By 2011 no municipality will receive adverse and disclaimed audit opinions.
- By 2012 at least 60% of municipalities must achieve unqualified audit opinions
- By 2013 this must increase to 75% of municipalities that achieve unqualified audits.
- By 2014 we must have 100% of 'clean audits'

Back-to-basics programme 2015

President Jacob Zuma, in his *State of the nation* address delivered on 17 June 2014, articulated government's concerns about the improvements needed at local government level: *We would like our people's experience of local government to be a pleasant one.*

Against this background, the Ministry of CoGTA is pursuing the back-to-basics approach to address challenges faced by local government, strengthen municipalities and instil a sense of urgency towards improving citizens' lives. At a very basic level, municipalities are expected to:

- put people and their concerns first and ensure constant contact with communities through effective **public participation** platforms.
- create conditions for decent living by consistently delivering municipal **services of the right quality and standard**. This includes planning for, delivering and maintaining infrastructure and amenities, and managing the budget.
- ensure that there are no failures in services and, where these occur, urgently restore services.
- be well governed and demonstrate **good governance and administration - cut wastage, spend public funds prudently, hire competent staff, ensure transparency and accountability**
- ensure sound **financial management** and accounting, and prudently manage resources to sustainably deliver services and bring development to communities.
- build and maintain sound institutional and administrative capabilities, administered and managed by dedicated and skilled personnel at all levels

The AGSA has a constitutional mandate and, as the SAI of South Africa, exists to strengthen our country's democracy by enabling oversight, accountability and governance in the public sector through auditing, thereby building public confidence.

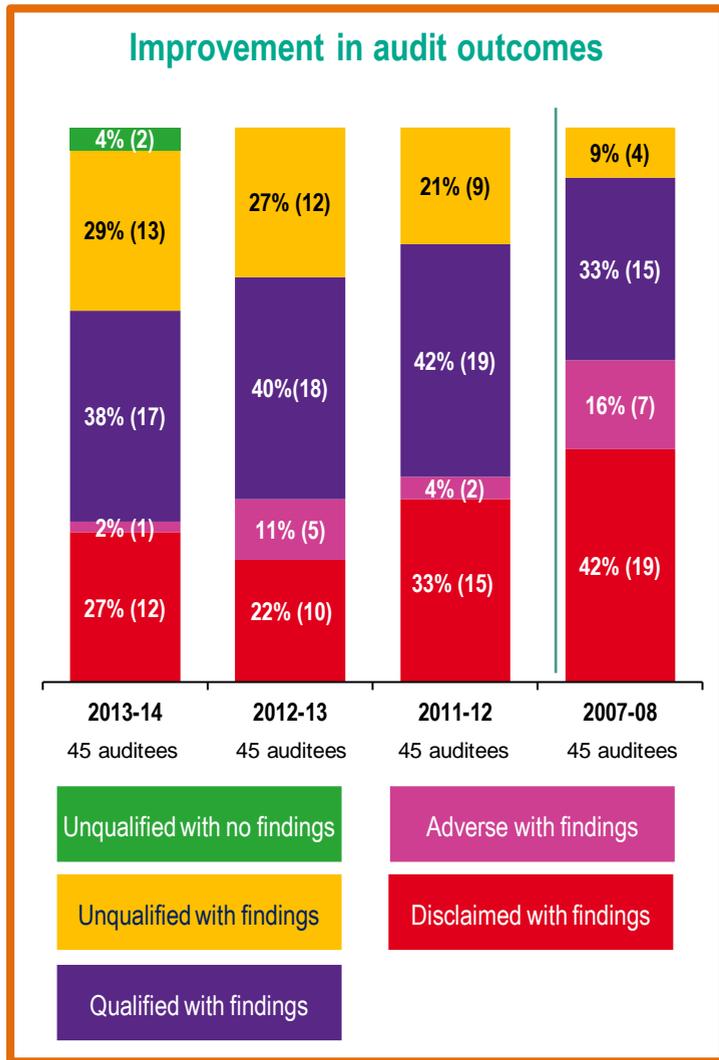
In support of CoGTA's operation clean audit, the AGSA intensified interactions with both the political and administrative leadership on the outcomes of their municipalities, the root causes underpinning the unfavourable outcomes and the need for a strong control environment entrenched in daily, weekly and monthly processes. The previous auditor-general also embarked on a door-to-door campaign, where he visited each municipality in the country with a message of support and where he highlighted that ***it is possible to obtain clean administration if there is true political will to change and if the leadership actively strives for quality and sustainability in executing its duties.***

The AGSA is committed to being a critical supporter of the back-to-basics initiative.

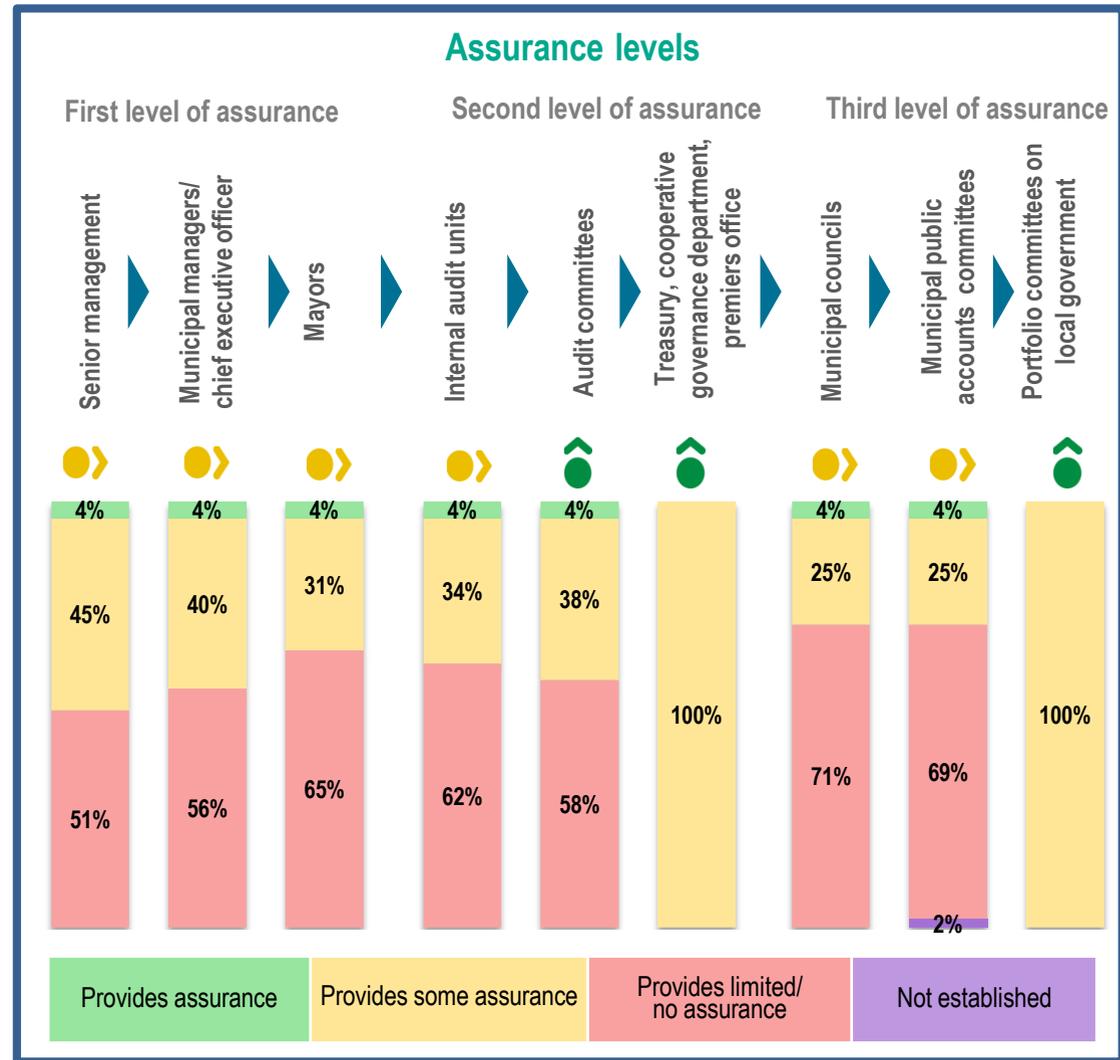
OVERVIEW

Summary of our message

Figure 1a: Overview of the audit message



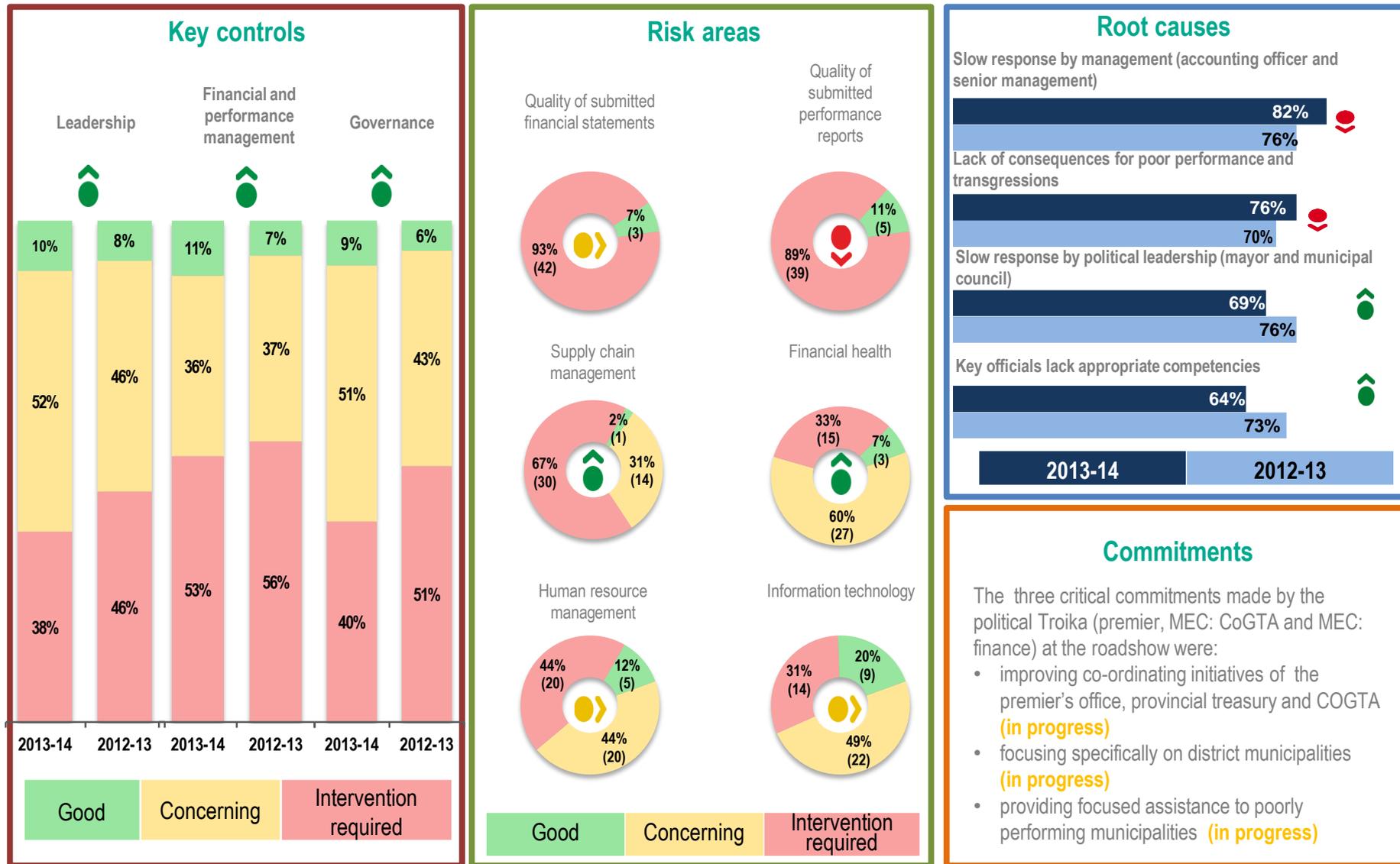
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To improve/maintain the **audit outcomes**, the key role players need to ...

Figure 1b: Overview of the audit message



3

4

5

... attend to the **key controls**, the **risk areas** and the **root causes**.

Characteristics of each of the categories of audit outcomes

Table 1 summarises the characteristics of auditees that fall within the different categories of audit outcomes over the following pages. This summary is provided to achieve the following:

- Assist the reader to understand the different audit outcomes.
- Highlight the good practices of auditees with clean audit opinions.
- Emphasise that auditees with an unqualified audit opinion with findings still have serious weaknesses that should be dealt with.
- Explain why auditees with qualified, adverse and disclaimed opinions are failing.

Table 1: Characteristics of auditees within the different categories of audit outcomes

Area	Best practices for clean audits (2)	Unqualified with findings (13)	Qualified with findings (17)	Adverse or disclaimed with findings (13)
<i>Financial statements</i>	Auditees produced financial statements that were free from material misstatement .	<p>Twelve auditees (92%) produced financial statements with material misstatements, but corrected these during the audit process.</p> <p>The most common areas in which auditees made corrections were:</p> <ul style="list-style-type: none"> • property, infrastructure and equipment • contingent liabilities and commitments • unauthorised and irregular expenditure. 	<p>Auditees produced financial statements with material misstatements that they could not correct before the financial statements were published.</p> <p>The most common areas that they could not correct were:</p> <ul style="list-style-type: none"> • unauthorised, irregular as well as fruitless and wasteful expenditure • property, infrastructure and equipment • other disclosure items. 	<p><u>Adverse (1)</u>: Auditees produced financial statements that included so many material misstatements that we disagreed with almost all the amounts and disclosures in the financial statements.</p> <p><u>Disclaimed (12)</u>: Auditees could not provide us with evidence for most of the amounts and disclosures in the financial statements. We were unable to conclude or express an opinion on the credibility of their financial statements.</p>
<i>Annual performance report</i>	Auditees measured and reported on their performance (in the annual performance report) in line with the predetermined objectives in their integrated development plans and service delivery and budget implementation plans, and in a manner that was useful and reliable .	<p>The annual performance reports of seven municipalities (54%) were not useful and/or reliable.</p> <p>Three municipalities (27%) obtained good outcomes only because they corrected the misstatements identified during the audit.</p>	The annual performance reports of 16 municipalities (94%) were not useful and/or reliable .	<p>One municipality (8%) did not prepare an annual performance report.</p> <p>The annual performance reports of 13 municipalities (100%) were not useful and/or reliable.</p>

Area	Best practices for clean audits (2)	Unqualified with findings (13)	Qualified with findings (17)	Adverse or disclaimed with findings (13)
Compliance with key legislation	<p>Auditees complied with key legislation.</p>	<p>Thirteen auditees (100%) did not comply with key legislation.</p> <p>The only material instance of non-compliance reported at the Joe Gqabi district was the poor quality of the financial statements submitted for auditing. It would have received a clean audit outcome had it not been for this compliance finding.</p>	<p>Seventeen auditees (100%) did not comply with key legislation.</p>	<p>Thirteen auditees (100%) did not comply with key legislation.</p>
Controls	<p>Auditees had good controls or were working on the areas that needed further attention to ensure that they maintained their clean audit status:</p> <ul style="list-style-type: none"> The leadership created an environment conducive to internal control and oversight (83% of auditees). Senior management ensured that controls were in place for robust financial and performance management reporting systems (90%). Auditees focused on governance through risk management activities and effective internal audit units and audit committees (100%). 	<p>Auditees had good controls in some areas but should pay attention to the following basic controls. A limited number of auditees had good controls in these areas:</p> <ul style="list-style-type: none"> Effective leadership culture (31%) Good human resource management controls (23%) Good information and communication technology (ICT) governance and controls (0%) Effective audit action plans (31%) Proper record keeping (31%) Strong daily and monthly controls (23%) Review and monitor compliance (0%). 	<p>No auditees had good controls in the following areas:</p> <ul style="list-style-type: none"> Effective leadership culture Human resource management ICT governance Effective audit action plans Proper record keeping Strong daily and monthly controls Reviewing and monitoring compliance. 	<p>The basic controls were weak. We assessed the status of controls at most of these auditees as 'intervention required'.</p> <p>The weakest controls were in the following areas:</p> <ul style="list-style-type: none"> Review and monitor compliance (100% needed intervention) Daily and monthly controls (100% needed intervention) Proper record keeping (92% need intervention) Human resource controls (92% need intervention).

Area	Best practices for clean audits (2)	Unqualified with findings (13)	Qualified with findings (17)	Adverse or disclaimed with findings (13)
Controls	<p>Their continued focus on these basic controls contributed to their success:</p> <ul style="list-style-type: none"> • The leadership established a culture of ethical behaviour, commitment and good governance (100% had good controls). • Good human resource practices ensured that adequate and sufficiently skilled officials were in place and that their performance was managed (100% had good controls). • Audit action plans were used to address internal control weaknesses (100% had good controls). • Proper record keeping ensured that information was accessible and available to support financial and performance reporting (100% had good controls). • Basic disciplines and controls were in place for daily and monthly processing and reconciling transactions (100% had good controls). • Mechanisms were in place to identify applicable legislation, changes and processes to ensure and monitor compliance with legislation (100% had good controls). 			

Area	Best practices for clean audits (2)	Unqualified with findings (13)	Qualified with findings (17)	Adverse or disclaimed with findings (13)
Assurance providers	<p>Key role players worked together to provide assurance on the credibility of the financial statements and performance reports and to ensure compliance with key legislation.</p> <p>These auditees understood that assurance on the credibility of the information in the financial statements and performance reports came primarily from the actions of management/leadership and their governance partners – internal audit units and audit committees.</p> <p>Their political leadership provided strong monitoring and oversight and held the administration to account.</p> <p>Full assurance was provided by all role players at both municipalities.</p>	<p>Not all role players provided the required level of assurance. As a result, the financial statements and/or annual performance reports prepared, reviewed and signed off by senior management and the municipal manager of these auditees were materially misstated.</p> <p>The internal audit units and the audit committees did not add to the credibility of these reports, while monitoring and oversight by the political leadership did not have the desired results.</p> <p>These role players also did not ensure, or insist on strong controls to ensure compliance with key legislation and to prevent, detect and correct material misstatements.</p> <p>None of the role players provided full assurance at any of the auditees in this category. The following role players provided some assurance:</p> <ul style="list-style-type: none"> • Senior management (100%) • Municipal managers (85%) • Mayors (85%) • Internal audit units (77%) • Audit committees (85%) • Municipal councils (69%) • Municipal public accounts committees (MPACs) (69%). 	<p>None of the role players provided full assurance at any of the auditees in this category. The role players at a few auditees provided some level of assurance while the majority provided no assurance.</p> <p>The following role players provided some assurance:</p> <ul style="list-style-type: none"> • Senior management (41%) • Municipal managers (41%) • Mayors (18%) • Internal audit units (29%) • Audit committees (35%) • Municipal councils (12%) • MPACs (12%). 	<p>The role players' contributions to assurance at these auditees were insignificant, with all role players providing limited or no assurance.</p>

Area	Best practices for clean audits (2)	Unqualified with findings (13)	Qualified with findings (17)	Adverse or disclaimed with findings (13)
Key officials	<p>There were no vacancies in the key positions of municipal manager, chief financial officer and head of the supply chain management (SCM) unit.</p> <p>There was stability at the level of municipal manager, chief financial officer and head of the SCM unit – the officials had been in these positions for almost 7 years.</p> <p>The competencies of these officials were assessed. Most had already achieved the competency requirements prescribed by the regulations. One of the two chief financial officers had not achieved the minimum competencies at year end. These competencies were, however, achieved after the year end.</p>	<p>Vacancies at the level of head of the SCM unit existed at three of the municipalities (38%) that had this position on their staff establishments.</p> <p>There was less stability, with key officials being in these positions for just under three years on average.</p> <p>A higher number of officials had not achieved their minimum competency requirements yet, or it had not been assessed – 8% of municipal managers and 23% of chief financial officers.</p>	<p>The vacancies in key positions were at a higher level:</p> <ul style="list-style-type: none"> • Municipal manager – 18% • Chief financial officer – 12% • Head of the SCM unit – 17% <p>There was even less stability, with key officials being in these positions for just more than two years on average.</p> <p>An even higher number of officials had not achieved their minimum competency requirements yet, or it had not been assessed – 43% of municipal managers, 60% of chief financial officers, and 30% of heads of the SCM units.</p>	<p>The vacancies in key positions were the highest at these auditees:</p> <ul style="list-style-type: none"> • Municipal manager – 8% • Chief financial officer – 39% • Head of the SCM unit – 45% <p>The stability in key positions at these auditees was similar to the qualified audits with findings. Key officials were in these positions for slightly longer than 2,5 years on average.</p> <p>At these auditees, most officials had not achieved their minimum competency requirements yet, or it had not been assessed - 63% of municipal managers, 63% of chief financial officers, and 67% of heads of the SCM units.</p>

Area	Best practices for clean audits (2)	Unqualified with findings (13)	Qualified with findings (17)	Adverse or disclaimed with findings (13)
Use of consultants	<p>One auditee effectively used consultants for financial reporting services. Senqu was assisted by consultants at a cost of R660 000.</p> <p>The municipality appointed the consultant in time, provided the consultant with the required records and documents, and managed the process effectively.</p>	<p>Although these auditees used consultants widely for financial reporting services, most could not produce financial statements without material misstatements – these material misstatements were corrected through the audit process.</p> <p>Twelve (92%) of these auditees were assisted by consultants at a cost of R28 million.</p>	<p>An even higher number of auditees were assisted by consultants - 16 (94%) at a cost of R51 million.</p> <p>These auditees had poor audit outcomes in spite of using consultants. The main reasons were:</p> <ul style="list-style-type: none"> • Poor project management by 56% of the auditees. • The records and documents that consultants needed to perform their services could not be provided to them at 25% of the auditees. • The consultants did not deliver on their contracts at 13% of the auditees. 	<p>The use of consultants was the most common in this category - 13 of these auditees (100%) were assisted by consultants at a cost of R24 million.</p> <p>These auditees had poor audit outcomes in spite of using consultants – the main reasons for this were:</p> <ul style="list-style-type: none"> • Poor project management by 15% of the auditees. • The records and documents that consultants needed to perform their services could not be provided to them at 23% of the auditees. • The consultants were appointed too late at 38% of the auditees.
Use of consultants		<p>Their practices in managing consultants (not limited to financial reporting) needs attention:</p> <ul style="list-style-type: none"> • No transfer of skills at 50% of auditees. • Poor performance management and monitoring at 25% of auditees. • Inadequate planning and appointment processes at 17% of auditees. 	<p>Weak practices in managing consultants (not limited to financial reporting) were widespread:</p> <ul style="list-style-type: none"> • No transfer of skills at 56% of auditees. • Poor performance management and monitoring at 63% of auditees. • Inadequate planning and appointment processes at 44% of auditees. 	<p>These auditees had the poorest practices in managing consultants (not limited to financial reporting):</p> <ul style="list-style-type: none"> • No transfer of skills at 92% of auditees. • Poor performance management and monitoring at 92% of auditees. • Inadequate planning and appointment processes at 69% of auditees.

Area	Best practices for clean audits (2)	Unqualified with findings (13)	Qualified with findings (17)	Adverse or disclaimed with findings (13)
<i>Use of grants</i>	<p>The municipalities effectively used the municipal systems improvement grant (MSIG) and financial management grant (FMG), which are aimed at improving financial and performance management. They spent their full grants and achieved the planned targets.</p> <p>One municipality received a municipal infrastructure grant (MIG), which was used effectively. It spent its full grant and achieved the planned targets.</p>	<p>The municipalities used the MSIG and FMG grants, but with less effect as they slightly underspent and achieved fewer targets:</p> <ul style="list-style-type: none"> • 4% of grants were not spent. • Targets were not achieved for 8% of the MSIG spent. <p>The weaknesses in the control environments of these municipalities also affected their ability to use the MIG effectively:</p> <ul style="list-style-type: none"> • 6% of the grant was not spent. • The targets were not achieved for 12% of the money spent. 	<p>The municipalities in this category used their grants with a lot less effect:</p> <ul style="list-style-type: none"> • Targets were not achieved for 45% of the MSIG spent and 15% of FMG spent. • 89% of MIG was spent by municipalities in this category; however, only 25% of the planned targets were achieved. 	<p>Municipalities in this category did not use their grants effectively.</p> <ul style="list-style-type: none"> • Although, 91% of the MSIG and FMG were spent, the targets were not achieved for 30% of the MSIG spent and 29% of the FMG spent. • Almost all (97%) of the MIG was spent by municipalities in this category, yet 85% of the planned targets relating to the use of this money were not achieved.

Area	Best practices for clean audits (2)	Unqualified with findings (13)	Qualified with findings (17)	Adverse or disclaimed with findings (13)
Supply chain management	<p>Auditees had no material instances of non-compliance with SCM legislation. Both auditees need to improve in some of the areas of SCM.</p> <p>Their levels of irregular expenditure were low as a result of their good SCM practices. They incurred only 0,38% of the irregular expenditure of all auditees and were responsible for 1,2% of the municipal budget.</p>	<p>In total, 38% of these auditees did not materially comply with SCM legislation. Only 8% had good SCM practices</p> <p>Their levels of irregular expenditure were low, but require attention to eliminate this expenditure completely. These auditees incurred 1% of the total irregular expenditure and were responsible for 17% of the municipal budget.</p> <p>At four auditees (31%), the municipal manager and council did not investigate the irregular expenditure of the previous year to determine whether anyone was liable for the expenditure.</p>	<p>In total, 88% of these auditees did not materially comply with SCM legislation.</p> <p>Their levels of irregular expenditure were high as a result of their poor SCM practices. These auditees contributed the most to the total irregular expenditure at 74%, while being responsible for only 64% of the municipal budget.</p> <p>The lack of investigation was more pronounced - at eight auditees (48%), the municipal manager and council did not investigate the irregular expenditure of the previous year to determine whether anyone was liable for the expenditure.</p>	<p>In total, 77% of these auditees did not materially comply with SCM legislation.</p> <p>We experienced limitations in performing the SCM audits at 54% of these auditees.</p> <p>Their levels of irregular expenditure were high as a result of bad SCM practices and could have been higher without the audit limitations.</p> <p>Even though they were responsible for only 18% of the municipal budget, these auditees contributed 24% of the total irregular expenditure.</p> <p>The lack of investigation was also prevalent in this category - at five auditees (38%), the municipal manager and council did not investigate the irregular expenditure of the previous year to determine whether anyone was liable for the expenditure.</p>

AUDIT OUTCOMES, ROOT CAUSES AND THE IMPACT OF KEY ROLE PLAYERS

1. Overall audit outcomes

The Eastern Cape municipal sphere consists of 45 municipalities and 11 municipal entities. The municipalities are made up of two metros, six district municipalities and 37 local municipalities. The municipalities operate on a budget of R34,2 billion (operating expenditure: R25,7 billion and capital expenditure: R8,5 billion). We have completed the audits of all 45 municipalities and the outcomes are reflected in this report

Where municipalities have municipal entities under their control, the audit opinion on their financial statements is that of the consolidated financial statements. However, all other statistics refer to the municipalities only as municipal entities only constitute 1% of the total municipal budget. The outcomes of the 11 municipal entities are dealt with separately in section 11 of this report.

Seven year analysis indicates slow improvement (2007-08 vs. 2013-14)

Figure 2: Seven year outlook on audit outcomes



Figure 2 shows that the province did not achieve 100% of unqualified audits by 2014, which was the target that government set itself through operation clean audit. Only Sarah Baartman district and Senqu achieved our elevated definition of clean audit opinions. We have taken note of the encouraging decline in adverse/disclaimed opinions and growth in the number of unqualified opinions. This positive movement has, however, been very slow. In comparing the 2013-14 outcomes to that of 2007-08, 26 municipalities (58%) improved their outcomes while seven (16%) regressed.

An analysis of the movement in outcomes over the seven years clearly indicates that the majority of municipalities did not address audit findings at a root cause level, leaving the sustainability of improvements in doubt. Where there are improvements, these are isolated to certain operational areas and tended to be overshadowed by significant control failures, especially in SCM and human resource management. This has underpinned the ever-present trend of improvements being negated by regressions. The year-on-year movements over this period show 70 improvements that have been negated by 41 regressions.

We had numerous intensive interactions with both the political and administrative leadership over this period. Topics included the audit outcomes of their municipalities, the root causes underpinning unfavourable outcomes and the need for a strong control environment entrenched in daily, weekly and monthly processes. During these engagements our consistent message has been that it is possible to obtain clean administration if there is a real will to change and if the leadership actively strives for quality and sustainability in executing its duties. This can be achieved by:

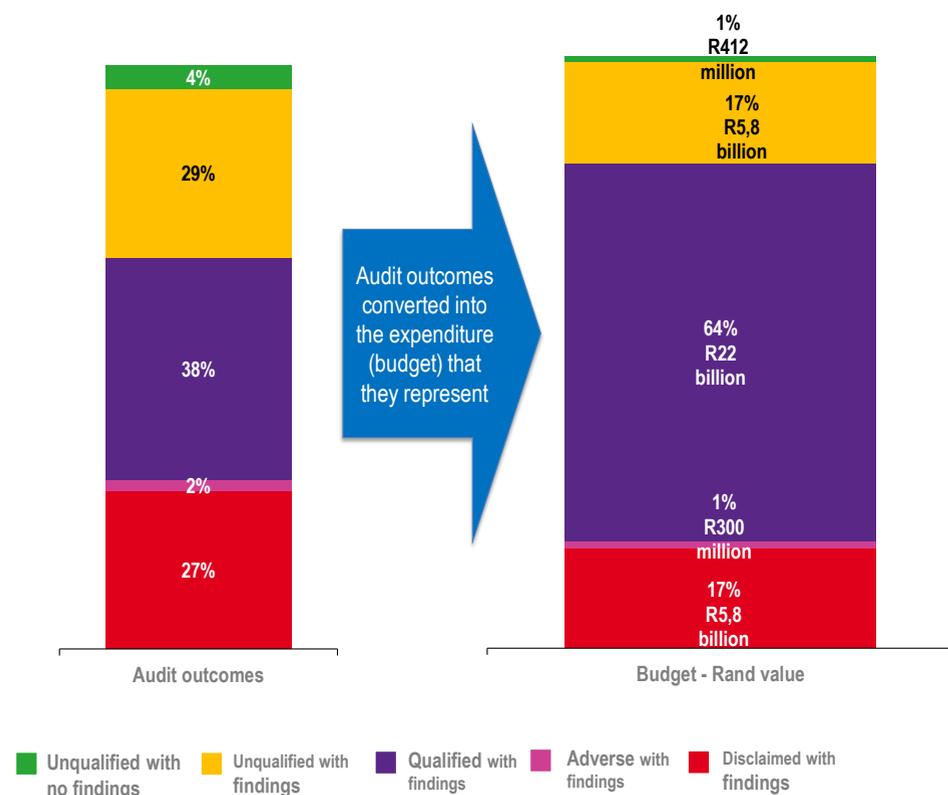
- **Ownership** - Political and administrative leadership must take full ownership of the internal control environment.
- **Skills** - Investment in appointing skilled staff.
- **Discipline** - Daily disciplines must be instilled that ensure excellence in financial management, service delivery execution and compliance with legislation.
- **Credibility** - Leadership must set a tone and implement processes to ensure the credibility of all the municipalities' reports.
- **Performance management systems** - Implementing performance management systems with clear and decisive consequences for poor performance.
- **Governance** - Internal audit, audit committees and MPACs need to ensure that all their activities are coordinated and contribute to the credibility of information.

All levels of leadership have been slow in responding to these messages and recommendations.

2. Audit outcomes for 2013-14

The 2013-14 municipal audit outcomes shown in figure 2 reflect an encouraging net improvement in five audit outcomes from the previous year. This net improvement is made up of 11 improvements, some of which were negated by six regressions.

Figure 3: Audit outcomes per budget



While 33% of the audit outcomes were **unmodified** (clean/unqualified opinions with findings on compliance or performance reporting), the fact that **modified** outcomes (qualified/adverse/disclaimed) still represented 67% of the outcomes remains a concern. This concern is intensified when translating the outcomes into the budgets managed by these municipalities.

Only 1% of the provincial budget, totalling R34,3 billion was managed by municipalities that could produce reliable and credible financial reports. A total of 99% of the provincial budget was therefore managed by municipalities whose reporting credibility was in question.

Submission and quality of financial statements

Municipalities are required by the Constitution and various other legislation to be transparent and accountable for the public resources that have been provided to them. Municipalities are required to prepare financial statements according to the applicable accounting framework and relevant legislation. These financial statements must constitute transparent reports by being reliable, accurate, credible and supported by underlying records.

Although there has been an improvement in submitting financial statements for audit over the past five years, their quality remains poor. That poor quality financial statements were submitted was the most common finding on compliance, reported at 93% of municipalities (42). This is a similar non-compliance level to the previous year's 96% of municipalities (43), which creates an impression of malicious compliance with the legislated submission date rather than improved processes of financial reporting.

Figure 4: Quality of financial statement submitted for audit

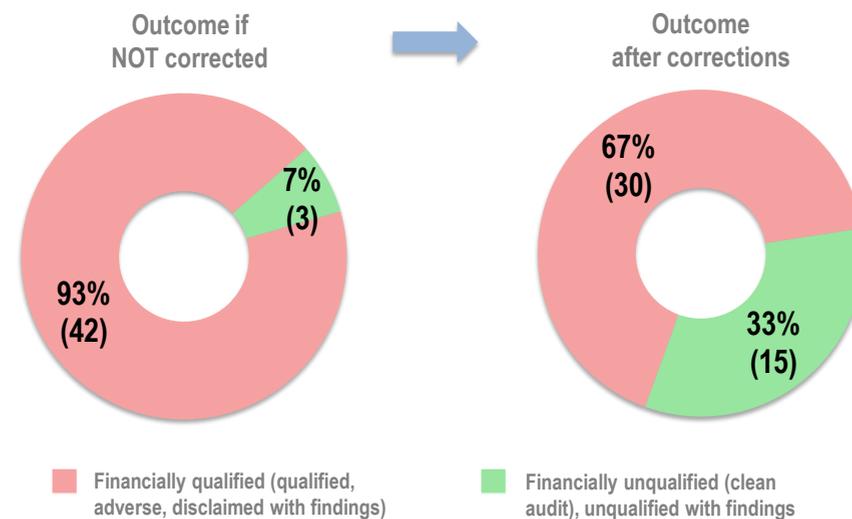


Figure 4 illustrates that three municipalities did not need to effect material adjustments to their financial statements during the audit process. Had adjustments not been effected, the 33% of reported unmodified opinions (15 municipalities) would have stood at a mere 7%. These significant adjustments to recorded balances are a clear indication of a breakdown in the control environment.

Movement in the 2013-14 outcomes

Figure 5: Movements in audit outcomes

	Outcomes	Improved 11	Unchanged 28	Regressed 6
Unqualified with no findings	4% 2	Sarah Baartman, Senqu		
Unqualified with findings	29% 13	Baviaans, Camdeboo, Kouga, Maletswai	District municipalities Amatole District Joe Gqabi District 9	Anahlati
Qualified with findings	38% 17	Alfred Nzo, Emma!eni, KSD Gartep, Inisika Yethu	Metros Buffalo City Metro, Nelson Mandela Bay Metro District municipalities Chris Hanu District 11	Inkwanca Ndlambe, Ntshankulu
Adverse with findings	2% 1		Local municipalities Mhlontlo 1	Great Kei, Mozzana
Disclaimed with findings	27% 12		District municipalities OR Tambo District 7 Local municipalities Ikwezi, Inxuba Yethemba, Lukhanji, Makana, Ngqushwa, Sundays River	

Improvements

At the forefront of the improvements were Sarah Baartman district and Senqu, which made the breakthrough to being the first two municipalities in the province to receive clean audit outcomes. The improvement in the outcomes of 11 municipalities were due to a combination of leadership setting the appropriate tone, responding to our previous message on leadership stability and employing people with appropriate skills and competencies. It should be noted that, with the exception of the two clean audits, adjustments made during the audit process and the use of consultants contributed significantly to the improvements. This raises concerns regarding the sustainability of these improvements. Leadership at these municipalities, under the direction of the municipal manager, have yet to respond to our message of ensuring a skilled workforce, holding people accountable and institutionalising daily and monthly disciplines in the control environment.

Unchanged

Nine municipalities have maintained an unqualified opinion with limited findings on compliance and performance reporting for a number of consecutive years. These municipalities became complacent at having attained an unqualified audit opinion and, despite the real danger of regressions, continually fail to respond to our audit findings. The risk is that a municipality might account correctly, but be comfortable with flouting SCM regulations. This could, in turn, lead to goods and services not being procured economically, effectively and efficiently.

Eleven municipalities stagnated on qualified opinions. Of particular concern within this group are the two metros, which administer a combined budget of R15 billion. This represents 44% of the total provincial municipal budget. Despite having substantial financial resources and being better positioned to attract a skilled and competent workforce, they continue to produce financial reports that are not credible and reliable.

The lack of decisive and progressive leadership and the disregard for good governance principles governing public administration entrenched the stagnation of the seven unchanged adverse or disclaimed opinions. These municipalities again failed to provide supporting documentation for a significant number of transactions and balances in their financial statements. This created an environment that did not support accountability and was susceptible to loss through fraudulent transactions. Had the political and administrative leadership responded to our messages over a number of years, this situation could have been avoided.

Regressions

Despite trying to reach the goal of sound financial management and accountability across the province, six municipalities regressed in their outcomes. It was clear that these municipalities did not address the root causes as highlighted in our findings and recommendations. In these cases, it was necessary for the provincial executive to apply measures that would ensure that role players are held accountable for any regressions.

Municipal districts

The province's outcomes varied from one district to the next. District municipalities had not only to coordinate development and delivery throughout the district, but also needed to play a vital supporting role in the financial management of their local municipalities. These responsibilities included the following:

- Coordinate the development of the district and service delivery

The slow movement is due to the political leadership and management not responding adequately to our message to embed controls, particularly those relating to preparing monthly financial statements and implementing action plans to address the root causes of audit findings.

Way forward

To ensure that the financial statements improve, the leadership must create an environment that facilitates accurate and complete financial reporting to assist chief financial officers and consultants to meet their deliverables. Furthermore, municipalities should:

- address the vacancies and lack of competencies at the chief financial officer level and in the finance units by appointing competent personnel. Intensive training programmes should be implemented to up-skill existing staff to enhance their competence in their daily functions.
- ensure that the control environment is strengthened by introducing key oversight controls. The preparation of reliable monthly and quarterly financial statements, as well as daily and monthly reconciliations, will ensure that transactions, balances and disclosures are accurately and completely recorded.
- implement a performance management system for all officials with clear consequence management for poor performance and transgressions.

4. Annual performance report

To facilitate transparency, responsiveness and accountability, municipalities should have an effective performance reporting system in place. The public should have access to performance information that indicates what has been achieved with the amounts allocated to municipalities.

Service delivery initiatives in the local government sector are determined by public participation in developing and/or updating municipal integrated development plans and service delivery and budget implementation plans. These plans should form the basis for the allocation of budgets each year. Municipalities are required to measure their service delivery against the performance indicators and targets set for each of their predetermined performance objectives, and to report on this in their annual performance reports. We audit the annual performance reports to determine whether the information in these reports is useful and reliable.

Submitting the annual performance report for auditing

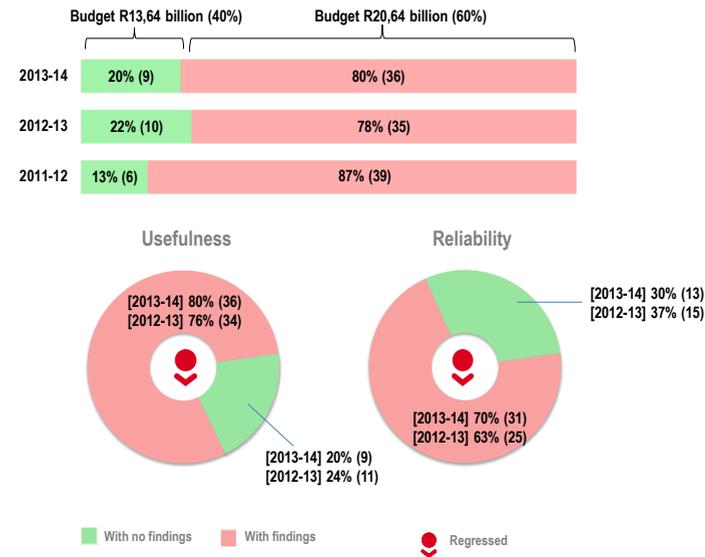
The submission of annual performance reports for auditing improved compared to the previous year. Only Ikwezi did not submit a report, compared to the five municipalities that did not submit in the previous year. This is encouraging as it is a step in the right direction.

Although the submission of annual performance reports improved, the quality of the reports was poor as only five (11%) of the submitted reports were of the required standard and did not require adjustments during the audit process to avoid findings. The quality of performance reports is poor because the leadership does not use performance reports as a tool to monitor and drive service delivery. The poor quality of performance reports is analysed further below.

Movement in outcomes on the annual performance report

Figure 8 shows the number of municipalities with material findings on the quality of their annual performance reports over the past three years, together with the number of municipalities with findings on usefulness and reliability.

Figure 8: Movement in outcomes on annual performance report and findings on usefulness and reliability



The regression of Umzimvubu was due to the municipality not embedding measures to address the usefulness of its information into its control environment.

Work is still required to improve the quality and credibility of the annual performance reports. Over the past four years we have conducted numerous sessions where recommendations on improving the quality of these reports were discussed. The leadership has generally been slow to respond to these messages. However, where the messages were taken seriously, the quality of the annual performance reports have improved. This points to the risk that municipalities prepare annual performance reports to comply with legislation rather than to use them as tools to drive their business and continually improve service delivery.

Findings on usefulness and reliability

Usefulness refers to setting objectives, indicators and targets in the planning document, and how they are reported on in the annual performance report. We measured the usefulness of the reported information against the criteria of presentation, consistency, relevance and measurability.

Figure 8 shows the number of auditees with findings on usefulness. The usefulness of targets and indicators also impacts the auditees' ability to collect information about actual performance and the reliability of actual reported performance. It is imperative that the usefulness of the planned objectives, indicators and targets as contained in the integrated development plans and service delivery and budget implementation plans receive urgent attention as they provide the foundation for measuring municipal performance. The most common findings on usefulness were the following:

- Indicators/measures were not well defined
- Performance targets were not measurable
- Objectives, indicators and targets reported on in the annual performance report were not consistent with those contained in the planning documentation.

Reliability refers to the accuracy, completeness and validity of the actual reported performance against the planned objectives, indicators and targets. Figure 8 shows that there was regression in the reliability of performance information. The regression was due to the lack of embedded systems and processes to ensure that actual performance is supported by appropriate evidence.

Findings on reliability result from municipalities not adequately considering the evidence required to prove performance when setting their objectives, indicators and targets, and not providing appropriate evidence to support their actual

reported performance. The most common finding on reliability related to the accuracy, validity and completeness of actual reported performance.

The credibility and quality of performance reports has a direct impact on the effective, efficient and economical allocation of resources to service delivery initiatives by councils. Figure 8 shows that the municipalities that were unable to provide credible performance reports managed R20,6 billion of the total local government budget within the province. There is a risk that these municipalities' in-year monitoring, oversight and decision-making processes could have been based on information that was not credible. This could have had a negative impact on the manner in which services were delivered.

Compliance with legislation relating to the annual performance report

Findings on managing strategic planning and performance were reported at 80% of municipalities (36) and were the third most common non-compliance area reported on. This is a regression compared to the previous year where this area was reported at 71% of municipalities (32). A lack of appropriate performance and reporting systems and a failure to set measurable indicators and targets were the most common findings relating to this compliance area.

Way forward

For citizens to reap the benefits of a well-functioning local government, municipal councils must empower themselves with credible performance information. They should therefore implement the following:

- Take ownership of developing and maintaining proper systems and processes for managing and reporting service delivery information. This implies that the council must scrutinise all service delivery plans (including the integrated development plan, service delivery and budget implementation plan, and budget), regularly monitor credible in-year service delivery reports and ensure that corrective action is taken when actual performance is below expectations.
- MPACs, audit committees and internal audit units should assist councils to make informed decisions by providing assurance that planning documents and in-year reports on actual performance are credible. In addition, these committees together with council should exercise in-year oversight of performance to ensure that money is used for its intended purpose and that the anticipated return on investment is achieved.
- Council and the administrative leadership should ensure that government priorities contained in the *State of the nation* and *State of the province* addresses that affect municipalities are included in their planning

documents (integrated development plan and service delivery and budget implementation plans).

- The National Treasury and the national CoGTA should assist municipalities to improve the usefulness of their performance information by setting standard key performance indicators for basic services that can be included in the service delivery and budget implementation plans of the local government sector.
- The leadership should pay attention to performance planning, reporting and monitoring if the back-to-basics initiative is to succeed. The initiative was introduced by the minister of CoGTA and is based on the principles of public participation, service delivery, good governance, sound financial management and building administrative and institutional capacity at municipalities.
- The National Treasury and the national CoGTA should research the possible implementation of computerised systems to facilitate standardised predetermined objectives reporting.

5. Compliance

Municipalities are required to deliver services to their communities according to the legislative prescripts applicable to them. The applicable legislation is based on the principles of good governance, accountability and transparency, and regulates the stewardship of the public resources at their disposal. We annually audit and report on compliance with legislation applicable to financial matters, financial management and other related matters.

Status of compliance with key legislation and movement

The compliance with key legislation improved slightly from the previous year as two municipalities (Sarah Baartman district and Senqu [2013: None]) had no material findings on key legislation.

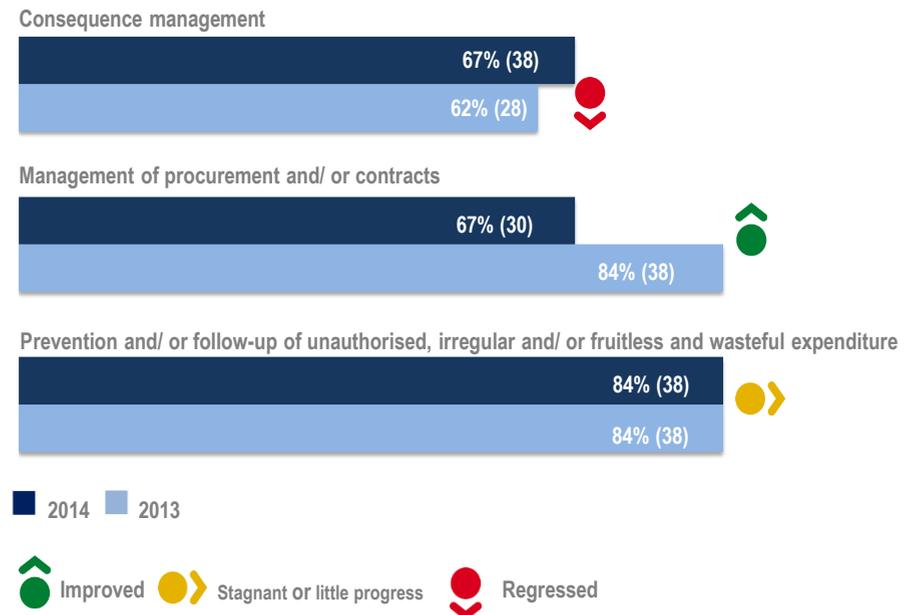
The elimination of material compliance findings at these municipalities is attributed to enforcing governance and accountability practices, in-year monitoring of compliance by management, audit committees and council, and implementing appropriate action plans to address the material compliance findings raised during the previous year's audit.

A further six municipalities have compliance findings in three or less of the legislative focus areas reported on. These municipalities are encouraged to follow the example set by Sarah Baartman and Senqu and address all findings on compliance by the next audit cycle.

At the remaining 37 municipalities, there was no progress in addressing the compliance findings raised during the previous audit cycles. This is attributed to a slow response by management, political leadership and oversight to our messages relating to the daily, weekly and monthly control disciplines required to ensure sustained compliance with legislation, including those applicable to SCM.

Figure 9 shows the most common non-compliance areas aside from those relating to annual financial statements, and performance and strategic management, which have already been dealt with in sections 2 and 4 respectively.

Figure 9: Most common compliance areas reported for procurement and contract management



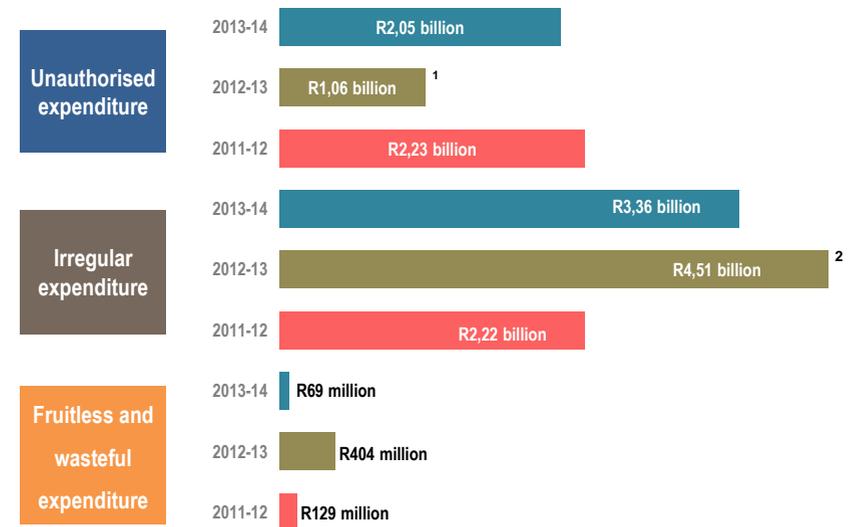
The non-compliance in figure 9 is grouped together as it relates to preventing **unauthorised, irregular as well as fruitless and wasteful expenditure, consequences** for incurring it and the main reason for irregular expenditure (non-compliance with **procurement** requirements). This non-compliance is analysed in detail in the sections that follow.

Unauthorised, irregular as well as fruitless and wasteful expenditure

The Municipal Finance Management Act (MFMA) requires accounting officers to take reasonable steps to prevent unauthorised, irregular as well as fruitless and wasteful expenditure. Where there is a persistent disregard for strengthening this control, opportunities may be inadvertently created to commit fraudulent transactions. Where municipalities are unable to prevent such expenditure, the MFMA requires disclosure of the amounts incurred in the financial statements and that such expenditure is investigated to determine liability. Where liability can be proven, the accounting officer must take disciplinary and/or criminal action against the liable employees and must institute procedures for the recovery of funds. Only after a committee of council certifies that such expenditure is not recoverable may it be written off.

Figure 10 shows the three-year trend of unauthorised, irregular as well as fruitless and wasteful expenditure that should have been prevented by the municipalities, while figure 11 shows that unauthorised, irregular as well as fruitless and wasteful expenditure totalling R5 billion had not been investigated and dealt with as required by the MFMA. Consequently, municipalities have not determined whether any of this expenditure resulted in money being wasted or if fraud was committed.

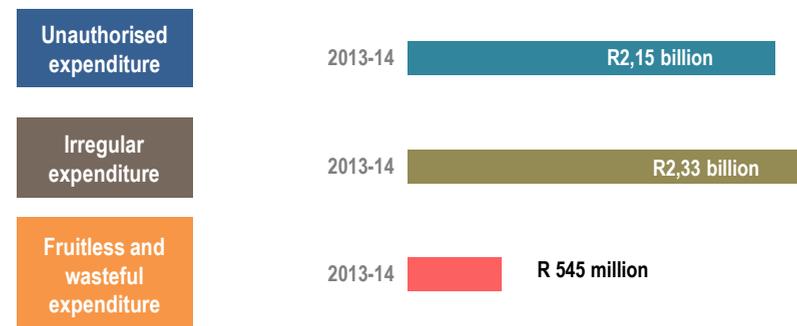
Figure 10: Trends in unauthorised, irregular as well as fruitless and wasteful expenditure



Footnotes

1. Reconciliation to the amount in the previous year's general report is as follows: R1,06 billion + previous year's adjustment at KSD of R1,1 billion = R2,16 billion disclosed in the previous general report
2. Reconciliation to the previous year's general report is as follows: R4,5 b – R805 m (Chris Hani's previous year's adjustment) – R150 m (Buffalo City's previous year's adjustment) – R189 m (Makana – 2013 late finalisation) – R31 m (Sundays River – 2013 late finalisation) = R3,33 billion disclosed in the previous general report

Figure 11: Previous year's unauthorised, irregular and fruitless and wasteful expenditure not dealt with



Unauthorised expenditure

Unauthorised expenditure is expenditure that was not incurred in accordance with the approved budget.

Of unauthorised expenditure of R2,05 billion incurred in 2013-14, most (99,7%) was a result of overspending the approved budget. Although 82% of this type of expenditure was disclosed by the auditees, it was only identified after the year-end when the financial statements were being prepared.

Figure 10 shows that the unauthorised expenditure amount relating to 2012-13 was reduced by an adjustment of R1,1 billion. This was processed by the King Sabata Dalindyebo municipality to rectify a previous year's error within their financial statements, for which they had received a qualification in their audit report.

At 22 municipalities the unauthorised expenditure reported on in the previous year was not investigated to determine whether any officials could be held liable. The lack of investigation undermines accountability and promotes a culture of tolerance for transgressions of legislation.

Non-cash items such as depreciation, the impairment of property, infrastructure and equipment, and receivables are included in the approved municipal budgets. The incorrect estimation of these items accounted for approximately 50% of local governments' unauthorised expenditure during 2013-14.

The depreciation was underestimated as full records of property, infrastructure and equipment were not maintained during the year. In most cases the records relating to assets were only updated at the year-end. This resulted in depreciation being under-recorded during the year, which led to unauthorised expenditure when calculating the depreciation for the financial statements. This correlates to the qualifications on property, infrastructure and equipment and the adjustments made to property, infrastructure and equipment as a result of the audit process.

The lack of adequate budget processes, credible in-year reports and monitoring of expenditure during the year were the main factors that gave rise to unauthorised expenditure.

Irregular expenditure with a focus on supply chain management

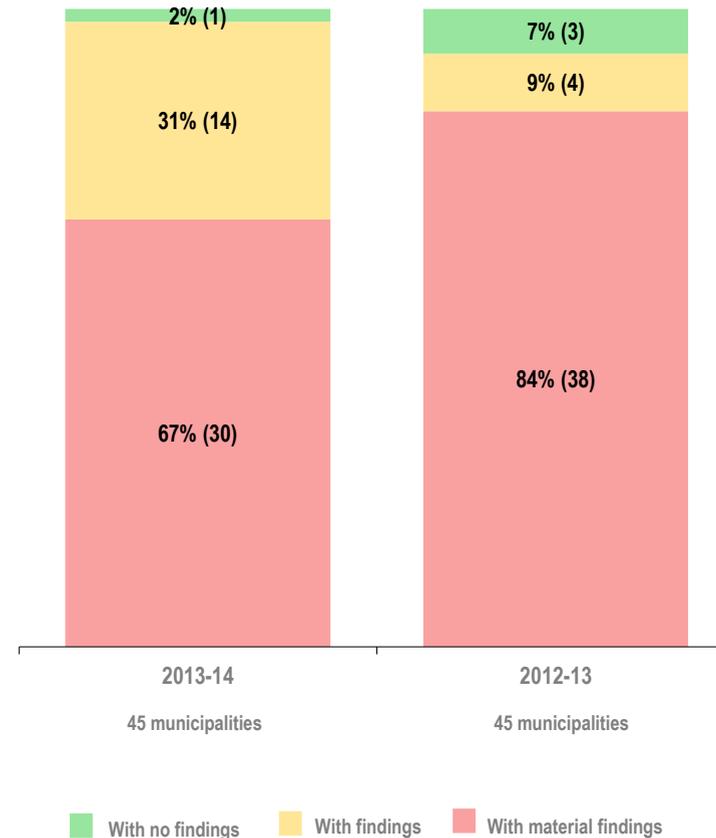
Irregular expenditure is expenditure that was not incurred in the manner prescribed by legislation. Such expenditure does not necessarily mean that money was wasted or that fraud had been committed, but is rather an indicator that legislation was not followed. This includes legislation aimed at ensuring that procurement processes are competitive and fair. It is the role of council to

investigate all irregular expenditure to determine whether it constitutes misconduct, fraud, or losses that should be recovered.

Almost all irregular expenditure (99%) was the result of not adhering to SCM prescripts. During the audit of compliance with the requirements of SCM legislation, we tested awards consisting of 1 188 contracts with an approximate value of R4,79 billion as well as 1 715 quotations with an approximate value of R95,7million.

Figure 12 shows the number of auditees with SCM findings as well as the number of municipalities with material findings on compliance reported in their respective audit reports.

Figure 12: Status of supply chain management



Although the number of auditees with material findings on compliance decreased, irregular expenditure remains high.

Figure 13: Findings on supply chain management

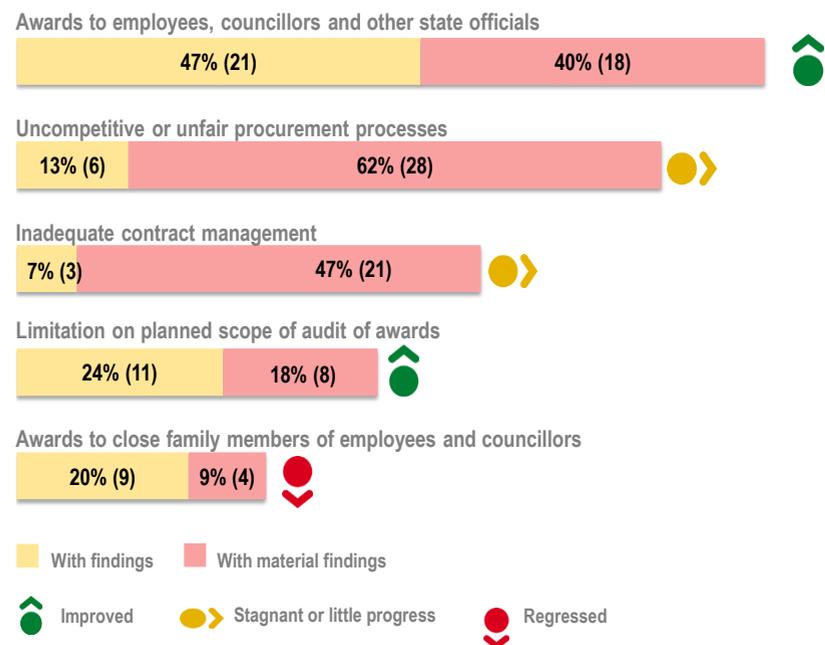


Figure 13 shows the number of auditees with findings on the key SCM risk areas that we audit, as well as the movement from the previous year.

The SCM transgressions that give rise to irregular expenditure are driven by conflicts of interest and non-adherence to SCM controls. The political and administrative leadership has not set an example of a low tolerance for deviations from controls (a lack of consequences for transgressions).

Persons with conflicts of interest may unfairly influence the outcomes of awards in favour of a particular supplier. Conflicts of interest, where awards were granted to councillors, employees, their close family and persons employed by the state amounted to R800,5 million for the year under review. This amount was made up of awards to the value of R734,5 million to employees, councillors and other state officials and awards to the value of R66 million to close family members of the councillors and employees.

Awards to employees, councillors and other state officials are specifically prohibited by legislation. Awards to close family members of employees and councillors are not specifically prohibited, but legislation requires disclosure by both the supplier and employee of the interest. It also requires municipalities to have processes to ensure fair, transparent and cost-effective procurement that guarantees the effective, efficient and economical use of resources. All awards to close family members and employees are required to be disclosed in the

financial statements. As much as 72% of the awards to close family members of employees and councillors did not meet these requirements.

Findings relating to **uncompetitive or unfair procurement processes** were of specific procurement processes that should have been followed (includes procurement without a competitive bidding process and non-compliance with procurement process requirements). The most common findings in this area related to procurement without obtaining three written quotations, not or incorrectly applying the preferential procurement processes, and procurement from suppliers without proof that their tax affairs were in order. These awards not only result in limited assurance that value for money was achieved or contracts were awarded to suppliers that were capable of delivery, but also exposes the municipalities to litigation by the parties that should have been awarded the contracts .

Contract management refers to how contracts are managed after they are awarded. The most common findings related to payments on contracts exceeding the approved contract values, the lack of performance monitoring by contractors, inadequate performance measures included in contracts and the failure to register construction projects with the Construction Industry Development Board within 21 days. Payments on contracts that exceed the approved contract value, together with approved variations, are the main cause of irregular expenditure related to non-compliance with legislation in contract management. These overpayments negate the benefits derived from a competitive bidding process and may be due to incentives provided by suppliers. This requires further investigation.

Awards to the value of R341,3 million requested for audit were not submitted due to **limitations imposed by management**. As a result, the findings in this section of the report and the irregular expenditure reported may not be complete. The possibility that these awards were deliberately withheld to conceal fraudulent transactions cannot be ruled out and requires further investigation.

The contribution of the risk areas highlighted above to the irregular expenditure of R3,36 billion incurred during the year is estimated as follows:

- Procurement without a competitive bidding or quotation process – R1,64 billion (49%).
- Non-compliance with procurement process requirements – R1,07 billion (32%).
- Non-compliance with legislation on contract management – R627 million (19%).

We did not investigate the irregular expenditure, as that is the role of the accounting officer and oversight bodies. We determined through our normal audits that R1,95 billion (58%) represented goods and services that were received despite the normal processes governing procurement not being

followed. As the balance was not audited, we cannot confirm that goods and services had been received. A further risk is that these transgressions are the result of either a lack of competence or an incentive to award contracts to related parties where the benefit of goods and services may not be fully realised. The high incidence of findings on uncompetitive or unfair procurement processes (34 auditees) is of particular concern and should be investigated further.

Although the irregular expenditure reported during 2013-14 decreased significantly when compared to the restated 2012-13 amount, it is still of concern. At R3,36 billion it amounts to 12,4% of the budget (less costs of employment) of the local government sector in the province.

In total, 61% of the irregular expenditure was the result of acts of non-compliance in the year under review, while the rest was expenditure resulting from transgressions in previous years.

Only 50% of the reported irregular expenditure was identified by the auditees' internal controls, with the rest being identified during the audit process. This means that auditees still do not have processes to detect irregular expenditure. Where auditees' systems of control did detect the irregular expenditure, the principle still stands that if it could be detected, then it should be prevented.

Our audits also identified that at 19 auditees (42%), the accounting officer and/or oversight bodies did not investigate the previous year's irregular expenditure to determine whether any person was liable for the expenditure. Consequently, auditees did not determine whether the irregularities constituted fraud or whether any money had been wasted.

Fruitless and wasteful expenditure

Fruitless and wasteful expenditure is expenditure that was made in vain and that would have been avoided had reasonable care been taken.

The significant reduction in fruitless and wasteful expenditure is attributed to a distorting one-off land claim settlement of R330 million paid by King Sabata Dalindyebo during 2012-13 that could have been avoided.

At R69 million for the year under review, this type of expenditure is still too high. Most of this expenditure relates to penalties and interest on late payments that could have been avoided.

Accounting officers (municipal managers) and oversight bodies (MPAC and councils) should insist on credible in-year reporting to monitor and better control this type of expenditure during the year. All fruitless and wasteful expenditure should be properly investigated and recovered from officials where possible.

Way forward

The findings relating to unauthorised, irregular as well as fruitless and wasteful expenditure and compliance with legislation were due to weak control environments. Good governance and sound financial management will ensure that local government resources are used in an economical, effective, efficient and transparent manner for the benefit of citizens. The following recommendations should be implemented to strengthen the control environment:

- The political and administrative leadership should set a tone of zero tolerance for transgressions of legislation and conflicts of interest. Decisive action should be taken against those that breach the requirements of legislation.
- Audit committees and internal audit units should assist by identifying breaches of legislation and reporting breaches to the leadership for action to be taken against those responsible.
- Councils and their MPACs should investigate all of the unauthorised, irregular as well as fruitless and wasteful expenditure that has not been dealt with to determine liability. Once liability has been established, the actions required by section 32 of the MFMA should be enforced
- Oversight role players (council and MPAC) must hold accounting officers and senior management accountable for providing the desired level of assurance that will result in improved audit outcomes.

6. Human resource management

Human resource management is effective if adequate, sufficiently skilled resources (in other words, staff) are in place, and if staff performance and productivity are properly managed. The effectiveness of human resource management is critical as it has a direct bearing on building and maintaining sound institutional and administrative capabilities.

Major internal control weaknesses in human resource management with significant periods of vacancy in the positions of municipal manager, chief financial officer and head of SCM contributed to there being no improvement in overall human resource management from the previous year, despite improved outcomes. This highlights the risk that the improvements on audit outcomes may not be sustainable.

Management of vacancies

Figure 14 shows the correlation between the average number of months key officials (municipal managers and chief financial officers) had been in their positions and the audit outcomes. It is evident that unqualified audit outcomes are more prevalent where key officials have been in positions for longer periods of time. This is, however, only the foundation required to build a sound financial and performance management control environment conducive to effective oversight and accountability. It is critical that all positions, including the vacancies, are filled with competent and skilled individuals that can adequately manage and mitigate the risks within the control environment and promote efficient and economic delivery of services. This should also be complemented by a zero tolerance for transgressions and poor performance.

Figure 14: Stability in key positions (chief financial officer and municipal manager) per audit outcome

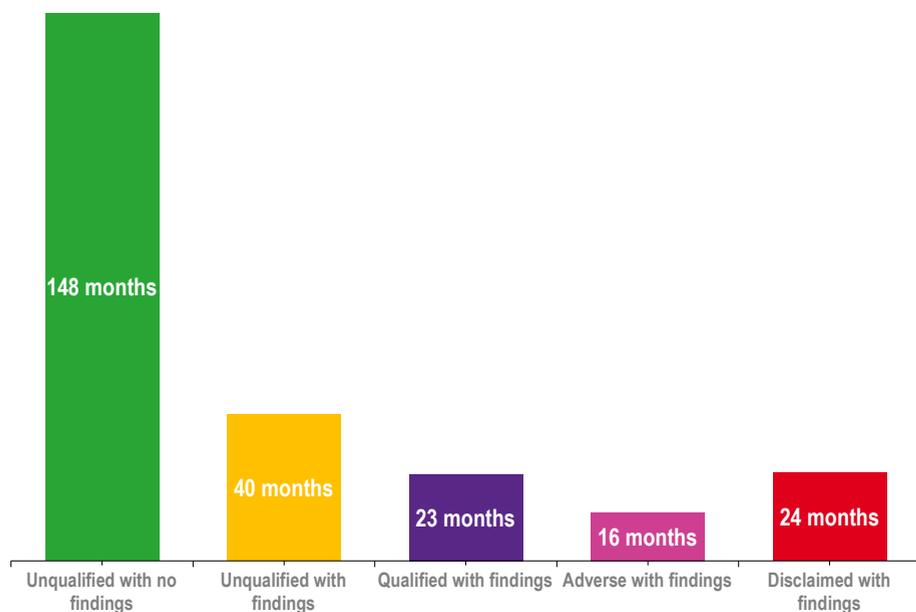


Figure 15: Municipalities with vacancies at year end

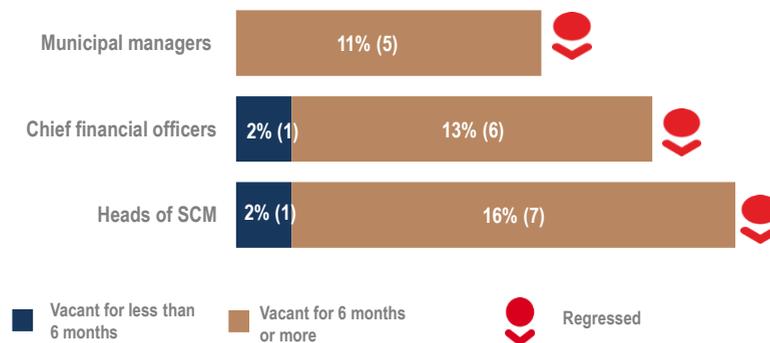
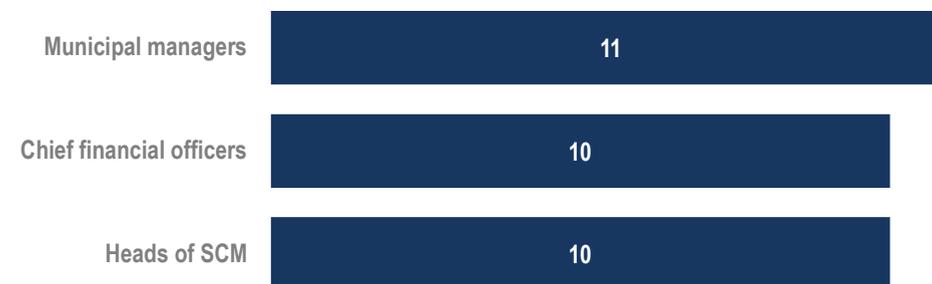


Figure 16: Average vacancy period (months)



The importance of retaining reliable and skilled staff is also evident as those municipalities that achieved unqualified financial audit outcomes had kept their key staff for an average period of 40 months or more. These experienced staff had the knowledge and skill to assist in improving and maintaining good audit outcomes.

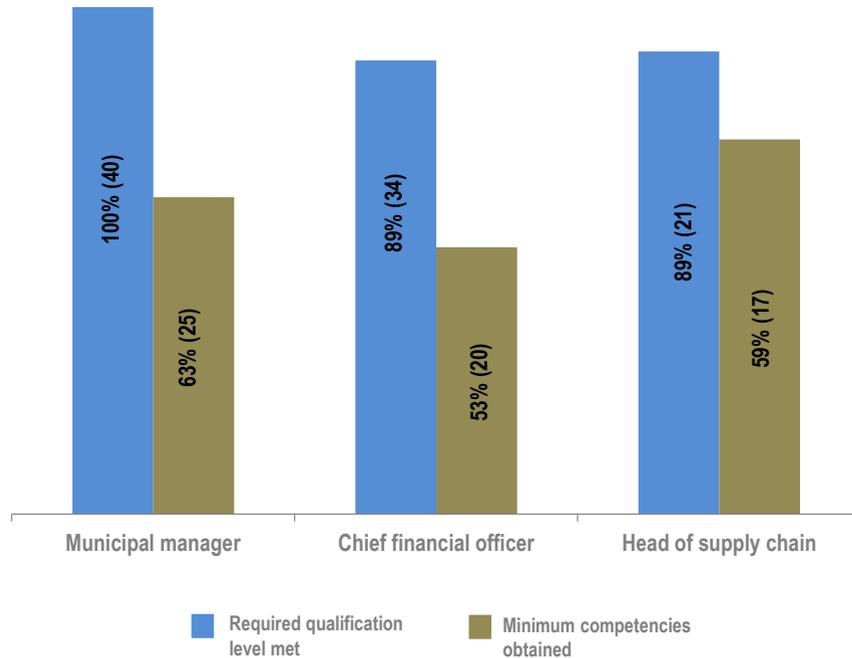
Considering the importance of key positions being filled, the picture reflected in figures 15 and 16 is concerning. The time it takes to fill vacancies indicates that the administrative and political leadership are not prioritising filling vacant posts; 31% of municipalities (14) had one or more vacancies within key positions.

The continued absence of permanent officials to lead and guide municipalities compromises the effectiveness and stability of the control environment. This is illustrated by the seven municipalities that had vacancies in their chief financial officer position at year-end also having all their audit outcomes modified. The time taken to fill vacancies in SCM is a contributing factor to the constant increase in irregular expenditure incurred by municipalities. Filling vacancies, particularly the position of chief financial officer and positions in the finance unit, had a significant impact on the governance of municipal finance and, ultimately, the audit outcomes.

Competencies and qualifications of key positions

The MFMA requires officials to meet prescribed competency levels in financial management and SCM. This is supported by the *Municipal regulations on minimum competency levels*, which sets the required levels of competence for accounting officers, senior managers, finance officials and other officials responsible for municipalities' SCM. The financial management and governance competencies ensure that chief financial officers are able to prepare credible and accurate financial reports on the accounts of municipalities.

Figure 17: Achievement of minimum competencies



As illustrated in figure 17, only 20 chief financial officers (53%) meet the overall competency requirements. Furthermore, a significant number of chief financial officers and heads of SCM still do not meet the minimum qualification requirements. Their lack of skills and knowledge has an impact on the ability of these key officials to adequately perform their required duties and instil an effective control environment. This is evident in the poor quality of financial statements received and the high incidence of non-compliance with SCM.

Most municipalities that had heads of SCM incurred irregular expenditure. The qualifications and competencies of these officials did not translate into a reduction in irregular expenditure by auditees. This shows that in this position the lack of consequences has a much larger impact on the amount of irregular expenditure than qualifications and competencies.

Impact of municipal managers on audit outcomes

Municipal managers, as accounting officers, are ultimately responsible for the audit outcomes. It is their responsibility to ensure that:

- the staff establishment is aligned to the municipal strategy
- vacant posts are filled in time with competent and skilled staff
- consequence management is enforced where staff are not performing
- the chief financial officer is performance managed
- processes are in place to manage consultants
- reports on performance against predetermined objectives are accurate.

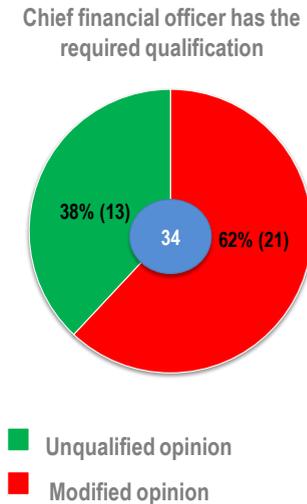
We are concerned about the five municipal manager positions that were vacant at year end. The vacant positions were filled by officials in an acting capacity; however, these officials also had to fulfil the duties of their own posts. Vacancies for extended periods at this level do not serve the interests of accountability. We are also concerned about the appointment of 11 municipal managers who do not have the required competencies for their positions. Processes should be implemented to ensure that these competencies are obtained as a matter of urgency.

The findings reported throughout this report, together with chief financial officer vacancies and competencies, an analysis of the impact of chief financial officers on audit opinions, and the analysis of the use of consultants, all support the view that most accounting officers are not doing what is required of them.

Impact of chief financial officers on financial statement opinions

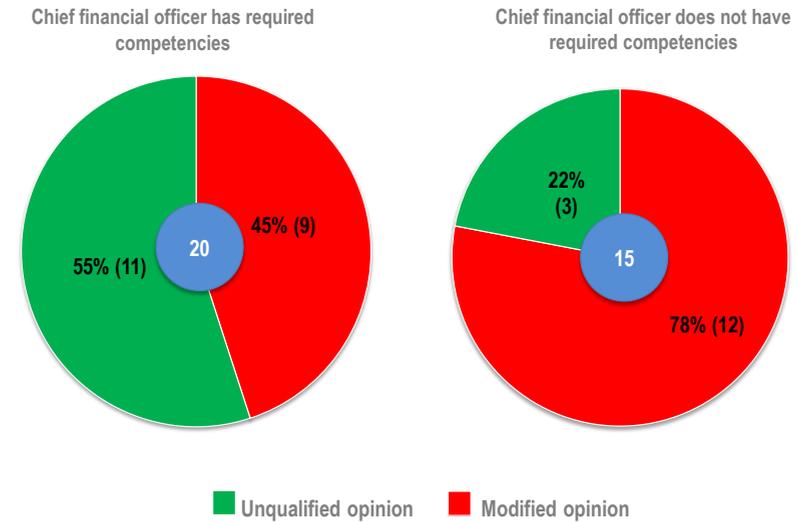
Although qualifications of chief financial officers are expected to translate into credible financial statements, our assessment of competencies and qualifications in relation to the financial statement audit outcomes indicates that there is no correlation between the two. This is depicted in figure 18.

Figure 18: Impact of chief financial officers' qualifications on financial statement audit opinions



Although we acknowledge the improvement in chief financial officers attaining qualifications and skills compared to the previous financial year, we are concerned that these competencies did not translate into credible financial statements. This picture is even worse if we consider that 12 of the 15 unqualified outcomes were achieved through audit adjustments as part of the audit process and the use of consultants. In addition, most municipalities appointed consultants to assist with the preparation of their financial statements.

Figure 19: Impact of chief financial officers' competencies on financial statement audit opinions



Furthermore, we assessed the competencies of the chief financial officers according to the National Treasury minimum competencies regulations. Government is not getting a return on the investment made in capacitating and up-skilling these officials. From this analysis, we can see that although measures may have been put in place to ensure that staff are capacitated with the skills to perform their jobs, the skills acquired do not translate into work performance unless there is adequate monitoring and oversight to ensure that they perform their jobs as expected. Chief financial officers are custodians of public funds and should therefore perform their jobs diligently to ensure that they account for these funds in an effective, efficient and economical manner.

With the exception of Sarah Baartman district, Kouga, Kou Kamma and Blue Crane, all auditees used consultants. The costs of consultants used for financial reporting increased by R34 million (49%) in the current year. The increase in the number of chief financial officers that attained competencies created an expectation that the use of consultants to prepare financial statements would decrease.

Performance management

As indicated in section 13, a lack of consequences for poor performance and transgressions was identified as a root cause of poor audit outcomes at 76% of auditees. When officials are not accountable for their actions, the perception is created that poor performance and unacceptable behaviour and their results are acceptable and tolerated.

Where a shortage of skills was identified as the cause of poor performance, appropriate training should be given to empower staff to perform their duties effectively. Although the majority of municipalities did have performance contracts for senior management, they were not actively and regularly monitored or used as a tool to drive good performance. Furthermore, junior staff did not have performance contracts, which did not provide an enabling environment for effective accountability.

Way forward

As indicated above, effective human resource management is a key driver in building a sound financial and performance control environment that is conducive to oversight and accountability. It is therefore critical that the following areas relating to consequence management, management of vacancies and maintaining a skilled and qualified workforce are addressed:

- Councils must ensure that municipal managers sign performance agreements and that their performance is regularly monitored during the year. Where performance is not at the level required, implement appropriate corrective action. Where officials have been equipped with the relevant qualifications and competencies, implement performance management in line with the staff development process.
- Councils should ensure that performance monitoring is done on the basis of accurate and credible information. The credibility and accuracy of the reports submitted to council should be assured by council committees such as MPAC and audit committees.
- To have a meaningful and sustained improvement in the control environment, municipalities should continue to ensure stability in key positions. The process of creating stability within key positions should entail a thorough analysis of the current staff establishment and its alignment to the strategic objectives of the municipality.

7. Use of consultants in the areas of financial and performance reporting

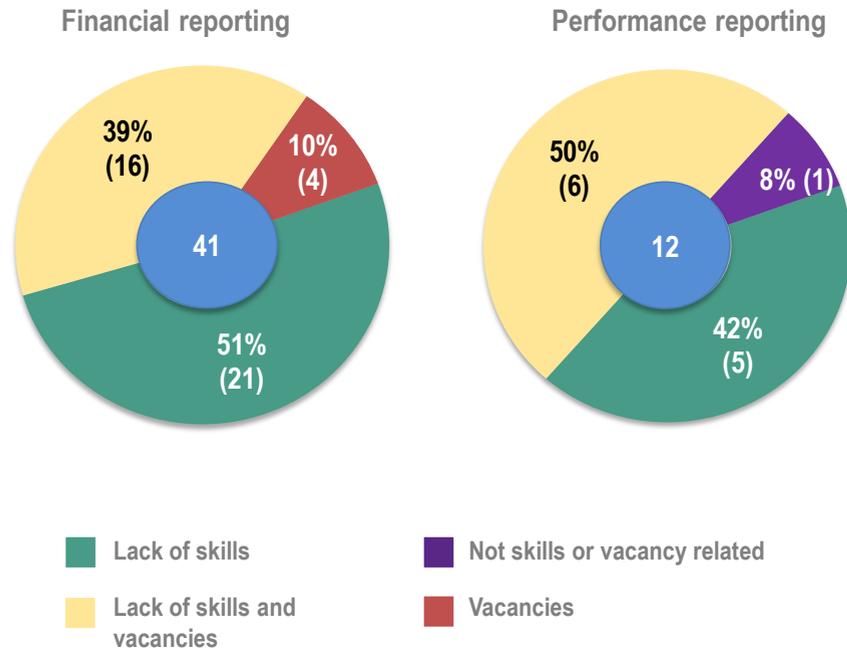
Our audit included an assessment of the work performed by consultants at municipalities. Although we acknowledge the need to appoint consultants to assist the public service, this must be needs-driven, with an emphasis on value for money, proper planning and monitoring, and the transfer of skills.

To supplement their human resources during the year, the municipalities used consultants to the value of R106 million (2012-13: R72 million) for financial reporting and R9,5 million (2012-13: R7,7 million) for performance reporting. This includes the R2,4 million paid by the provincial CoGTA for interventions to assist four municipalities with financial reporting.

The consultants' financial reporting services included preparing financial statements and related accounting processes such as preparing and reconciling the fixed asset register to the general ledger, preparing key account reconciliations and processing transactions into the general ledger. All of these services are functions that should have been performed by the chief financial officers and their finance teams.

The consultants' performance reporting services included assistance with preparing the integrated development plans and service delivery and budget implementation plans, and preparing the annual performance report. These are functions that should have been performed by the municipal managers and their senior management teams.

Figure 20: Reasons for using consultants



As indicated in figure 20, the main reason for the high use of consultants was a combination of a lack of skills and vacancies within municipalities for both financial and performance reporting. This is consistent with the reasons given in the previous year.

Thirty-eight municipalities (84%) had filled their chief financial officer positions at year-end. Thirty-four of these municipalities (89%) used consultants for financial reporting during the year.

There is a correlation between chief financial officers achieving minimum competencies, shown in figure 17, and the reasons for the use of consultants (figure 20). A lack of skills was cited as the main reason for using consultants at 13 (72%) of the 18 municipalities whose chief financial officers did not meet the prescribed minimum competency levels.

Considering that the preparation of financial statements is one of the core responsibilities of a chief financial officer, it is of concern that consultants are still being used to discharge the functions of the appointed chief financial officers. This does not promote the efficient and effective use of public funds as the chief financial officer, the officials in the finance units and the consultants are all paid for the same service.

Figure 21: Vacancies at finance units of auditees that used consultants

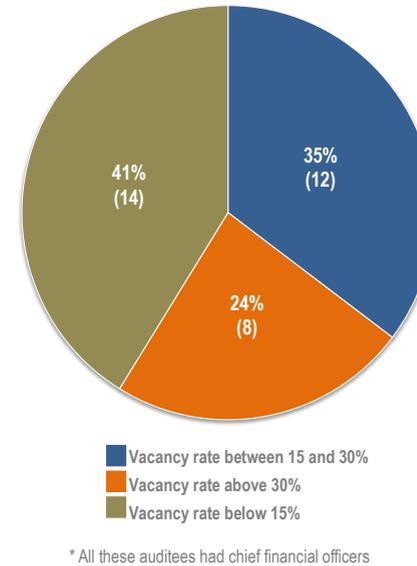


Figure 21 shows the vacancies within the finance units of municipalities where consultants were used. The finance unit vacancy rates above 15%, at 20 municipalities, are of concern as they have a negative impact on the control environment and financial reporting processes. The organograms of these units should be reviewed to ensure that they are still relevant. If they are still relevant, chief financial officers should address their high vacancy rates and the time taken to fill vacant posts.

Figure 22: Impact of consultants

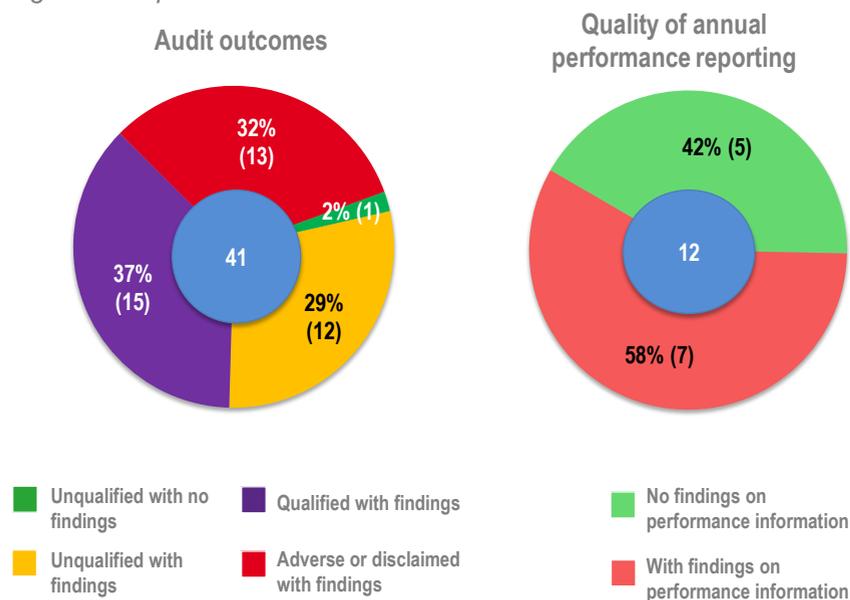


Figure 22 shows that the use of consultants was not effective as they did not have a significant impact on the audit outcomes. Only 13 (32%) of the 41 municipalities that made use of consultants for financial reporting improved their audit opinion, while five (42%) of the 12 municipalities that used consultants for performance reporting improved their outcomes in this area. Of concern is the number of auditees that received qualified/adverse/disclaimed audit outcomes even with the use of consultants. Based on these results, there has not been a substantial benefit from the funds used for the acquisition of consultants. The reasons for the ineffective use of the consultants are documented in the table 2.

Table 2: Reasons for the lack of impact of consultants:

Reason for lack of impact	Financial Reporting	Performance Reporting
Lack of records and documents	16%	20%
Other auditee ineffectiveness	8%	0%
Consultants appointed too late	28%	0%
Poor project management by the auditee	40%	80%
Consultant did not deliver	8%	0%
Total	100%	100%

As indicated in table 2, the largest contributor towards the ineffective use of consultants is poor project management by the auditee, followed by the late appointment of consultants and a lack of records. This indicates a lack of capacity by the municipalities to adequately plan for the efficient and effective use of consultants. As such, municipalities cannot ensure that they will derive sustainable benefits and that the overall control environment and the systems within the municipality are improved with the use of consultants.

In addition, at 26 of the auditees that used consultants (63%), skills were not transferred. This is a result of either the contracts not specifying the transfer of skills as a requirement or, where it was specified, the transfer of skills not being monitored. Other findings included poor performance management and monitoring at 24 auditees (58%) and inadequate planning and appointment processes at 17 auditees (41%).

Way forward

The following should be addressed to use consultants more effectively and gain the most out of their appointments:

- The justification and extent of services to be contracted should be considered at a strategic level and should be approved by council. This should include the costs of contracted services versus the costs of filling positions or up-skilling staff, as well as reasons for procuring the services of consultants where there is a fully staffed finance unit
- The accounting officers should ensure that adequate and effective processes are put in place to manage the effective use of consultants.

- Transfer of skills should be included as a requirement in all contracts with consultants. This should be monitored to ensure that it is executed in terms of the contract and that sufficient time and resources are allocated to enable skills transfer.

8. Conditional grants

Government's priorities are articulated in the MTSF, where focus is placed on providing sustainable and reliable access to basic services including electricity, water, sanitation and refuse removal.

In support of these goals, grants are provided to municipalities to upgrade their infrastructure and build their institutional capacity. An MIG is provided to municipalities to upgrade their infrastructure, while the MSIG and the FMG are provided to enhance municipal capacity. This is to enable municipalities to improve coordination, accountability and performance management. These grants are conditional and can only be used for the purposes stipulated.

Figure 23: Municipal infrastructure grant

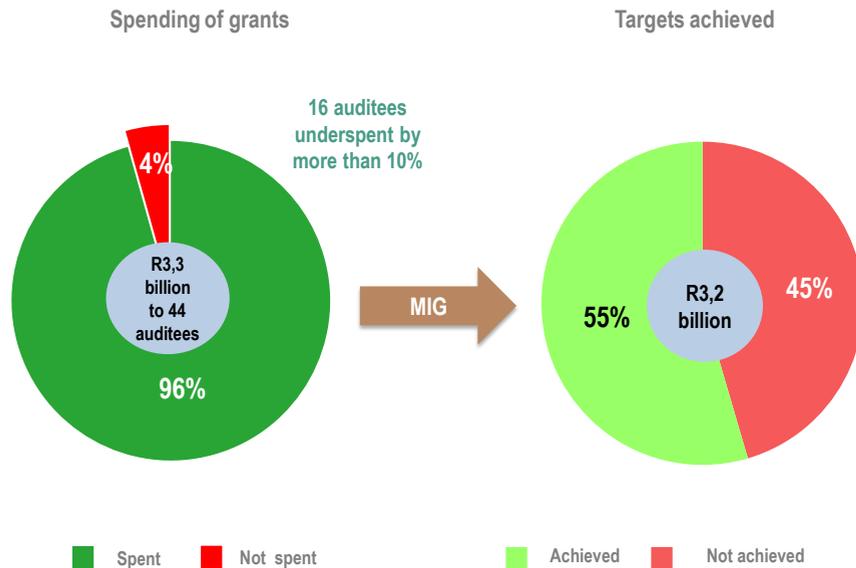
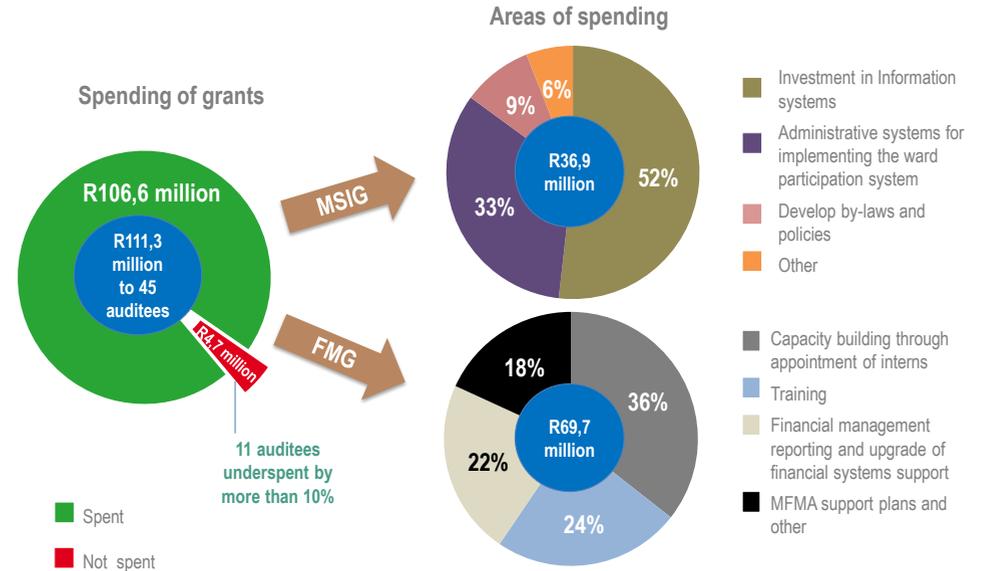


Figure 23 shows that most of the MIG was spent, yet only 55% of the planned targets relating to this grant were achieved. This raised the risks that municipalities spent the MIG without due regard to value for money and economical delivery of services, or there was fiscal dumping, whereby suppliers are paid without the services being delivered. Also of concern was whether value for money was derived from this spending and the actual use of the funds, as the targets of those funds had not been achieved. The risks correlate to the

high levels of non-compliance with SCM requirements and the high levels of irregular expenditure reported in the section 5 of this report. In addition, this had a negative impact on the municipalities' ability to deliver services to their communities and had implications for their financial viability, as additional funding will be required to achieve the original planned targets.

Figure 24: Analysis of MSIG and FMG spending



All the municipalities received FMGs while only 43 municipalities received the MSIG (the two metros did not receive this grant). Figure 24 shows how municipalities spent these grants and the capacity building areas on which they were spent. These areas were specifically selected by the National Treasury to ensure that municipal institutional capacity is strengthened. This should promote good governance and transparent and accurate reporting that will result in viable, sustainable and developmental municipalities that deliver effective services.

Figure 25: Analysis of outcomes where targets were reported as achieved by municipalities

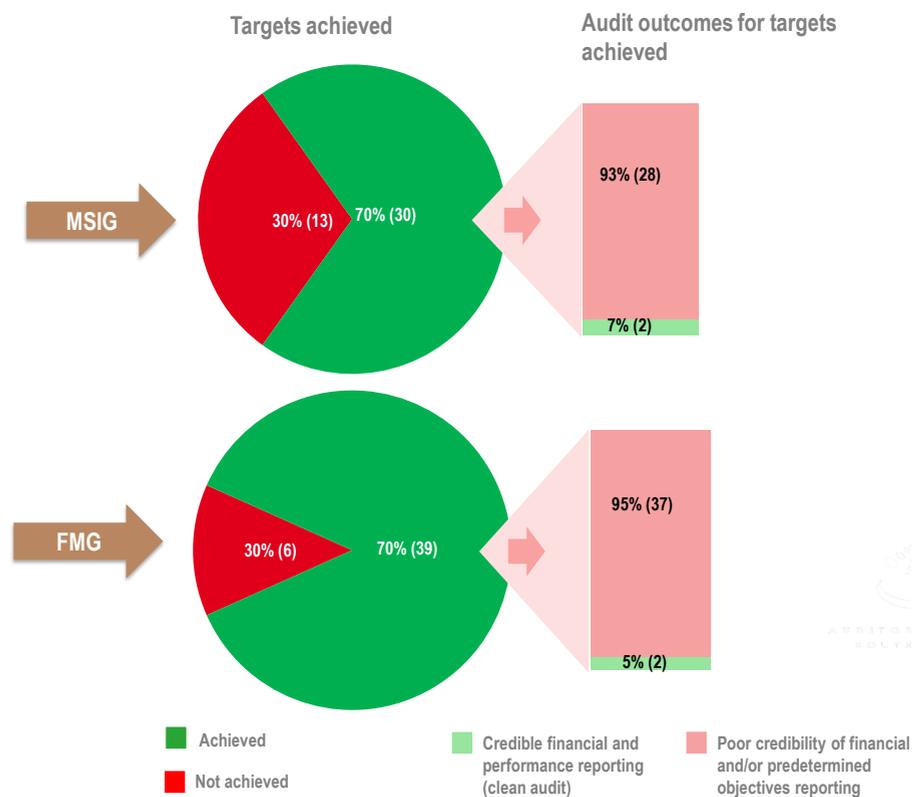


Figure 25 depicts the municipalities' achievements of the targets set for the MSIG and FMG and the impact that achieving planned targets had on credible financial and/or predetermined objectives reporting.

Only 70% of the planned targets for both the MSIG and FMG were achieved although most of these grants (96%) were spent. This highlights the possible risks that planned targets may not have been appropriate, that the achievement of targets was not properly monitored during the year and that services were acquired without applying the prescripts that result in the economical acquisition of goods and services or value for money. This correlates to the levels of non-compliance with SCM requirements and the high levels of irregular expenditure reported in section 5. The inability of municipalities to achieve the set targets prevents them from obtaining the full benefit and impact of the grants.

Figure 25 also shows that achieving the planned targets did not necessarily translate into credible financial and performance reporting. This lack of credible reporting is attributed to weak control environments where daily, weekly and monthly control activities are not adequately monitored and supervised. The planned indicators and targets relating to the MSIG and FMG did not measure their impact on the control environments of municipalities. As a result, the expected impact on financial and performance reporting did not materialise.

These shortcomings are attributed to poor planning, inadequate project management and a lack of in-year reporting, monitoring and follow-up. They also support our analyses of human resource practices, the use of consultants, irregular expenditure and financial viability contained in this report, as well as the concerns we highlighted in section 4 (annual performance reports). This indicates that the use of these grants has not had the desired impact on the quality of the administrative practices within the municipal environment.

9. Financial viability

Our audits included an analysis of the auditees' financial viability indicators to provide management with an overview of selected aspects of their current financial management status and practices. This analysis will enable timely identification and remedial action where the auditees' operations may be at risk due to poor financial management. Furthermore, the assessment indicates whether the municipalities provide services to the citizens in a sustainable manner, as required by the constitution. To deliver services to their residents and ensure the continuation of such services, municipalities need to carefully manage the money flowing in and the money being spent, as depicted in figure 26:

Figure 26: Cash flow management



As part of our assessment, we evaluated four aspects that relate to this balancing act:

- Whether the **financial position** of auditees was sound.
- Whether revenue collection was adequate to ensure a steady stream of income to finance service delivery activities (**revenue management**).
- Whether creditors were managed effectively (**meeting financial obligations**).
- Whether the **spending patterns** of auditees were sound.

Auditees in a poor financial position

Our assessment indicated that only three municipalities (7%) had good financial viability indicators. In evaluating the underlying reasons for this unfavourable situation, we analysed the drivers of financial viability. The main driver is the availability/ability of human resources to effectively manage financial resources.

This assessment excludes thirteen municipalities that received disclaimed and adverse opinions, as the financial statements of these municipalities are not

credible and would therefore distort the financial analysis. It is, however, critical that attention be paid to these municipalities as their finance units are unable to provide credible financial information and are therefore exposed to a high level of financial viability risk.

Based on the analysis performed on vacancies and competencies within the human resources section of this report, 59% of municipalities had a vacancy rate of 15% or more within their finance units. Furthermore, 45% of chief financial officers either had no qualifications or did not meet the required competency level or both. This is a serious concern considering the importance of skills in managing critical financial activities that impact financial viability. As analysed in the predetermined objectives section of this report, municipalities do not have processes to ensure credible performance planning and reporting. This has an impact on the planning and effective use of financial resources which, in turn, affects the financial sustainability of municipalities and, ultimately, their ability to deliver services efficiently and economically.

Revenue management

Debts owed to the municipalities should be collected within 30 days. Our analysis indicated that the collection of debts for services provided by municipalities remains a major challenge as 26 municipalities (81%) had a debt collection period of more than 90 days. At 31 municipalities (97%), more than 10% of their debts were assessed as irrecoverable. The long outstanding debts included money owed by provincial and national government departments, which is a concern. The process of converting receivables to cash is critical to maintain a healthy cash flow and a municipality's ability to meet their financial obligations. This process is also important in terms of ensuring that municipalities are able to meet their revenue projections as set out in their budgets, to fund their service delivery targets.

Municipalities need to generate their own revenue to be viable by providing services to their residents. Currently municipalities are reliant on grant funding to cover their operational and service delivery needs. This is, however, not sustainable as grant funding is limited and does not necessarily meet all of their financial requirements. Furthermore, municipalities are not adequately managing their infrastructure assets, which results in abnormal water and electricity distribution losses. These losses result in a loss of revenue, which impacts the financial sustainability of the municipalities.

Meeting financial obligations

In terms of legislation, creditors are to be paid within 30 days of receipt of invoices. Our analysis indicated that 16 municipalities (50%) paid their creditors after 90 days. These creditors include small and medium companies, which could affect their sustainability and local economic development (LED). This is a significant regression from the previous period and further illustrates the

importance of capacitating the finance units. Only then will the municipalities be in a position to effectively manage their revenue generation, debt collection, cash flows and the effective, efficient and economic use of available resources.

Spending patterns

Municipal spending, which is mainly made up of capital and operational spending, should be aligned to service delivery priorities.

A **capital budget** is part of the approved annual budget set aside for developing and improving infrastructure such as roads and water and sanitation systems, or to purchase assets such as ambulances and refuse removal trucks. As many municipalities cannot raise enough revenue through rates and taxes to fund infrastructure projects and improvement programmes, national government contributes through **conditional grants**. Our analysis indicated that fourteen municipalities (44%) had underspent their conditional grants by more than 10% and 17 municipalities (53%) had underspent their capital budget by more than 10%. Continued underspending over time could have a negative impact on the delivery of services to communities.

Way forward

For local government to operate in a sustainable manner, the following should be implemented:

- Revenue enhancement strategies should be developed and implemented to ensure that the municipalities are capacitated to generate their own revenue.
- Municipalities should consider including debt collection as part of their performance plans and cascade it down to the individual performance agreements of senior managers. Improved collection patterns would assist in improving the financial viability of municipalities and will lead to increased funding being available for service delivery initiatives.
- Priority should be given to capacitating finance units with adequately skilled and competent people who will drive the revenue generation and collection strategies. This will ensure the financial sustainability of municipalities and improved cash flow management, including paying creditors on time.
- Municipalities need to develop adequate LED strategies to generate adequate economic activities in their areas. This will improve the standard of living of citizens and create sustainable revenue bases. Furthermore, the LED departments should be adequately capacitated with suitably qualified staff and adequate resources and support to implement the LED strategy.
- Municipalities should limit the use of external service providers and should monitor and control the costs associated with the services provided by them to improve financial sustainability.

10. Information technology systems

Information technology (IT) controls ensure the confidentiality, integrity and availability of state information, enables service delivery and promotes national security. It is thus essential for good IT governance, effective IT management and a secure IT infrastructure to be in place.

Effective **IT governance** is essential for the overall well-being of an organisation's IT function and ensures that the organisation's IT control environment functions well and enables service delivery. An IT governance framework is being developed by a national coordinating and monitoring structure that was established by the minister of CoGTA. The framework is in draft format and currently undergoing a consultative process with the objective of achieving final approval and implementation during the 2015-16 financial year.

Our audit also included an assessment of the IT controls that focus on security management, user account management and IT service continuity. There has been little improvement since the previous year in the number of auditees that had findings on IT controls. The most common findings were as follows:

Security management:

Security management findings were reported at 51% of the municipalities, which is a regression of 5% from the previous year. The regression is due to the inclusion of five auditees that were not included in the audit coverage in the previous year, most of which had security management findings.

IT-related policies and procedures had not been reviewed and approved to ensure that they would be properly implemented and enforced. The security of critical files containing financial data to be uploaded onto electronic file transfer systems was also not properly managed. In most district municipalities and high-capacity municipalities it was noted that access to these critical files was not restricted and that the files were in a format that could be edited.

User access management:

User access management findings were reported at 70% of municipalities, which is a similar percentage than last year.

The key findings related to the inappropriateness of users' access privileges, a lack of approved user access management procedures, inadequate processes for creating new user accounts, terminating former employees' user accounts and reviewing and monitoring administrators' activities.

The use of informal controls introduced a number of vulnerabilities in municipalities' systems. For instance, the lack of formally implemented controls

gave rise to users obtaining a level of access to municipal systems that was not in line with their job descriptions. Such access gave users the ability to make changes to supplier details, meter readings and employee details, such as leave and banking account information.

Information technology service continuity:

Service continuity findings were reported at 55% of municipalities, which is a regression of 12% from the previous year. The regression is due to an additional five municipalities being included in the audit coverage, all of which had findings on service continuity.

There was a lack of approved disaster recovery plans and backups were not consistently taken and tested for restorability.

The lack of appropriate IT skills and competencies is at the core of the IT findings referred to above as only 33% of the municipalities had appointed chief information officers. Furthermore, in most of these cases, the appointment was at a level lower than a section 57 manager. As a result, the chief information officers were unable to adequately influence the strategic direction of the IT services within municipalities.

Government has realised that many of the financial management systems (computer packages) used by municipalities do not support all the complex and sophisticated business environments of local government. This is a contributing factor for achieving poor audit outcomes. The standard chart of accounts project being implemented by National Treasury is expected to improve the financial management systems of local government.

Way forward

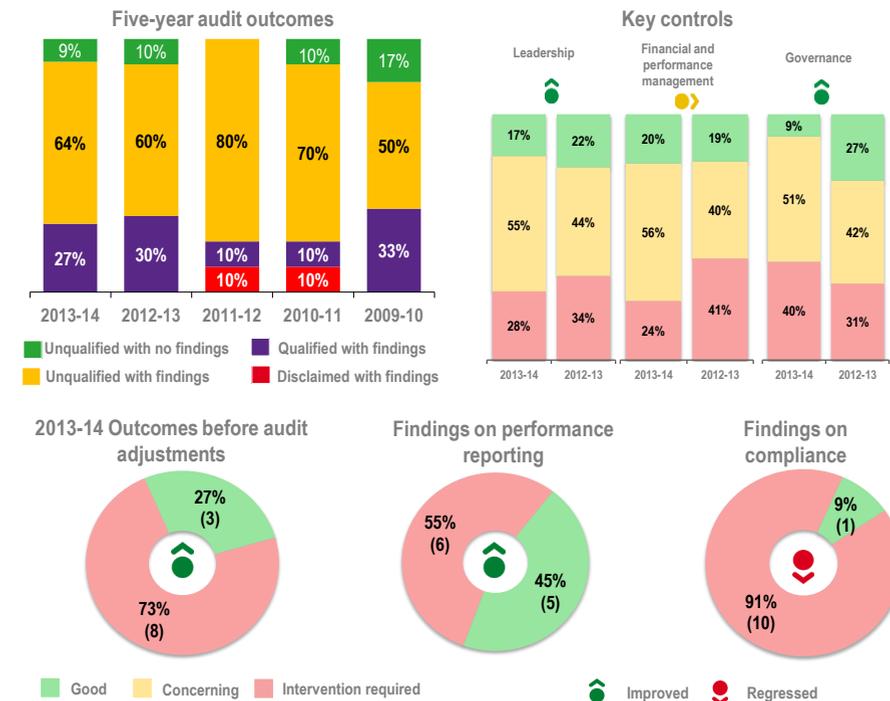
Municipalities must attend to the IT control weaknesses highlighted above as a matter of urgency. The weak IT controls identified not only increases the risk of fraud but may also undermine the improved audit outcomes of the local government sector in the province.

To address the root causes of IT findings, it is very important that municipalities plan for, budget, and attract the required IT skills. Provincial CoGTA and provincial treasury should assist municipalities to address their IT findings by providing appropriate support in the form of skilled personnel, grants and training. The South African Local Government Association should assist municipalities in improving the skills of the existing IT personnel by providing appropriate training to them.

11. Municipal entities

The Eastern Cape currently has 11 municipal entities. These entities, however, only represent 1% of the province's total municipal budget and were therefore excluded from the overall analysis. Municipal entities are independent organisations (although they are under the ownership control of the parent municipality) that perform municipal services on behalf of the municipality. Given the nature of these entities and the reason for their establishment, it is of concern that 55% of the entities had material findings on the quality of their annual performance reports. Material findings on compliance were reported at 91% of the municipal entities. These matters point to a weak control environment and the fact that the inadequate execution of controls and deviations from legislation were tolerated, which is unexpected given the relatively small size of most of these entities.

Figure 27: Audit outcomes of municipal entities



Although the outcomes of most entities are on par or better than the outcomes of their parent municipality, the overall outcomes of municipal entities have still shown a regression from the previous year. This was because of the deterioration in the drivers of internal control. Although the controls that require intervention did show a slight improvement, controls that were assessed as

sustainable in the previous year had not been monitored to ensure that they operated effectively during the year under review, which ultimately led to the overall regression of key controls.

While it is pleasing that no entities received a disclaimed or adverse opinion, 27% of the municipal entities received a qualified opinion. A further 37% of the entities only avoided qualification through adjustments identified during the audit process.

As in the previous year, the Nelson Mandela Bay Development Agency (NMBDA) was the only auditee to receive an unqualified audit opinion with no findings. The only other entity to achieve a clean audit over the past years was Joe Gqabi Development Agency in the 2010-11 financial year. NMBDA is the only entity that has sustainable governance controls and a control environment supporting continued clean administration and good governance. This environment enhances the credibility of information used for enforcing accountability. These best practices can be copied not only by other agencies, but by the metro as well.

Overall, 51% of the governance-related controls at municipal entities were still being implemented while 24% required intervention, meaning that governance structures at these auditees did not yet have a positive impact on audit outcomes.

Way forward

The council, and more specifically MPAC, should ensure that the board of the municipal entity is aligned to the objectives of the municipality to enhance the oversight and governance of the entities. This should include steps to ensure that there are sound internal controls, which will not only lead to an improvement in audit outcomes but also to enhanced service delivery through the achievement of performance targets

The member of the executive council (MEC) for Local Government and Traditional Affairs should assess the fiscal discipline, good governance principles and viability of these entities, to ensure that they deliver on the mandate for which they were originally established, and that their resources are used in an economical, effective and efficient manner.

12. Key controls

A key legislated responsibility of accounting officers, senior management and officials is to implement and maintain effective and efficient systems of internal controls. As part of our audits, we assessed auditees' internal controls to determine the effectiveness of their design and implementation in ensuring reliable financial and performance reporting and compliance with key legislation. To make it easier to implement corrective action, we have categorised the

principles of the different components of internal control under leadership, financial and performance management and governance.

Figure 28: Key Controls

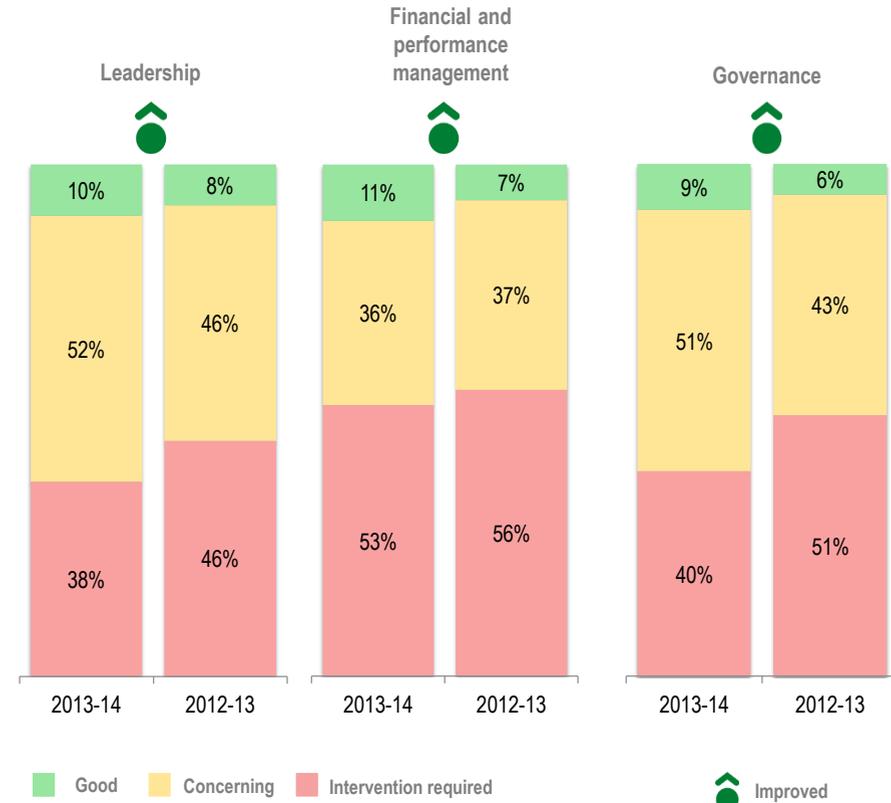


Figure 28 provides an overall assessment of the drivers of key controls and the movement since the previous year, based on the significant internal control shortcomings identified during the audits. It is clear from figure 28 that, on a provincial level, we only see a marginal improvement in the control environment. The slight improvement in the control arena does not directly correlate to the 24% improvement in audit outcomes. This is due to the majority of outcome improvements being as a result of audit adjustments and the use of consultants and not necessarily a result of an improvement in the control environment.

The slow movement in these controls remains reason for serious concern and underlines the need for political leadership intervention. Implementing the basic key controls has been a focused message of ours for the past five years and formed the basis for numerous interactions. In addition, this has been reported on in detail in four previous general reports. The non-implementation raises questions on how serious leadership is to turn financial administration around.

Sarah Baartman and Senqu should serve as examples to the other municipalities. They have illustrated that by responding to our messages and maintaining a sound control environment throughout the year, a clean audit can become a reality rather than merely a goal.

Way forward

A control environment can only be effective if it is properly resourced and maintained. It is critical for leadership to address the weaknesses of vacancies, instability and consequence management reported in section 6 of this report to ensure that the foundation is in place.

To improve the status of internal control in a sustainable manner, the leadership must:

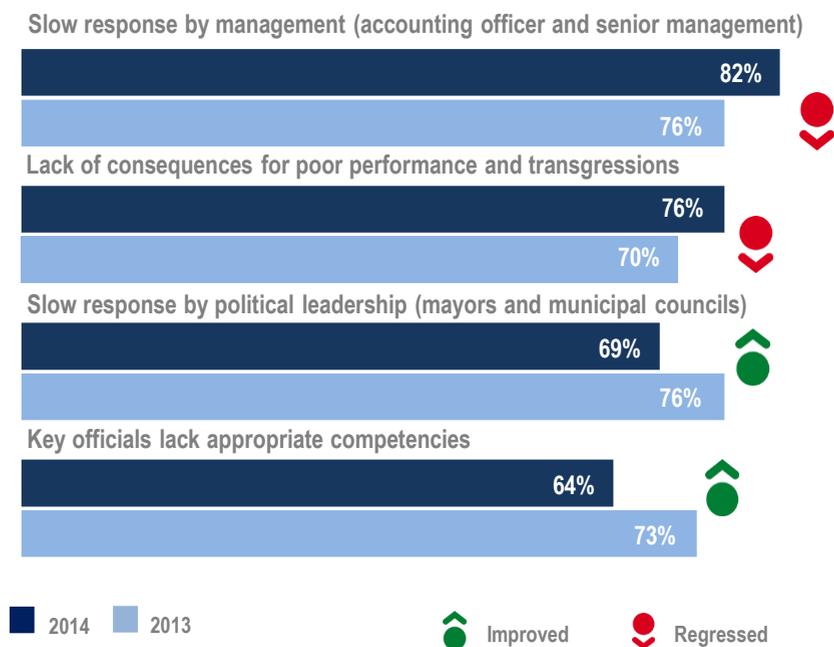
- take ownership of key controls and ensure that adequate daily, weekly and monthly controls and reconciliations are effectively implemented and monitored.
- show an appreciation of the role that consequence management plays in restoring accountability, integrity and public confidence in the system of provincial government.
- guide the work plans of internal audit units and audit committees to focus on the key internal control challenges faced by auditees, to provide the leadership with focused and timely feedback on sustainably addressing these shortcomings.
- ensure that recommendations from internal audit units and audit committees are developed into actions plans that are adequately implemented and monitored to ensure improved outcomes.

13. Root causes

Our audits included an assessment of the root causes of audit findings. These root causes are constantly reported to all levels of leadership. We constantly highlight that, should these root causes not be addressed, the errors will recur and sustainable improvement will not be possible. The repetitive nature of the identified root causes over the years shows that municipalities do not address the root causes as highlighted in our messages and recommendations, but rather focus on the symptoms of findings. This is not a sustainable practice and underpins the 25 cumulative regressions over the past five years.

The information that follows summarises the four most common root causes of the audit outcomes, provides recommendations to address the root causes and identifies the role players responsible for addressing such root causes.

Figure 29: Root causes to be addressed



Slow response to our messages

Slow response by management, accounting officers and senior management

At our regular interactions with municipal managers and senior management we discuss the audit and management reports, audit findings, the status of the key controls and the root causes that underpin the findings and audit status. We also obtain and follow up on these at subsequent interactions. Despite these interactions, commitments from leadership to address our findings as well as follow up interactions, management at 82% of municipalities have not taken our messages of improving audit outcomes seriously and have not taken timely action to address our previously reported findings and root causes.

This raises serious concern about the disregard of section 62 of the MFMA that states *the accounting officer is responsible for managing the financial administration of the municipality.*

The increase in auditees with this root cause is of concern and points to leadership not being serious about obtaining sustainable solutions for the findings raised in our audit reports.

Municipal managers should take ownership of addressing our messages by making the appropriate commitments and, in turn, translate these commitments into resourced action plans.

Slow response by political leadership (mayors and municipal councils)

With reference to the highlighted slow response of management to our findings and messages, we noted that the political leadership at municipal level is not leading by example. A slow response by political leadership to our messages was recorded at 69% of municipalities. During our interactions with mayors, municipal councils and MPACs, we discuss and provide feedback on findings in audit and management reports, status of the key controls and root causes.

The outcomes and repetitive nature of findings illustrates that political leadership at a large number of municipalities, in the same vein as management, have not taken our messages seriously and have not delivered on their previous year's commitments. Section 131 of the MFMA states *a municipality must address any issues raised by the Auditor-General in an audit report. The mayor of a municipality must ensure compliance by the municipality with this subsection.*

Change and corrective measures start at the top and the political leadership must embrace this challenge by ensuring that they implement the commitments they make to address audit findings and, ultimately, the audit outcome of the municipality. They should, in turn, hold management accountable to honour their commitments and action plans for sustainable improvement.

Lack of consequence for poor performance and transgressions

A lack of consequence management for poor performance and transgressions increased from the previous year and is prevalent at 76% of municipalities. Not holding people accountable creates the perception that it is acceptable to continue with inappropriate behaviour. This in turn creates the platform for the lack of discipline around financial and performance reporting. Poor performance by staff involved in delivering services will affect service delivery to citizens and the efficiency with which this service is delivered. If this is not addressed, there will be no noticeable improvement in the control environment, quality of financial statements and performance reports and, thus, no improvement in overall audit outcomes.

Auditees need to ensure that a robust performance management system is implemented, which is linked to strategic planning documents. Performance agreements must be implemented at all levels. These agreements should record the expected level of performance, provide for recognition of those employees who perform well and provide for consequences in the case of poor performance. It is very important for the political and administrative leadership to

be proactive in implementing performance reviews and following up poor performance. This will enforce a culture of accountability.

Key officials lack appropriate competencies

Staff at 64% of municipalities do not possess the appropriate competencies to perform their required roles and responsibilities. Although there has been a slight improvement in this root cause since the previous year, it is still a large contributor to the unfavourable audit outcomes. Certain staff do not have the required ability, skills and qualifications to carry out the requirements of their positions. This includes employees who were appointed without the minimum competencies or those that have failed to update their competencies with ongoing training and development.

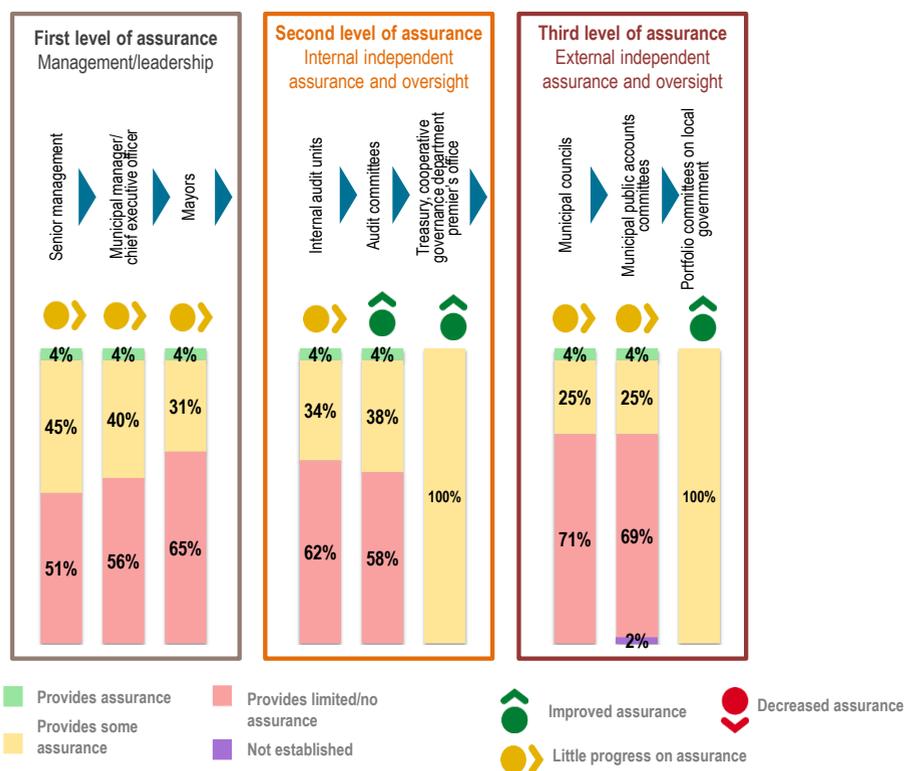
The limited number of municipalities that were able to improve on this root cause appointed skilled staff, conducted training interventions with existing staff and received a transfer of skills where consultants had previously been used.

Going forward, management must ensure that appointments made have shown adequate proof to support the minimum competencies required for the role. In addition, management must ensure that they identify employees who lack the appropriate competencies and implement interventions such as ongoing training, development, coaching and mentoring to ensure that all staff have the competencies that their positions require.

14. The level of assurance provided and the impact of these role players on audit outcomes

The poor status of the drivers of internal controls highlighted in this report reflects the inadequate assurance provided by those role players that have a direct impact on the municipalities. The direct link is that if controls are not in place, credible information is not passed up the assurance chain and the other assurance providers are hampered in executing their responsibilities of providing assurance. Those responsible for the first level of assurance are responsible for a break in the value chain.

Figure 30: Assurance provided by key role players



First level of assurance

Senior management

Senior management, which includes the chief financial officer, chief information officer and head of the SCM unit, provides assurance by implementing basic financial and performance controls.

Only a very limited number of role players at this first level were able to fully provide the required level of assurance. Municipal managers and mayors relied on senior management for implementing basic financial and performance management controls. These controls include the following:

- Ensure proper record keeping so 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 of transactions.

- Prepare regular, accurate and complete financial and performance reports that are supported and evidenced by reliable information.
- Review and monitor compliance with legislation.
- Design and implement formal controls over IT systems.

The poor internal control environments are not conducive to producing accurate and reliable information. As a result there is a risk that the leadership is using information for decision-making that may not be credible. This can impact the quality of decision-making.

Going forward, the human resource management challenges outlined in this report should be addressed as a matter of urgency. This includes filling all critical vacancies with the appropriate skills and competencies and holding senior management accountable for executing their responsibilities through a strict system of performance management.

Municipal manager

Municipal managers are responsible for auditees' internal controls, including leadership, planning, risk management, oversight and monitoring. While municipal managers depend on senior management for designing and implementing the required financial and performance management controls, they should create an environment that helps to improve such controls. They should also implement consequence management to ensure accountability.

The assurance provided by municipal managers is not at the level required to create an environment conducive to credible decision-making. In exceptional cases, some municipal managers were able to provide some assurance due to the assistance received from consultants.

This is not a sustainable practice, however, as it addressed the symptoms rather than the root causes. The present weaknesses in effective leadership, planning, risk management and oversight and monitoring functions do not support sustainable practices that will lead to improved audit outcomes. Going forward, the leadership should create an environment that enhances the improvement in controls by focusing on the following:

- Provide effective and ethical leadership, and exercise oversight of financial and performance reporting and compliance with legislation.
- Implement effective human resource management to ensure that adequate and sufficiently skilled staff are employed.
- Set the correct tone to improve the performance and productivity of staff by implementing sound performance management processes, evaluating and monitoring performance, and imposing proper consequences for poor performance.

- Establish policies and procedures to enable sustainable internal control practices, and monitor the implementation of action plans to address internal control deficiencies.
- Establish an IT governance framework that supports and enables the achievement of objectives, delivers value and improves performance.
- Implement appropriate risk management activities to ensure that regular risk assessments, including the consideration of IT risks and fraud prevention, are conducted and that a risk strategy to address the risks is developed and monitored.
- Ensure that an adequately resourced and functioning internal audit unit and audit committee are in place and that their reports are responded to.

Mayor

Mayors have a monitoring and oversight role within municipalities. They have specific oversight responsibilities in terms of the MFMA and the Municipal Systems Act, which include reviewing the integrated development plan and budget management as well as ensuring that auditees address the issues raised in audit reports. Mayors can bring about improvements in their auditees' audit outcomes by being actively involved in key governance matters and managing the accounting officers' performance.

Information presented by senior management was not credible and as a result, mayors were unable to make informed decisions based on sound financial information. Mayors have therefore not provided the required level of assurance; this was confirmed through our interactions with them. The mayors should implement corrective action where necessary, as it remains their responsibility to enforce accountability and set the right tone from the top.

Over the past years, we have increasingly engaged with mayors on how they can improve the audit outcomes of their municipalities. This includes discussing the status of key controls and mayoral commitments to improve audit outcomes, while sharing identified risks. At an overall level, these interactions were well received. The impact of these interactions was, however, dependent on the political will of the mayor concerned and their commitment to change. Those mayors that were responsive towards our messages and implemented our recommendations made improvements in the levels of assurance provided and, ultimately, their audit outcomes.

Going forward, a decisive and pro-active leadership tone is required that instils a culture of accountability and good governance.

Second level of assurance

Internal audit and audit committees

Internal audit units assist accounting officers and authorities in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation.

An audit committee is an independent body that advises the council, mayor, accounting officer or authority and senior management on matters such as internal controls, risk management, performance management, evaluation and compliance with legislation. The committee is required to provide assurance to the council on the adequacy, reliability and accuracy of financial reporting and performance information.

The impact on audit outcomes and the assurance provided by these pivotal role players have been limited. It is clear that the effectiveness of these structures is hampered by poor resourcing and management not responding to their work and reports. Repetitive findings and the failure to address root causes also raise the question of whether internal audit units and audit committees are focusing their efforts on risk management and on improving the systems to enhance the credibility of information through implementing the necessary controls. Going forward, risk assessments should ensure that the proper weighting is assigned to this area, while responses to those risk assessments should be focused on systems and controls that entrench the credibility of information in the daily operations of the auditee.

Mayors, municipal managers and senior management are urged to recognise these structures as key partners in the accountability chain, to resource these structures appropriately, and to react seriously to their work.

Co-ordinating departments and their executive leadership (provincial treasury, Office of the Premier and the provincial Department of Cooperative Governance and Traditional Affairs)

The Constitution stipulates that provincial government must support and strengthen the capacity of municipalities to manage their own affairs, to exercise their powers and to perform their duties. The MFMA further requires provincial government to assist municipalities in building capacity to support efficient, effective and transparent financial management. The provincial departments that have a direct role to play in supporting and monitoring local government, and thereby providing a level of assurance, are the provincial treasury, CoGTA and the Office of the Premier. Our assessment of the assurance provided by these departments is based on their initiatives to support and monitor local

government and the impact they have had on improving the internal controls of auditees.

The success of these departments' interventions was hampered by the fact that not all municipalities cooperated with the assistance provided and the mayors and municipal managers of these municipalities did not take ownership and accountability for the process. Furthermore, inappropriate assistance was provided as the need and/or root causes were addressed in a one-size-fits-all approach.

• **Provincial treasury**

The provincial treasury is a critical role player in provincial government and has responsibilities in terms of the Constitution and the MFMA to support and strengthen the capacity of municipalities to manage their own affairs, to exercise their powers and to perform their duties. Provincial government, with the provincial treasury as custodian, must also assist municipalities in building capacity to support efficient, effective and transparent financial management. The following are the main areas of assistance that the provincial treasury provided to municipalities:

- Technical support and compliance monitoring, where the provincial treasury deployed staff to nine municipalities to support the chief financial officers.
- Ongoing training on minimum competency levels; the outcome of this is analysed in the human resource section
- The provincial treasury, together with CoGTA, had a drive in the current year to assist municipalities with the recovery of debts owed by provincial and national departments.

• **Department of Cooperative Governance and Traditional Affairs**

The Eastern Cape CoGTA is a crucial role player within the local government environment. The Constitution requires the department to support, intervene and monitor municipalities, while ensuring good governance, the delivery of basic services and infrastructure development, as well as coordination and integration with other spheres of government. The department remains pivotal in ensuring solid economic growth, poverty alleviation and job creation within the context of a developmental local government agenda. This developmental role is accompanied by the provision of adequate institutional and administrative support and financial resourcing. The department implemented a two-tier approach to assist municipalities in addressing poor audit outcomes and service delivery matters. This entailed providing support through the operation clean audit initiative and through other initiatives.

Operation clean audit support

The operation clean audit support was geared towards assisting municipalities that had previously received adverse or disclaimed audit opinions by:

- addressing issues raised in previous year's audit reports
- developing, documenting and ensuring implementation of internal controls
- transferring skills from operation clean audit teams
- preparing to compile annual financial statements and audit readiness
- seconding staff in critical vacancies
- continuous engagement and interaction with all relevant stakeholders.

The support ensured that at least four municipalities moved from a disclaimed or adverse audit opinion to a qualified audit opinion; however, this equates to only 36% of municipalities supported and questions the impact of this initiative.

Other support

The other support focused on regular visits to auditees with unqualified and qualified opinions. However, these visits did not have the desired impact as four auditees regressed and 20 remained unchanged. Other initiatives included the following:

- The MEC signed performance agreements with all the mayors.
- An administrator was appointed at Inkwanca after the council was dissolved. The assistance was too late to have an impact and there were limited resources within the finance section.
- Ad hoc interventions where critical gaps were identified. This was in the form of either providing service providers, seconding officials from the departments or financial assistance.
- Accountability sessions convened by the MEC, whereby the political and administrative leadership of municipalities with disclaimed/adverse opinions had to avail themselves to the MEC and provide feedback on progress to improve audit outcomes and the status of action plans.

Challenges that affected the impact of initiatives

The department experienced challenges with municipalities not cooperating with the assistance provided. Only 23 of 45 municipalities submitted turnaround plans to CoGTA. Mayors and municipal managers of these municipalities did not take ownership and accountability for the process. Furthermore, assistance was not focused on the entity-specific need and/or root causes, but was rather generic in nature.

• Office of the Premier

The Office of the Premier has an important role to play within the administration of the province, which includes coordinating and supporting local government. This is in line with the Constitution, which requires these offices to administer, develop and implement national and provincial policy and legislation and coordinate and support the functions of the provincial administration and its departments. A further critical part of their mandate is to promote and enable intergovernmental relations and a cooperative government.

In terms of the MTSF and the back-to-basics approach, cooperative governance must be strengthened to enable better service delivery that can improve the lives of the citizens. The MTSF further requires that this office, in collaboration with CoGTA, strengthen and support the planning and delivery of services by municipalities. The Office of the Premier therefore has a critical role to play in taking accountability and enabling all political and administrative leadership to meet the goals as set out in these documents. It is crucial that they support and assist capacity building within the province to ensure that the principles of the back-to-basics approach can be effectively implemented and monitored and, where necessary, corrective action can be taken. The Office of the Premier has therefore included the MTSF deliverables in its current annual performance plan. Going forward, its technical support unit will provide more direct support and intervention to King Sabata Dalindyebo, the Buffalo City metro and the Nelson Mandela Bay metro in the drive towards clean administration.

We raised a concern in previous years about the lack of coordination between the Office of the Premier, the provincial treasury and CoGTA in terms of the nature and timing of their support. This lack of coordination has resulted in a lack of ownership and accountability, as well as the ineffectiveness of the support rendered. As these role players have a limited capacity of finance and skills, it is very important that they work together and pool their resources to have a greater impact and to avoid a duplication of efforts. The Office of the Premier should play the leading role in this area.

• Provincial executive (Troika)

The four critical commitments that could directly impact on improved outcomes were reaffirmed by the new political Troika:

- **Premier** - The drive to clean audit will become a more prominent standing agenda item at all Exco meetings, with reporting from the provincial treasury and CoGTA as well as robust debate by the role players. Cognisance is taken of the fact that this commitment has been implemented. However, it remains critical that both the provincial treasury and CoGTA provide Exco with meaningful and credible data at these meetings to ensure focused attention and maximum impact.

- **MEC for finance and MEC for CoGTA** - Improved liaison between the provincial treasury, the Department of Local Government and Traditional Affairs and the operation clean audit unit, who together make up district support teams. This commitment remains in progress and leadership is urged to ensure that the process gains momentum.
- **MEC for finance** - The provincial treasury is to set up a district monitoring committee consisting of the provincial treasury, the Department of Local Government and Traditional Affairs and the district municipality, to provide an oversight role and review the state of projects and municipalities quarterly. As with the previous commitment, the implementation is slow with no visible impact.
- **MEC for CoGTA** - The MEC will drive a process to achieve leadership stability at the highest level within the municipalities that are politically unstable. This remains an ongoing commitment.

Third level of assurance

Council and municipal public accounts committee

The council is required to provide assurance through monitoring and oversight. This includes approving or overseeing certain transactions and events as well as investigating and acting on poor performance and transgressions, such as financial misconduct and unauthorised, irregular as well as fruitless and wasteful expenditure. MPAC is a council committee that is responsible for improving governance, transparency and accountability. This committee is an important provider of assurance; it is required to give assurance to the council on the credibility and reliability of financial and performance reports, compliance with legislation and internal controls. It must be noted that to a large extent, these structures are inhibited from effectively fulfilling their responsibilities by the inability of senior management and the municipal managers to provide credible information for oversight purposes.

This is, however, not the only concern relating to the responsibilities of council that impacted on the level of assurance provided by council. Section 131 of the MFMA clearly states that a municipality must address all issues raised by the auditor-general and charges the mayor to ensure compliance. The year on year repetitive nature of audit findings indicated in this report, on financial statements, reporting on predetermined objectives and compliance with legislation, show that section 131 is not adhered to and not effectively overseen by council.

In addition, section 32 of the MFMA charges councils to investigate all unauthorised, irregular and wasteful expenditure incurred and to determine whether money should be written-off or recovered from officials. Section 5 of this report very clearly illustrated that this critical function of councils is not executed.

The Association of Public Accounts Committees has been active in training councillors on oversight functions. This intervention is relatively new and has thus not yet achieved its full impact.

Provincial legislature and portfolio committee on CoGTA

Legislatures have the crucial role of conducting oversight by monitoring and reviewing the actions of the executive organs of government. This mandate is exercised through portfolio committees, who scrutinize executive authority decisions on the implementation of service delivery programmes. This executive authority includes the MEC for local government and traditional affairs and other executives involved in local government, such as the MEC for finance.

The mechanism used to conduct oversight of local government is the portfolio committee on CoGTA. Members of this portfolio committee have visited some municipalities to get first-hand knowledge of the status of the municipalities and to act on this knowledge. The intervention was new and was not in place for most of the year; thus, it had no impact on improving the assurance provided.

Way forward

The management and leadership of the auditees and those that perform an oversight or governance function should work towards improving the key controls, addressing the root causes and ensuring that there is an improvement in the six key risk areas, thereby providing assurance on the quality of the financial statements and performance reports as well as compliance with legislation.

The roles of the municipal manager and the actions that council needs to take to drive the municipality towards clean administration, as highlighted in this report, is critical to enhance assurance. Only when the municipal manager enforces accountability and ensures timely, credible and transparent records and reports, can council effectively enhance their oversight function and enhance the assurance that they provide. Then all role players and decision-makers can take comfort in the knowledge that all information presented to them is credible and that their decisions are based on accurate information.

Further, it is imperative that the Office of the Premier strengthen intergovernmental relations to ensure that all public institutions that have a role to play in providing services to the citizens within local government are adequately coordinated. This would include oversight of the two coordinating departments of CoGTA and provincial treasury, which have a direct bearing on the functioning of municipalities.

Oversight by the relevant portfolio committees of Legislature should be enhanced by monitoring the implementation and impact of turnaround and support plans of the coordinating departments. It is also necessary for these committees to work together and not in isolation to ensure maximum impact of their processes on the local government sphere.

15. Conclusion

For local government to be positioned to achieve the goals as set out in the MTSF and the five key performance areas of the back-to-basics approach, it is imperative that each role player diligently executes their responsibilities. In this manner leadership can build a professionalised local government that embraces the concepts of transparency, accountability, and credible and reliable financial and performance reporting. The enabling role of the municipal manager and the oversight functions of councils will play a pivotal role in creating an environment where effective, efficient and economical service delivery and a clean audit outcome is a natural outflow of doing the right things at the right time.

TESTIMONIES, CLEAN AUDITS AND SUCCESSFUL SERVICE-DELIVERY PROJECTS



**Cllr Kekana
Mayor**

Sarah Baartman District

'The district municipality attained a clean audit by enhancing their daily disciplines around financial and performance reporting as well as maintaining stringent oversight processes by MPAC, the council and the audit committee.'

Clean administration and service delivery field visits

We conclude this report by sharing some success stories of municipalities that have both achieved clean audits and effectively delivered infrastructure projects to improve the lives of their citizens. The section firstly gives some background on the auditor-general's (AG) field visits to these municipalities, then lists key characteristics that have had a positive impact on the audit outcomes and service delivery of these municipalities, and lastly details specific projects before touching on the way forward.

The table below shows the 2013-14, 2012-13 and 2007-08 audit outcomes of the municipalities in the province that achieved clean audit outcomes in the current year.

Table 3: Comparison of current year, previous year and 2007-08 audit outcomes of municipalities with clean audits

Auditee	Auditee type	2013-14 audit outcomes	2012-13 audit outcomes	2007-08 audit outcomes
		Audit opinion	Audit opinion	Audit opinion
Sarah Baartman District	DM	Unqualified with no findings	Unqualified with findings	Unqualified with findings
Senqu	LM	Unqualified with no findings	Unqualified with findings	Qualified with findings

Legend (audit outcomes)
Unqualified with no findings
Unqualified with findings
Qualified with findings
Adverse with findings
Disclaimed with findings
Audit not finalised at legislated date
New auditee

M = metropolitan municipality
 DM = district municipality
 LM = local municipality
 ME = municipal entity

The field visits were part of our effort to put a face to the concept of a clean audit as well as demonstrate that it is all in the hands of the leadership to restore confidence in local government. It is our earnest desire that all entrusted with

financial management and oversight responsibilities in local government can take some useful lessons from the better practices of these municipalities. We applaud all of them for blazing a trail in this effort towards good financial management and governance.

Background

In the first three months of 2015, AG Kimi Makwetu and staff from our office visited different municipalities across the country that had received clean audits. As previously explained, an auditee achieves a clean audit (or an unqualified opinion with no findings) when the financial statements are unqualified and we report no findings on either reporting on predetermined objectives or compliance with key legislation.

The aim of the field visits was to observe, first hand, the correlation between clean audit outcomes and service delivery achievements as well as to identify the key characteristics of these clean audit municipalities.

The leadership of these municipalities had an opportunity to reflect on the importance of clean administration as a catalyst to drive service delivery, showcase their governance structures as a critical area in ensuring the attainment of clean audit outcomes, and accompany the AG and his team on visits to key projects.

In this regard, we are now in a better position to confirm that these clean audits do not come on the back of the non-delivery of services, as demonstrated by the projects described further on in this section. The same practices applied by these municipalities over the last few years in achieving clean audits were also evident in the management of the projects visited. These included using action plans with clear timelines; officials being assigned specific roles and responsibilities and being adequately supervised and monitored by senior management; employing skilled people in key positions, such as engineers; a healthy interface between the administrative and the political leadership; and effective oversight by governance structures, such as audit committees.

The observations made during the visits should not be regarded as an audit, but we considered it worthwhile to share the good practices noted during the visits to municipalities across the country, as these could benefit other municipalities struggling to achieve clean administration and grappling with service delivery challenges.

Key characteristics that have had a positive impact on audit outcomes and service delivery

Leadership

- The roles of the council and the administration are clarified and understood, and they actively participate in forums to promote a common vision for good governance through accountable financial and performance management and compliance with legislation.
- The municipal leadership displays a great awareness and understanding of what municipalities have to achieve on a daily basis, both from a financial management and governance perspective as well as a service delivery point of view.
- They have suitably qualified officials to implement the disciplines around financial management and good governance, which are supported by dedicated political leaders who monitor and ensure that these disciplines are implemented.
- Credible action plans are developed and implemented to correct the internal control deficiencies we had highlighted in previous years.
- The monitoring of the implementation of action plans is a standing agenda item at meetings of councils and audit committees on a quarterly basis.
- Particular attention is paid to the systems used to manage and report on their performance while corroborating their service delivery reports, apart from being able to produce credible accounts on their revenue, expenses, liabilities and assets.

Financial and performance management

- Basic internal controls and systems, including performing daily, monthly and quarterly reconciliations of their financial records, are embedded in the control environment of municipalities.
- Proper record keeping is implemented in a timely manner to ensure that complete, relevant and accurate information is accessible and available to support financial and performance reporting.
- Regular, accurate and complete financial and performance reports are prepared and supported by reliable information.
- Measures are implemented to ensure that legislated duties are performed and that prohibited transactions are prevented to ensure compliance with regulations.

Governance

- Ongoing risk identification and risk management form an integral part of the governance arrangements at these municipalities.
- Fully functional internal audit units are in place, over which audit committees provide effective oversight.
- MPACs have been established and contribute to enhanced oversight.

Further factors making the municipalities successful

- Making good governance and service delivery the norm is a key element of the success of the municipalities who achieved clean audits.
- The municipalities take great pride in their work and responsibilities, as they believe they exist to provide effective services to their citizens.
- The municipal leadership creates platforms and facilities for communities to express their needs and service delivery concerns to the municipality; for example, through regular meetings in community halls and having a 24-hour hotline to report service breakdowns.
- Innovation to enhance the services provided to citizens is central to ensuring that municipal resources are applied economically, effectively and efficiently.
- Entrenched skills in engineering and project management are present at these municipalities.
- The municipalities do not see the achievement of a clean administration as a project, but rather as an outcome of the continuous implementation of governance processes and disciplines, which are key in achieving service delivery. Consequently, these municipalities achieve clean administration without compromising service delivery.
- The municipalities use their clean administration status to attract investors and donors, which then collaborate with the municipalities and provide more funding, enabling the municipalities to deliver more and better services to their communities.
- The municipalities are determined to sustain their clean audit status.
- There is no fear of being audited and the municipalities respond positively to our recommendations.

These key characteristics were evident at all the municipalities visited, as further detailed below.

Field visits in the province

The Eastern Cape had two municipalities that had obtained a clean audit for the 2013-14 financial year, namely Sarah Baartman District and Senqu. The AG visited Sarah Baartman District on 16 April 2015, and was scheduled to visit Senqu after the writing of this report.

Sarah Baartman District



The AG and his team with council members of Sarah Baartman District and Camdeboo.

Sarah Baartman District undertook a joint project with one of its local municipalities, Camdeboo. The AG's visit to Graaff-Reinet, which is the seat of the Camdeboo municipal council, was hosted by both mayors, Cllr Khunjuzwa Kekana (Sarah Baartman District) and Cllr Hanna Makoba (Camdeboo).

Cllr Kekana provided a detailed presentation of the profile of the district as well as the business model they had adopted to ensure that they meet their mandated responsibilities. She said that the district municipality attained a clean audit by enhancing their daily disciplines around financial and performance reporting as well as maintaining stringent oversight processes by MPAC, the council and the audit committee. 'These controls and processes have subsequently resulted in requests being made to the district municipality to share their best practices, and a delegation from five Western Cape

municipalities is scheduled to visit the district municipality in April 2015,' she pointed out.

Project visited

Nieu Bethesda wastewater works

The municipality took the AG to this project due to its impact in terms of service delivery to the community as well as its value.

Before the construction of the Nieu Bethesda wastewater works, the community relied on septic tanks, VIP toilets or the bucket system for their sanitation needs. When the eradication of the bucket system was initiated, Camdeboo and Sarah Baartman District partnered to create a more sustainable sewer management system. They had to move away from a decentralised to a centralised system where household waste is transported away from the households by using a network of sewer pipes to a municipal treatment plant. By developing this system, the municipality could ensure that all households had access to a water-borne sewer system and thus a flushing toilet indoors. A non-mechanised system was also designed to service 500 households in the area.

According to the project manager, Ivor Berrington, this project has limited the carbon footprint, as the system is solar- and lunar-powered with no reliance on Eskom. 'This best practice has been published and the case has been presented in the Netherlands. There are future plans to establish a wood lot, which will be irrigated using the treated effluent water produced by the plant,' said Berrington.

Director of engineering at the municipality, Bheki Makedama, said that the water produced by the plant has met the required quality standards and received approval by the Department of Water Affairs, but has not yet been audited for its green drop status. He further pointed out that the operations controller monitors the water quality daily and weekly, while independent tests are performed each month to ensure that quality standards are met.

Municipal manager, Ted Pillay, explained that the project was planned for and is included in the municipality's SDBIP. Importantly, it was monitored regularly with progress reported quarterly. The reported performance in the annual performance report is reflected as 100% completed, as evidenced by the handover of the completed project to the local municipality. The project is discussed in the municipal manager's overview in chapter 1 on page 5 of the annual report and also on page 80, and relates to the broader key performance area (KPA) 2: service delivery – sanitation services.

Conclusion

The municipalities we visited demonstrate impeccable levels of discipline and oversight in their financial management and operational activities. They have strong financial and performance management systems and governance structures, which enable them to safeguard public money and use it appropriately and transparently to improve the lives of people through service delivery within the framework of applicable laws. These systems and governance structures support the municipalities' ability to develop service delivery plans, allocate funds and utilise them within the framework of the law to deliver public services, and accurately report on their ability to deliver these services.

A key ingredient for obtaining a clean audit and delivering services is the presence of strong governance structures and systems, which would easily detect and timeously correct the breakdown of controls in municipalities. Such environments are characterised by readily available documentation. Most importantly, they have accountable managers and leaders who are able to provide explanations and additional evidence in support of the transactions they are reporting on. They also have the support of strong oversight by mayors and councils that back the efforts of municipal managers and chief financial officers.

Those municipalities that are struggling to improve the quality of their financial and service delivery reporting as well as to prevent non-compliance with legislation have not institutionalised these good practices, which can result in service delivery objectives not being achieved. They should implement the key disciplines entrenched at the municipalities with clean audit outcomes, as detailed earlier on in this section under the key drivers of internal control.

Municipalities are at the forefront of service delivery, as they have a direct impact on the experiences and lives of South Africans. It is therefore important for municipalities to have sound systems and governance structures that will enable them to continue to achieve high levels of efficiencies and find innovative ways to deliver services. The municipalities that achieved clean audits have demonstrated that they are better placed to continuously improve the delivery of services.



Above: A part of the first phase of the wastewater works project in Nieu Bethesda has been completed.

Below: Another part of the project that aims to convert most of the town's household ablutions to the water-borne system.



ANNEXURES

Annexure 1: Auditees' audit outcomes, areas qualified, findings on predetermined objectives, compliance and specific focus areas

Auditee	2013-14 audit outcomes		2012-13 audit outcomes		Financial statement qualification areas							Findings on pre-determined objectives				Findings on compliance													Findings on specific risk areas				Unauthorised, irregular as well as fruitless and wasteful expenditure									
	Audit opinion	Predetermined objectives Compliance with legislation	Audit opinion	Predetermined objectives Compliance with legislation	Non-current assets	Current assets	Liabilities	Capital and reserves	Other disclosure items	Revenue	Expenditure	Unauthorised, irregular, as well as fruitless and wasteful expenditure	Aggregate misstatements	Reported information not useful	Reported information not reliable	Information not submitted in time	No annual performance report	Material misstatement or limitations in submitted AFS	Unauthorised, irregular, as well as fruitless and wasteful expenditure	Annual financial statements and annual report	Asset management	Liability management	Budgets	Expenditure management	Consequence management	Audit committees	Internal audit	Revenue management	Strategic planning and performance management	Transfer and conditional grants	Procurement management	HR management	Other	Quality of submitted performance reports	Supply chain management	Financial health	Human resource management	Information technology	Unauthorised expenditure Amount R	Irregular expenditure Amount R	Fruitless and wasteful expenditure Amount R	
Metros																																										
Buffalo City Metro	R	R	R	R	A						R		R	R			R	R	A	R			R	R			A	R		R	A		R	R	F				186,80	409,30	4,70	
Nelson Mandela Bay Metro		R		R			N				N	R					R	R				R	N	R	N		A		A	R	R		N	R	F				743,90	1052,40	10,60	
District municipalities																																										
Alfred Nzo District	R	R	R	R	A		A	A	R		R	A	A	R	R		R	R	A	N		A	R	N		N	R	A	R	N		R	R	F				106,80	188,90	2,20		
Amathole District		R		R													R	R		N			N				A	N	A			R	F					0,01	0,62	0,44		
Chris Hani District	R	R	R	R			A	R			A	R	R	R			R	R	A	A		R	A	R	N	N		R	R	R	R		R	R	F				14,50	133,70	0,13	
Joe Gqabi District		R		R													R	A				A										A	N					0,00	0,36	0,50		
OR Tambo District	R	R	R	R	R	R	R	R	R	R	R	A	R	R			R	R	A	R	R	A	R	R	R	R	R	R	A	R	A		R	R	M				5,10	178,90	2,30	
Sarah Baartman District		A		R													A														A	N						0,00	12,10	0,00		
Local municipalities																																										
Amahlati	R	R		R	R	N											R	R	A	R	N	N	R	N			A	R	A	R	R		R	R	F				78,60	7,10	3,40	
Baviaans		R		R	A						A	A					R	N			R	R	A	N	R	A	A	A	A	A			R	M				5,40	2,30	2,10		
Blue Crane Route	R	R	R	R	R		A		N		R	R	R	R			R	R	A	R	R	R		R	R	R		R	A	R	R		R	R	F				12,80	28,70	0,02	
Camdeboo		R	R	R	R	A								N		A	R	N	R	A	N	A	R	A	A	A		R	N	R	N		R	R	F				20,10	1,00	0,09	
Elundini		R		A	R												N	R														R	R	F				5,20	0,05	0,09		
Emalahleni	R	R	R	R	A	A	A		R	R	A	R	R	R	N	A	R	R	A	A	A	A	N	N		R	R	A	R	A		R	R	F				12,70	55,40	0,27		
Engcobo		R	R	R	R												R	A	R	R	A	A	A	R	A	A	R	R	A	A	N		R	R	F				0,00	0,00	0,10	
Gariep	R	R	R	R	A		R	A	A	A		A	A	R	R		R	N	R	A	A	A	A	R	A	N	N	N	R		R	R		R	R	F				6,50	3,10	5,50

Legend (Audit outcomes)	Unqualified with no findings	Unqualified with findings	Qualified with findings	Adverse with findings	Disclaimed with findings	Audit not finalised at legislated date	New auditee	Legend (Findings)	Addressed (A)	New (N)	Repeat (R)	Not reported (NR)	Financial health findings	Material unfavourable indicators	Unfavourable indicators	No unfavourable indicators	Legend (Expenditure)	Improved	Regressed
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Auditee	2013-14 audit outcomes		2012-13 audit outcomes		Financial statement qualification areas					Findings on pre-determined objectives				Findings on compliance												Findings on specific risk areas				Unauthorised, irregular as well as fruitless and wasteful expenditure															
	Audit opinion	Pre-determined objectives Compliance with legislation	Audit opinion	Pre-determined objectives Compliance with legislation	Non-current assets	Current assets	Liabilities	Capital and reserves	Other disclosure items	Revenue	Expenditure	Unauthorised, irregular, as well as fruitless and wasteful expenditure	Aggregate misstatements	Reported information not useful	Reported information not reliable	Information not submitted in time	No annual performance report	Material misstatement or limitations in submitted AFS	Unauthorised, irregular, as well as fruitless and wasteful expenditure	Annual financial statements and annual report	Asset management	Liability management	Budgets	Expenditure management	Consequence management	Audit committees	Internal audit	Revenue management	Strategic planning and performance management	Transfer and conditional grants	Procurement management	HR management	Other	Quality of submitted performance reports	Supply chain management	Financial health	Human resource management	Information technology	Unauthorised expenditure Amount R	Irregular expenditure Amount R	Fruitless and wasteful expenditure Amount R				
Local municipalities																																													
Great Kei		R	R		R	R	R	R	A	R	R	R	R	R	R	R		R	R	R	R	R	R	R	N		R	R		R	R		R	R	M					9,90	2,30	0,76			
Ikwezi		R	R		R	R	R	R	N	R	N	R	R	R	R		R	R	R	N	A	A	N	R	A	R	R	R	N	A	A	A		R	R	M					74,00	10,20	0,90		
Ingquza Hill		R	R		R	R								R					N								N					R	N	F						0,64	0,00	0,00			
Inkwanca		R	R		R	R	R	R	N	R	R	R	R	R	R		R	R	R	R	N	R	R	R	R	R	R	R		R	R	M								6,30	1,70	0,46			
Intsika Yethu		R	R		R	A	A	R	A	R	A	R	A	R	R		R	R	A	A	R	R	R	R	R	A	R	R	R	R	R	R	F								47,60	18,20	0,20		
Inxuba Yethemba		R	R		R	R	R	R	R	R	R	R	R	R	R		R	N	N	R	R	R	R	R	R	A	N	R	N	R	R	M									0,00	18,80	0,28		
King Sabata Dalindyebo		R	R		R	A	R	A	A	R	R	A	R	A	R		R	R	A	R	N	R	R	R	R	R	R	R	N	R	R	F								354,40	367,10	7,20			
Kou Kamma		R	R		R	R				R				R	R		R	R	A	N	A	R	A	R	A	R	R	R	R	R	F									16,20	29,80	0,60			
Kouga		R	R		R			A						R	R		R	R	A		A	R	R	R	A		R	N	N	R	R	F									24,00	1,10	2,30		
Lukhanji		R	R		R	R	R	R	R	R	R	R	R	R	N		R	R	N	R	R	R	R	R	R	R	R	R	R	R	R	M									30,00	56,70	0,48		
Makana		R	R		R	R	R	R	N	R	R	R	R	A	R		R	R	R	R	N	R	R	R	R	R	R	R	N	R	M										6,40	115,30	0,89		
Maletswai		R	R		R	A			A			A	A	R	R		A	R		A		R	A	R	R		R	A	R	R	M										17,90	0,28	2,80		
Matatiele		R			A	R											R	R											R		N	R	F									9,70	7,50	0,00	
Mbhashe		R	R		R	R	N		A		N	R		R	R		R	R	R	R			N	A	R	N		R	R	F													2,00	21,00	0,46
Mbizana		R	R		R	R	A	R		R		R	R	A	R	N		R	R	N	R	R		N	R	R	A	A	R	A	R	N	M									0,74	19,60	0,43	
Mhlontlo		R	R		R	R	N	R		R	R	R	R	A	R	R		R	R	A	R	R	N	N	R		N	R	A	R	R	M										19,50	113,60	0,07	
Mnquma		R	R		N	R	R	N	N	R		R	R	A	R	R		R	R	A	A		R	R	N	N	N	R	R	R	R	F										6,70	76,50	0,15	
Ndlambe		R	R		R	N	R	N	N	R	N	A	R		R	R		R	R	A	A	A	A	A	A	R	R	N	R	R	A												62,00	132,80	0,21
Ngqushwa		R	R		R	R	N	R	N	R	R	R	R	A	R	A		R	R	R	N	R	R	N	N	N	R	R	R	R	M											1,40	37,10	0,07	
Nkonkobe		R	R		R	R	N	R		A		R	A	R	R	R		R	R	A	R	R	R	R	R	N	R	N		A	A	F											38,50	3,20	1,50
Ntabankulu		R	R		R	R	N	N	N	R	N	R	R	N	R	N		R	R	R	N	R	R	R	N		R	R	N	R	A												11,20	15,10	4,70
Nxuba		R	R		R	R					A	A	A	R	R		R	R		R		R	N	R		A	A	R	A	A	R	F											17,90	10,70	2,60
Nyandeni		R			A	R											R	A									R			A		N	R										0,00	26,80	0,01
Port St. Johns		R	R		R	R		R	R		N	R	R	R	R		R	R	A	R		A	R	N	A		R	R	R	R	N	F											0,00	61,90	8,90
Sakhisizwe		R	R		R	R				R			R	A	R	N		A	R	R	R	A	R	R	R	A	R	R	R	R	F												30,30	23,70	0,03
Senqu		R	A		A	R																		A						A													0,00	1,20	0,00
Sundays River Valley		R	R		R	R	R				A	A	A	R	N		R	R	N	A		R	A		N		A	R	A	A	M												64,80	113,00	0,50
Tsolwana		R	R		R	R								R	N		A	R	R	N		A		R	A	A		R		A	A	F											3,70	0,11	0,05
Uzimvubu		N	R		A	R								N			R	A			R		A				N	A		N	A	F											0,00	0,58	0,00

Auditee	2013-14 audit outcomes		2012-13 audit outcomes		Financial statement qualification areas				Findings on pre-determined objectives		Findings on compliance														Findings on specific risk areas			Unauthorised, irregular as well as fruitless and wasteful expenditure											
	Audit opinion	Predetermined objectives Compliance with legislation	Audit opinion	Predetermined objectives Compliance with legislation	Non-current assets	Liabilities	Capital and reserves	Other disclosure items	Revenue	Expenditure	Unauthorised, irregular, as well as fruitless and wasteful expenditure	Aggregate misstatements	Reported information not useful	Reported information not reliable	Information not submitted in time	No annual performance report	Material misstatement or limitations in submitted AFS	Unauthorised, irregular, as well as fruitless and wasteful expenditure	Annual financial statements and annual report	Asset management	Liability management	Budgets	Expenditure management	Consequence management	Audit committees	Internal audit	Revenue management	Strategic planning and performance management	Transfer and conditional grants	Procurement management	HR management	Other	Quality of submitted performance reports	Supply chain management	Financial health	Human resource management	Information technology	Unauthorised expenditure Amount R	Irregular expenditure Amount R

Municipality entities

Alfred Nzo Development Agency	R	R	N	R	R	N	N	N	N	N	N	R	N			R	R		N	R	N	N	R	R	N	N			R	A		R	R					0,00	9,10	2,20		
Amathole Economic Development Agency	A	R		N	R							A				R	A																						0,00	0,00	0,00	
Blue Crane Route Development Agency	R	R		R	R		A			N	R	A	R	A		R	A		A	A		R	N	R	N	A	N			R	N		R	R	F				0,00	4,40	0,00	
Buffalo City Development Agency	N	R			R										N	R		R			R	A	N			N				N									0,00	0,17	0,00	
Cacadu Development Agency		N																											N			N							0,00	0,11	0,00	
Chris Hani Development Agency	R	R		N	N		R	N	A		R	A			R	R	R	N		N	A		N	R	A		N		R		R	R							0,00	4,00	0,10	
Joe Gqabi Economic Development Agency	A	R		R	R							A	A			A				A						N				A										0,00	0,00	0,03
Mandela Bay Development Agency				A	R																								N										0,00	0,00	0,00	
Nkonkobe Economic Development Agency		R		A	R											R	A		R		A		N	A		A		R														
Ntinga OR Tambo Development Agency	R	N		R								R	R			N				N						N		N		R	N	F							0,00	0,01	0,08	
Port St. Johns Development Agency	R	R		R	R					A	A	R	N			R			A	N	R	R	N	N		R		R		R	N	M							0,00	0,13	0,64	

Legend (Audit outcomes)	Unqualified with no findings	Unqualified with findings	Qualified with findings	Adverse with findings	Disclaimed with findings	Audit not finalised at legislated date	New auditee	Legend (Findings)	Addressed (A)	New (N)	Repeat (R)	Not reported (NR)	Financial health findings	Material unfavourable indicators	Unfavourable indicators	No unfavourable indicators	Legend (Expenditure)	Improved	Regressed
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Auditee	2013-14 audit outcomes		2012-13 audit outcomes		Financial statement qualification areas					Findings on pre-determined objectives				Findings on compliance											Findings on specific risk areas			Unauthorised, irregular as well as fruitless and wasteful expenditure																		
	Audit opinion	Predetermined objectives Compliance with legislation	Audit opinion	Predetermined objectives Compliance with legislation	Non-current assets	Liabilities	Capital and reserves	Other disclosure items	Revenue	Expenditure	Unauthorised, irregular, as well as fruitless and wasteful expenditure	Aggregate misstatements	Reported information not useful	Reported information not reliable	Information not submitted in time	No annual performance report	Material misstatement or limitations in submitted AFS	Unauthorised, irregular, as well as fruitless and wasteful expenditure	Annual financial statements and annual report	Asset management	Liability management	Budgets	Expenditure management	Consequence management	Audit committees	Internal audit	Revenue management	Strategic planning and performance management	Transfer and conditional grants	Procurement management	HR management	Other	Quality of submitted performance reports	Supply chain management	Financial health	Human resource management	Information technology	Unauthorised expenditure Amount R	Irregular expenditure Amount R	Fruitless and wasteful expenditure Amount R						
Consolidation audits																																														
Metropolitan municipalities																																														
Buffalo City Metro		R		R	R	A						R	A	A		R	R	A	R			R	R			A	R		R	A		A														
Nelson Mandela Bay Metro		R		R		N			N	R					R	R				R	N	R	N			A		A	R	R																
District municipalities																																														
Alfred Nzo District		R		R	R	A	A	A	R	R	A	A	A	A		R	R	A	N	A	R	R	N		N	R	A	R	N		A															
Amathole District		R		R											R	R			N			N						A	N	A																
Chris Hanani District		R		N	N			A	R			A	R	A		R	R	A	A	R	A	R	N	N			R	R	R		A															
Joe Gqabi District		R		R											N	A					A																									
OR Tambo District		R		N	R	R	R	R	R	R	R	R	A	A	A		R	R	A	R	R	A	R	R	R	R	R	R	A	R	A		A													
Sarah Baartman District																																														
Local municipalities																																														
Blue Crane Route		R		R	R	R		A	N			R	R	A	A		R	R	A	R	R	R		R	R	R		R	A	R	R		A													
Nkonkobe		R		R	R	R		R	R		R	A	R	A	A		R	R	A	R	R	R	R	N	R		N		A	A		A														
Port St. Johns		R		R	R	R		R	N		R	R	A	A		R	R	A	R	A	R	N	A		R	R	R	R	N		A															

Legend (Audit outcomes)	Unqualified with no findings	Unqualified with findings	Qualified with findings	Adverse with findings	Disclaimed with findings	Audit not finalised at legislated date	New auditee	Legend (Findings)	Addressed (A)	New (N)	Repeat (R)	Not reported (NR)	Financial health findings	Material unfavourable indicators	Unfavourable indicators	No unfavourable indicators	Legend (Expenditure)	Improved	Regressed
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Annexure 2: Comparison of audit opinions over five years

Auditee	Audit outcome 2013-14			Audit outcome 2012-13			Audit outcome 2011-12			Audit outcome 2010-11			Audit outcome 2009-10		
	Audit opinion	Findings		Audit opinion	Findings		Audit opinion	Findings		Audit opinion	Findings		Audit opinion	Findings	
		Predetermined objectives	Compliance		Predetermined objectives	Compliance		Predetermined objectives	Compliance		Predetermined objectives	Compliance		Predetermined objectives	Compliance
Matatiele	Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with findings		
Mbhashe	Qualified			Qualified			Qualified			Qualified			Disclaimed		
Mbizana	Disclaimed			Adverse			Adverse			Disclaimed			Disclaimed		
Mhlonlto	Adverse			Adverse			Qualified			Qualified			Disclaimed		
Mnquma	Qualified			Qualified			Unqualified with findings			Unqualified with findings			Qualified		
Ndlambe	Disclaimed			Qualified			Qualified			Qualified			Qualified		
Ngqushwa	Disclaimed			Disclaimed			Disclaimed			Disclaimed			Qualified		
Nkonkobe	Qualified			Qualified			Qualified			Qualified			Disclaimed		
Ntabankulu	Disclaimed			Qualified			Qualified			Qualified			Adverse		
Nxuba	Qualified			Qualified			Disclaimed			Disclaimed			Disclaimed		
Nyandeni	Unqualified with findings			Unqualified with findings			Qualified			Disclaimed			Unqualified with findings		
Port St. Johns	Qualified			Qualified			Qualified			Qualified			Unqualified with findings		
Sakhisizwe	Qualified			Qualified			Qualified			Qualified			Adverse		
Senqu	Unqualified with no findings			Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with findings		
Sundays River Valley	Disclaimed			Disclaimed			Qualified			Qualified			Disclaimed		
Tsolwana	Unqualified with findings			Unqualified with findings			Qualified			Unqualified with findings			Qualified		
Umzimvubu	Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with findings			Qualified		
Municipal entities															
Alfred Nzo Development Agency	Qualified			Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with findings		
Amathole Economic Development Agency	Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with no findings		
Blue Crane Route Development Agency	Qualified			Qualified			Qualified			Unqualified with findings			Qualified		
Buffalo City Development Agency	Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with findings		
Cacadu Development Agency	Unqualified with findings			New auditee			New auditee			New auditee			New auditee		
Chris Hani Development Agency	Qualified			Qualified			New auditee			New auditee			New auditee		
Joe Gqabi Economic Development Agency	Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with no findings			New auditee		
Mandela Bay Development Agency	Unqualified with no findings			Unqualified with no findings			Unqualified with findings			Unqualified with findings			Unqualified with findings		
Nkonkobe Economic Development Agency	Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with findings			New auditee		
Ntinga OR Tambo Development Agency	Unqualified with findings			Unqualified with findings			Unqualified with findings			Qualified			Qualified		
Port St. Johns Development Agency	Unqualified with findings			Qualified			Disclaimed			Disclaimed			New auditee		

Auditee	Audit outcome 2013-14			Audit outcome 2012-13			Audit outcome 2011-12			Audit outcome 2010-11			Audit outcome 2009-10			
	Audit opinion	Findings		Audit opinion	Findings		Audit opinion	Findings		Audit opinion	Findings		Audit opinion	Findings		
		Predetermined objectives	Compliance		Predetermined objectives	Compliance		Predetermined objectives	Compliance		Predetermined objectives	Compliance		Predetermined objectives	Compliance	
Consolidation audits																
Metropolitan municipalities																
Buffalo City Metro	Qualified			Qualified			Qualified			Adverse			Disclaimed			
Nelson Mandela Bay Metro	Qualified			Qualified			Qualified			Unqualified with findings			Unqualified with findings			
District municipalities																
Alfred Nzo District	Qualified			Disclaimed			Disclaimed			Disclaimed			Disclaimed			
Amathole District	Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with findings			Qualified			
Chris Hani District	Qualified			Qualified			New auditee			New auditee			New auditee			
Joe Gqabi District	Unqualified with findings			Unqualified with findings			Unqualified with findings			Unqualified with findings			New auditee			
OR Tambo District	Disclaimed			Disclaimed			Disclaimed			Adverse			Qualified			
Sarah Baartman District	Unqualified with no findings			New auditee			Unqualified with findings			Unqualified with findings			Unqualified with findings			
Local municipalities																
Blue Crane Route	Qualified			Qualified			Qualified			Unqualified with findings			Qualified			
Nkonkobe	Qualified			Qualified			Qualified			Qualified			New auditee			
Port St. Johns	Qualified			Qualified			Qualified			Qualified			New auditee			

GLOSSARY OF TERMS, ACRONYMS AND ABBREVIATIONS

Glossary of key terminology used in this report

Adverse audit opinion (on financial statements)

The financial statements contain misstatements (see 'misstatement') that are not confined to specific amounts, or the misstatements represent a substantial portion of the financial statements.

Asset (in financial statements)

Any item belonging to the auditee, including property, infrastructure, equipment, cash, and debt due to the auditee.

Assurance / assurance provider

As used in this report, assurance is a positive declaration that is intended to give confidence in the credibility of financial and performance reports tabled by auditees and in the extent to which auditees have adhered to applicable legislation.

Through the audit report issued to the auditees, we provide assurance on the credibility of auditees' financial and performance information as well as their compliance with key legislation.

There are role players in local government (assurance providers), other than the external auditors, that are also required to contribute to assurance and confidence by ensuring that adequate internal controls are implemented to achieve auditees' financial, service delivery and compliance objectives. Such assurance providers include senior auditee officials, various committees (for example, municipal public accounts, performance and audit committees) and internal audit units.

Other role players that should provide assurance further include oversight structures and coordinating or monitoring departments (see 'oversight structures as well as coordinating and monitoring departments').

Backups

In information technology, a backup, or the process of backing up, refers to the copying and archiving of computer data so that it may be used to restore the original after a data loss event. The primary purpose of a backup is to recover data after its loss, be it by data deletion or corruption.

Business continuity plan (BCP)

A business continuity plan is a plan to continue operations if a place of business is affected by different levels of disaster, which can be localised short-term disasters, to days-long building-wide problems, to a permanent loss of a building. Such a plan typically explains how the business would recover its operations or move operations to another location after damage by events like natural disasters, theft or flooding. For example, if a fire destroys an office building or data centre, the people and business or data centre operations would relocate to a recovery site.

<i>Capital budget</i>	The estimated amount planned to be spent by auditees on capital items in a particular financial period; for example, fixed assets such as property, infrastructure and equipment with long expected lives and that are required to provide services, produce income or support operations.
<i>Cash flow (in financial statements)</i>	The flow of money from operations: incoming funds are revenue (cash inflow) and outgoing funds are expenses (cash outflow).
<i>Clean audit</i>	The financial statements receive a financially unqualified audit opinion and there are no material findings on the quality of the annual performance report or compliance with key legislation.
<i>Commitments from role players</i>	Initiatives and courses of action communicated to us by role players in local government aimed at improving the audit outcomes.
<i>Conditional grants</i>	Money transferred from national government to auditees, subject to certain services being delivered or on compliance with specified requirements.
<i>Consolidated financial statements</i>	Financial statements that reflect the combined financial position and results of a municipality and those of the municipal entities under its control.
<i>Contingent liability</i>	A potential liability, the amount of which will depend on the outcome of a future event.
<i>Creditors</i>	Persons, companies or organisations that the auditee owes money to for goods and services procured from them.
<i>Current assets (in financial statements)</i>	These assets are made up of cash and other assets, such as inventory or debt for credit extended, which will be traded, used or converted into cash in less than 12 months. All other assets are classified as non-current, and typically include property, plant and equipment as well as long-term investments.
<i>Disaster recovery plan (DRP)</i>	A disaster recovery plan is a documented process or set of procedures to recover and protect an auditee's information technology infrastructure in the event of a disaster. Usually documented in written form, the plan specifies the procedures that an auditee should follow in the event of a disaster. It is a comprehensive statement of consistent actions to be taken before, during and after a disaster. The disaster could be natural, environmental or artificial. Artificial disasters could be intentional, such as the act of an attacker; or unintentional (in other words, accidental), such as the wall of a dam breaking).

Disclaimed opinion (on financial statements)

The auditee provided insufficient evidence in the form of documentation on which we could base an audit opinion. The lack of sufficient evidence is not confined to specific amounts, or represents a substantial portion of the information contained in the financial statements.

Financial and performance management (as one of the drivers of internal control)

The performance of internal control and monitoring-related tasks by management and other employees to achieve the financial management, reporting and service delivery objectives of the auditee.

These controls include basic daily and monthly controls for processing and reconciling transactions, preparing regular and credible financial and performance reports as well as reviewing and monitoring compliance with key legislation.

Financially unqualified audit opinion (on financial statements)

The financial statements contain no material misstatements (see 'material misstatement'). Unless we express a clean audit opinion, findings have been raised on either the annual performance report or compliance with key legislation, or both these aspects.

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Firewall

A security system used to prevent unauthorised access between networks (both internal/internal and internal/external). A firewall will allow only approved traffic in and/or out by filtering packets based on the source or destination. The firewall inspects the identification information associated with all communication attempts and compares it to a rule set consistent with the auditee's security policy. Its decision to accept or deny the communication is then recorded in an electronic log.

Fruitless and wasteful expenditure

Expenditure that was made in vain and could have been avoided had reasonable care been taken. This includes penalties and interest on the late payment of creditors or statutory obligations as well as payments for services not utilised or goods not received.

Going concern

The presumption that an auditee will continue to operate in the near future, and will not go out of business and liquidate its assets. For the going concern presumption to be reasonable, the auditee must have the capacity and prospect to raise enough financial resources to stay operational.

Governance (as one of the drivers of internal control)

The governance structures (audit committees) and processes (internal audit and risk management) of an auditee.

Human resource (HR) management

The management of an auditee's employees, or human resources, which involves adequate and sufficiently skilled people as well as the adequate management of their performance and productivity.

<i>Information technology (IT)</i>	The computer systems used for recording, processing and reporting financial and non-financial transactions.
<i>IT controls</i>	Computer-related controls ensure the confidentiality, integrity and availability of state information; enable service delivery; and promote national security.
<i>IT governance</i>	The leadership, organisational structures and processes which ensure that the auditee's information technology resources will sustain its business strategies and objectives.
<i>IT security management</i>	The controls preventing unauthorised access to the computer networks, computer operating systems and application systems that generate and prepare financial information.
<i>IT service continuity</i>	The processes of managing the availability of computer hardware, system software, application software (computer programmes) and data to enable auditees to recover or establish information system services in the event of a disaster.
<i>IT user access management</i>	The procedures through which auditees ensure that only valid and authorised users are allowed segregated access to initiate and approve transactions on the information systems.
<i>Internal control / key controls</i>	<p>The process designed and implemented by those charged with governance, management and other personnel to provide reasonable assurance about the achievement of the auditee's objectives with regard to the reliability of financial reporting, the effectiveness and efficiency of operations, and compliance with key legislation.</p> <p>It consists of all the policies and procedures implemented by auditee management to assist in achieving the orderly and efficient conduct of business, including adhering to policies, safeguarding assets, preventing and detecting fraud and error, ensuring the accuracy and completeness of accounting records, and timeously preparing reliable financial and service delivery information.</p>
<i>Irregular expenditure</i>	Expenditure incurred without complying with applicable legislation.
<i>Key drivers of internal control</i>	The three components of internal control that should be addressed to improve audit outcomes, namely leadership, financial and performance management, and governance (which are defined elsewhere in this glossary.)

Leadership (as one of the drivers of internal control)

The administrative leaders of an auditee, such as municipal managers and senior management.

It can also refer to the political leadership (including the mayor and the council) or the leadership in the province (such as the premier).

Material finding (from the audit)

An audit finding on the quality of the annual performance report or compliance with key legislation that is significant enough in terms of either its amount or its nature, or both these aspects, to be reported in the audit report.

Material misstatement

(in financial statements or annual performance reports)

An error or omission that is significant enough to influence the opinions or decisions of users of the reported information. Materiality is considered in terms of either its rand value or the nature and cause of the misstatement, or both these aspects.

Misstatement (in financial statements or annual performance reports)

Incorrect or omitted information in the financial statements or annual performance report.

Net current liability

The amount by which the sum of all money owed by an auditee and due within one year exceeds the amounts due to the auditee within the same year.

Net deficit (incurred by auditee)

The amount by which an auditee's spending exceeds its income during a period or financial year.

Operational budget / operating budget

A short-term budget, usually prepared annually, based on estimates of income and expenses associated with the auditee's operations, such as service delivery costs, administration and salaries.

Oversight structures as well as coordinating and monitoring departments

Oversight structures consist of the provincial legislatures, the portfolio committees on local government and the National Council of Provinces.

Coordinating or monitoring departments include the Department of Performance Monitoring and Evaluation, the National Treasury and provincial treasuries, the national and provincial departments of cooperative governance as well as the offices of the premier.

Password

In access control, confidential authentication information, usually composed of a string of characters, may be used to control access to physical areas and data. Passwords have to comply with certain complexity rules to ensure that they are not easy to guess.

<i>Property, infrastructure and equipment (in financial statements)</i>	Assets that physically exist and are expected to be used for more than one year, including land, buildings, leasehold improvements, equipment, furniture, fixtures and vehicles.
<i>Qualified audit opinion (on financial statements)</i>	The financial statements contain material misstatements in specific amounts, or there is insufficient evidence for us to conclude that specific amounts included in the financial statements are not materially misstated.
<i>Receivables / debtors (in financial statements)</i>	Money owed to the auditee by persons, companies or organisations that have procured goods or services from the auditee.
<i>Reconciliation (of accounting records)</i>	The process of matching one set of data to another; for example, the bank statement to the cheque register, or the accounts payable journal to the general ledger.
<i>Root causes (of audit outcomes being poor or not improving)</i>	The underlying causes or drivers of audit findings; in other words, why the problem occurred. Addressing the root cause helps to ensure that the actions address the real issue, thus preventing or reducing the incidents of recurrence, rather than simply providing a one-time or short-term solution.
<i>Supply chain management (SCM)</i>	Procuring goods and services through a tender or quotation process and monitoring the quality and timeliness of the goods and services provided.
<i>Unauthorised expenditure</i>	Expenditure that was in excess of the amount budgeted or allocated by government to the auditee, or that was not incurred in accordance with the purpose for which it was intended.
<i>Vulnerability</i>	In information security, a weakness or flaw (in location, physical layout, organisation, management, procedures, personnel, hardware or software) that may be exploited by an attacker to cause an unfavourable impact.

Acronyms and abbreviations

AG	<i>auditor-general (the person)</i>
AGSA	<i>Auditor-General of South Africa (the institution)</i>
APP	<i>annual performance plan</i>
BCP	<i>business continuity plan</i>
CoGTA	<i>Department of Cooperative Governance and Traditional Affairs</i>
DM	<i>district municipality</i>
DRP	<i>disaster recovery plan</i>
EC	<i>Eastern Cape</i>
FMG	<i>financial management grant</i>
HR	<i>human resources</i>
ICT	<i>information and communications technology</i>
IDP	<i>integrated development plan</i>
IT	<i>information technology</i>
KPA	<i>key performance area</i>
LED	<i>local economic development</i>
LM	<i>local municipality</i>
ME	<i>municipal entity</i>
MEC	<i>member of the executive council</i>
MFMA	<i>Municipal Finance Management Act, 2003 (Act No. 56 of 2003)</i>
MIG	<i>municipal infrastructure grant</i>
MPAC	<i>municipal public accounts committee</i>
MSA	<i>Municipal Systems Act, 2000 (Act No. 32 of 2000)</i>
MSIG	<i>municipal systems improvement grant</i>
MTSF	<i>medium term strategic framework</i>
NCOP	<i>National Council of Provinces</i>
NMBDA	<i>Nelson Mandela Bay Development Agency</i>
SALGA	<i>South African Local Government Association</i>
SCM	<i>supply chain management</i>
SDBIP	<i>service delivery and budget implementation plan</i>



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