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SOUTH AFRICA

Auditor-General of South Africa

## Okhahlamba Local Municipality – Final Management Report 2018-19





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# FINAL MANAGEMENT REPORT

## OKHAHLAMBA LOCAL MUNICIPALITY

**30 June 2019**

**Communicated to the accounting officer on: 11 December 2019**



# MANAGEMENT REPORT

## OKHAHLAMBA LOCAL MUNICIPALITY

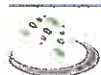
30 June 2019

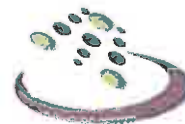
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## MANAGEMENT REPORT TO THE ACCOUNTING OFFICER ON THE AUDIT OF THE OKHAHLAMBA LOCAL MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2019

### INTRODUCTION

1. The purpose of the management report is to communicate audit findings and other key audit observations to the accounting officer and does not constitute public information. This management report includes audit findings arising from the audit of the financial statements, performance information and compliance with legislation for the year ended 30 June 2019.
2. These findings were communicated to management and the report details management's response to these findings. The report includes information on the internal control deficiencies that we identified as the root causes of the matters reported. Addressing these deficiencies will help to improve the audit outcome.
3. In accordance with the terms of engagement, our responsibility in this regard is to:
  - express an opinion on the financial statements
  - express an opinion in the management report on the usefulness and reliability of the reported performance information for selected development objective, and report the material findings in the auditor's report
  - report on material findings raised on compliance with specific requirements in key applicable legislation, as set out in the general notice issued in terms of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA).









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

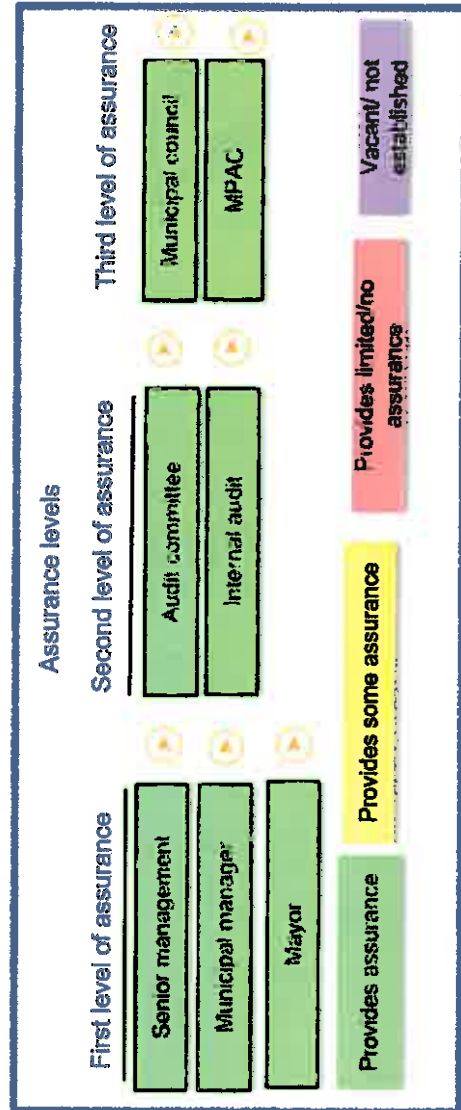
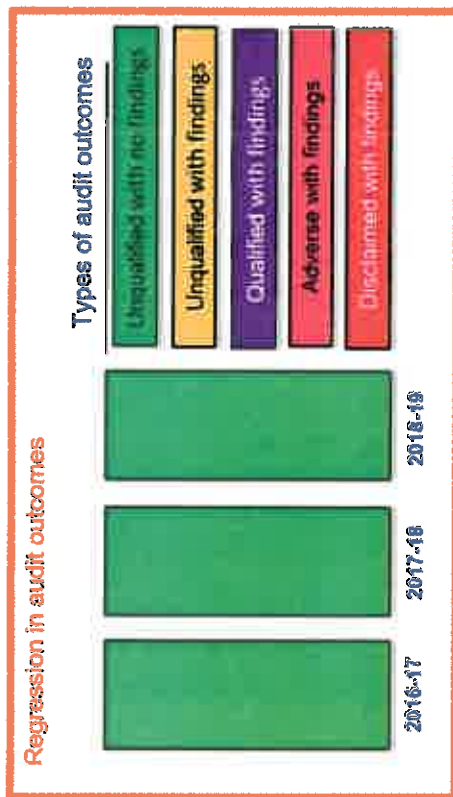
4. This management report consists of the overall message arising from the audit, summary of key findings and observations, annexures containing the detailed audit findings, annexures to the report on the audit of performance information as well as the annexure to internal control deficiencies reported.
5. The auditor's report is finalised only after the management report has been communicated. All matters included in this report that relate to the auditor's report remain in draft form until the final auditor's report is signed. In adherence to section 50 of the PAA, we do not disclose any information obtained during the audit and contained in this management report.
6. Please note that the information contained in these documents is confidential, privileged and only for the information of the intended recipient(s) and may not be used, published or redistributed without the prior written consent of the Auditor-General of South Africa (AGSA). Any form of reproduction, dissemination, copying, disclosure, modification, distribution and or publication of this material is strictly prohibited. Should the information be used or processed in a manner that contravenes any laws in the Republic, the AGSA is fully indemnified from liability that may arise from such contravention.
7. The figure that follows provides a pictorial summary of the audit results and our key messages on how to improve the audit outcomes with the focus on the following:
  - Status of the audit outcomes
  - Status of the level of assurance provided by key role players



- Status of the drivers of internal controls
- Status of risk areas
- Root causes to be addressed

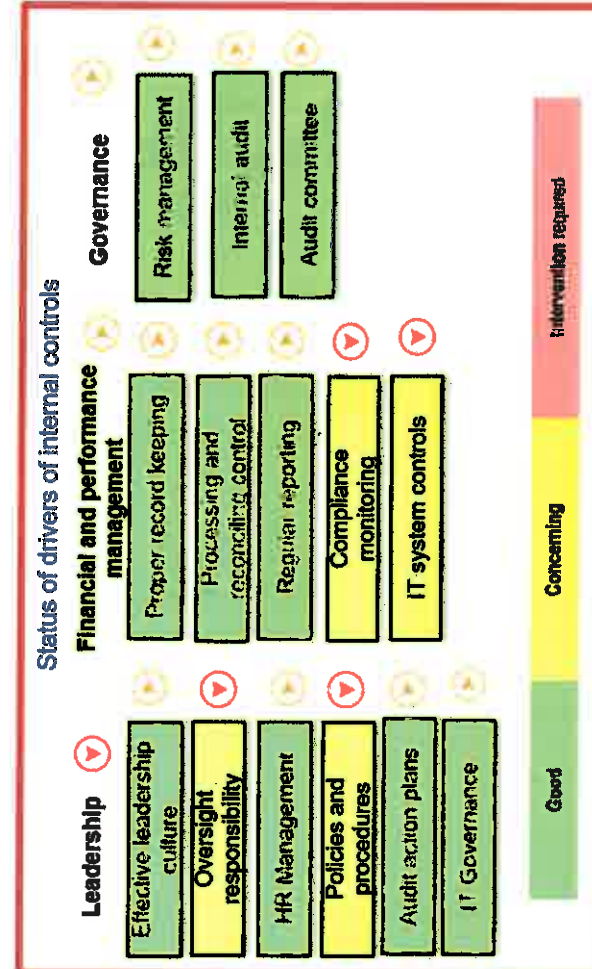
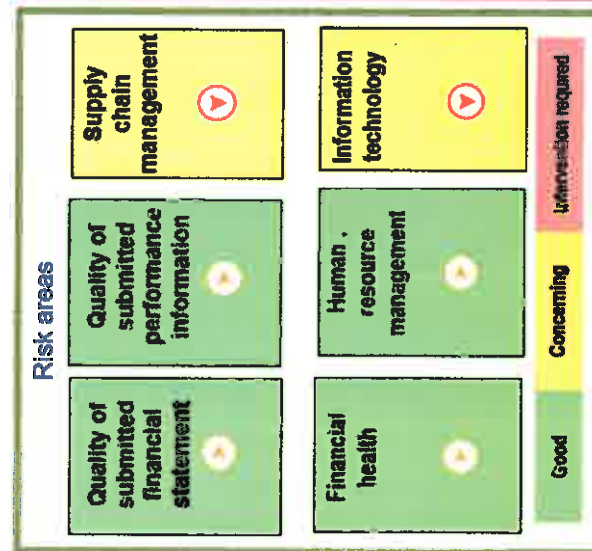
Movement from the previous year is depicted as follows:

-  /  Improved
-    /  Unchanged / slight improvement / slight regression
-  /  Regressed



**Best practices to should be maintained**

- Continuous monitoring of compliance with policies and regulations
- Ensuring adequate and resourced internal audit
- Strong control environment that promotes clean administration with top level of management leading by example





## OVERALL MESSAGE

8. The municipality is to be commended on maintaining a clean audit, the quality of the submitted annual financial statements and the annual performance report. However, deficiencies were identified in the internal controls environment which management need to address to ensure that the clean administration is maintained going forward.
9. Our staff remains committed to assisting in identifying and communicating good practices to improve governance and accountability and to build public confidence in government's ability to account for public resources in a transparent manner.

## SECTION 1: Interactions with stakeholders responsible for oversight and governance

10. During the audit cycle, we met with the following key stakeholders responsible for oversight and governance to communicate matters relating to the audit outcome and matters identified during our status of records review(s) of the municipality:

Key stakeholder	Purpose of interaction	Number of interactions
Municipal council	Tabling the audit report	1
Municipal public accounts committee	Observation of MPAC processes	1
Mayor	Engagement meeting and Fraud risk discussion	2
Municipal manager	Various	2
Audit committee	Various	4

11. At these interactions, we highlighted the following key matters affecting audit outcomes and the auditee:
  - Maintenance of a strong control environment from top management
  - Continuous monitoring and review of compliance with legislation
  - Ensuring an adequately resourced internal audit unit to be able to expand their scope and continuously monitor the implementation of internal controls.
12. All stakeholders made commitments to implement initiatives that can maintain the audit outcome. The commitments given and the progress of previous commitments are included in section 3, which deals with the assessment of assurance providers.

## SECTION 2: Matters relating to the auditor's report

### AUDIT OF THE FINANCIAL STATEMENTS

13. We commend the municipality for submitting financial statements that were free from material misstatements.

### MATTERS TO BE BROUGHT TO THE ATTENTION OF USERS

#### Emphasis of matter paragraphs

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

#### Material provision for impairments – consumer debtors

15. As disclosed in note 9 of the financial statements, the municipality recognised a provision for bad debts of R32,39 million (2018: R24,43 million) on consumer debtors as the recoverability of these amounts were doubtful.

#### Restatement of corresponding figures

16. As disclosed in note 34 to the financial statements, the corresponding figures for 30 June 2018 were restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2019.

#### Irregular expenditure

17. As disclosed in note 39 to the financial statements, the municipality incurred irregular expenditure of R31,41 million, as proper tender processes were not followed.

#### Other matter paragraphs

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

#### Unaudited disclosure notes

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

#### Unaudited supplementary schedules

20. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion on them.

## AUDIT OF THE ANNUAL PERFORMANCE REPORT

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

### Introduction and scope

22. We have undertaken a reasonable assurance engagement on the reported performance information for the following selected objective presented in the annual performance report of the municipality for the year ended 30 June 2019:

Objective	Pages in annual performance report	Opinion	Movement
Objective 2 : Advanced access to basic services	x – x	Unqualified	

23. We conducted our reasonable assurance engagement in accordance with the International Standard on Assurance Engagements, ISAE 3000: *Assurance engagements other than audits or reviews of historical financial information*.
24. We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Advanced access to basic services

#### Opinion

25. In our opinion, the reported performance information for Objective 2: Advanced access to basic services is useful and reliable, in accordance with the applicable criteria as developed from the performance management and reporting framework as set out in annexure D to this report.

#### Other matter

26. We draw attention to the matter below. Our opinion is not modified in respect of this matter.

#### Achievement of planned targets

27. Refer to the annual performance report on pages x to x for information on the achievement of planned targets for the year.

### Responsibilities of the accounting officer for the reported performance information

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

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

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

## AUDIT OF COMPLIANCE WITH LEGISLATION

32. We did not identify any instances of material non-compliance with selected specific requirements of applicable legislation, as set out in the general notice issued in terms of the PAA.

## OTHER INFORMATION

33. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes the audit committee's report. The other information does not include the financial statements, the auditor's report and those selected objectives presented in the annual performance report that have been specifically reported in the auditor's report.
34. Our opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and we do not express an audit opinion or any form of assurance conclusion thereon.
35. In connection with our audit, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected objectives presented in the annual performance report, or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement in this other information, we are required to report that fact. We have nothing to report in this regard.

## INTERNAL CONTROLS

36. The significant deficiencies in internal control which led to our overall assessment of the status of the drivers of key controls, as included in the figure in paragraph 7, is described below. The detailed assessment of the implementation of the drivers of internal control in the areas of financial statements, performance reporting and compliance with legislation is included in annexure F.

### Leadership

#### Oversight responsibility

37. The Accounting Officer and management did not effectively monitor compliance with SCM laws and regulations resulting in irregular expenditure being identified during the audit.
38. The Chief Financial Officer (CFO) did not properly review the schedules supporting the annual financial statement and the underlying records to ensure financial statements are supported by reliable evidence. Material misstatements were identified in irregular expenditure.

#### Policies and procedures

39. The approved asset management policy was not properly implemented by management to ensure that valuation of assets is in line with GRAP requirements.

### Financial and performance management

#### Compliance monitoring

40. Non-compliance with legislation, supply chain management regulations and MFMA could have been prevented had the municipality correctly applied section 116(3) of the MFMA.

#### Information technology systems

41. Findings were identified relating to the VIP payroll and SAGE Evolution systems. These findings ranged across the IT general controls focus areas of IT Governance, User access management and IT service continuity.

### Summary

42. We considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. We did not identify any significant deficiencies in internal control

## OTHER REPORTS

43. We draw attention to the following engagements conducted by various parties that have or could potentially have an impact on the municipality's financial statements, reported performance information and compliance with applicable legislation and other related matters. The reports noted do not form part of the opinion on the financial statements or findings on the reported performance information or compliance with legislation.

44. The municipality's internal audit performed an investigation into allegations of misappropriation of monies receipted and not banked covering the period 2018-19. The matter has been referred to the South African Police Services for further investigation.
45. The municipality's internal audit performed an investigation into allegations of ghost employees covering the period 2014-15. The matter has been referred to the South African Police Services for further investigation.

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

#### **ASSESSMENT OF ASSURANCE PROVIDERS**

46. The annual report is used to report on the financial position of auditees, their performance against predetermined objectives and overall governance. One of the important oversight functions of the municipal council is to consider auditees' annual reports. To perform this oversight function, they need assurance that the information in the annual report is credible. To this end, the annual report includes our auditor's report, which provides assurance on the credibility of the financial statements and the annual performance report, as well as on the auditee's compliance with legislation.
47. Our reporting and oversight processes reflect on past events, as they take place after the end of the financial year. However, management, the leadership and those charged with governance contribute throughout the year to the credibility of financial and performance information and compliance with legislation by ensuring that adequate internal controls are implemented.
48. We assess the level of assurance provided by these assurance providers based on the status of internal controls (as reported in section 2.6) and the impact of the different role players on these controls. We provide our assessment for this audit cycle below.

#### First level of assurance

##### **Senior management: provides assurance**

- Senior management is pro-active in responding to issues identified by both internal and external audit with action plans being developed to address deficiencies. Action plans implemented are actively monitored to ensure that actions are effectively addressing the deficiencies and to prevent any repeat findings

##### **Accounting officer: provides assurance**

- The municipal manager sets a tone from the top and drives clean administration on a daily basis. Action plans implemented to address audit findings are sound and regularly monitored to ensure that all deficiencies are adequately addressed.





### Mayor: provides assurance

- The Mayor participated in quarterly meetings and assisted the municipal manager in driving high performance within the municipality.

### Second level of assurance

#### Internal audit unit: provides assurance

- Legislation in South Africa requires the establishment, roles, and responsibilities of internal audit units. Internal audit units form part of the internal control and governance structures of the municipality and play an important role in its monitoring activities. Internal audit provides an independent assessment of the municipality's governance, risk management and internal control processes.
- The internal audit unit of a municipality must prepare a risk-based audit plan and internal audit programme for each financial year. It must advise the accounting officer and report to the audit committee on implementation of the internal audit plan and matters relating to internal audit; internal controls; accounting procedures and practices; risk and risk management; performance management; loss control and compliance with the MFMA. The internal audit unit must also perform such other duties as may be assigned by the accounting officer.
- Internal audit follows a risk based internal audit plan and produces quality audit reports which provides management with value-add findings and recommendations to improve the control environment within the municipality.

#### Audit committee: provides assurance

- The audit committee is an independent advisory body to the council, accounting officer and the management and staff of the municipality on matters relating to internal financial control and internal audits; risk management; accounting policies; the adequacy, reliability and accuracy of financial reporting and information; performance management; effective governance; the MFMA and any other applicable legislation; performance evaluation and any other issues.
- The audit committee is also expected to review the annual financial statements to provide an authoritative and credible view of the municipality, its efficiency and effectiveness and its overall level of compliance with the applicable legislation.
- The audit committee provided excellent oversight over the internal audit function and consistently drives the good control environment at the municipality.

### Third level of assurance

#### Municipal council: provides assurance

- The Council provided oversight on the implementation of the municipal policies.

#### Municipal public account committee (MPAC): provides assurance

- The extent to which the Council has been adopted MPAC guidelines had been considered in the assessment of MPAC as an assurance provider.

## STATUS OF IMPLEMENTING COMMITMENTS AND RECOMMENDATIONS

No specific commitments were recorded, as we had reported no significant deficiencies in internal control.

### SECTION 4: Specific focus areas

#### FINANCIAL VIABILITY

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

FINANCIAL VIABILITY ASSESSMENT			
		AS AT 30 JUNE 2019	AS AT 30 JUNE 2018
EXPENDITURE MANAGEMENT			
1.1	Creditor-payment period	49 Days	33 Days
REVENUE MANAGEMENT			
2.1	Debtor-collection period (after impairment)	189 Days	180 Days
2.2	Debtors impairment provision as a percentage of accounts receivable	61%	56%
	• Amount of debtor's impairment provision	R32 392 650	R24 427 693
	• Amount of accounts receivable	R53 492 590	R43 557 597
ASSET AND LIABILITY MANAGEMENT			
3.1	A deficit for the year was realised (total expenditure exceeded total revenue)	No	No
	• Amount of the surplus / (deficit) for the year	R22 827 961	R54 875 879
3.2	A net current liability position was realised (total current liabilities exceeded total current assets)	No	No
	• Amount of the net current assets / (liability) position	R6 819 038	R14 489 392
3.3	A net liability position was realised (total liabilities exceeded total assets)	No	No
	• Amount of the net asset / (liability) position	R373 201 022	R349 425 603
CASH MANAGEMENT			
4.1	The year-end bank balance was in overdraft	No	No





FINANCIAL VIABILITY ASSESSMENT			
		AS AT 30 JUNE 2019	AS AT 30 JUNE 2018
	• Amount of year-end bank balance (cash and cash equivalents) / (bank overdraft)	R26 657 949	R29 591 731
4.2	Net cash flows for the year from operating activities were negative	No	No
	• Amount of net cash in / (out)flows for the year from operating activities	R54 048 243	R62 102 000
4.3	Creditors as a percentage of cash and cash equivalents	33%	21%
	• Amount of creditors (accounts payable)	R8 758 998	R6 320 718
	• Amount of cash and cash equivalents / (bank overdraft) at year-end	R54 048 243	R62 102 000
4.4	Current liabilities as a percentage of next year's budgeted resources	46%	14%
	• Amount of current liabilities	R50 187 604	R42 152 389
	• Amount of next year's budgeted income	R109 836 000	R300 567 000
OVERALL ASSESSMENT			
Overall the financial viability is assessed as:		Yellow (Concerning)	Yellow (Concerning)

### High-level comments

50. The impairment provision for consumer debtors is high. This highlights the ineffectiveness of credit control and collection policies.
51. The amount of revenue billed in the current financial year has increased making the municipality more sustainable on their operational revenue. The amount of cash and cash equivalent relative to current liabilities is sound.
52. The municipality's creditors payment period is concerning as it is above 30-day requirement.
53. The surplus for the year has reduced by 56,7% when compared to the prior year. This was mainly due to the municipality not receiving a Massification Grant and a Department of Rural Development Grant which were not received in the current year.

### PROCUREMENT AND CONTRACT MANAGEMENT

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

### Irregular expenditure

55. R31,41 million (100%) of the irregular expenditure incurred in the current financial year was as a result of the contravention of SCM legislation. The root cause for the lack of effective prevention and detection is inadequate review by management of compliance with SCM processes

### Awards to persons in the service of the state

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

57. The findings were as follows:

Finding	Number and value of awards made	Number and positions of official/councillor identified	Number of suppliers identified	Further non-compliance or irregularities regarding the awards			
				Supplier did not submit declarations of interest	Supplier did not declare interest (false declaration)	Official/councillor did not declare interest	Official/councillor or was involved in awarding the contract/ quotation
Awards to persons in the service of other state institutions	7 R5 904 503	7	7	0	7		

### Procurement processes

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

	Total		Quotations		Contracts	
	Number	Value R	Number	Value R	Number	Value R
<b>Awards selected for testing</b>	36	R135 516 892	19	R856 092	17	R134 660 800
<b>Expenditure incurred on selected awards – current year</b>		R102 872 493		R856 092		R102 016 401
<b>Limitations – awards selected</b>	0	0	0	0	0	0

	Total		Quotations		Contracts	
	Number	Value R	Number	Value R	Number	Value R
but could not be tested						
Awards on which non-compliance was identified	6	R31 313 951	2	R300 000	4	R31 013 951
Irregular expenditure identified	6	R31 313 951	2	R300 000	4	R31 013 951
Instances of irregular expenditure where goods/ services were not received	0	0	0	0	0	0

### Procurement processes – general

- One contract with a value of R41,47 million was procured without inviting competitive bids, and the deviation was not approved.
- Some competitive bids with a value of R10,48 million were adjudicated by adjudication committees that were not properly constituted.
- Some quotations with a value of R300 000 were procured without inviting competitive bids, and the deviations were not approved.

### Internal control deficiencies

59. Awards are approved without due regard of the SCM policy and regulations.

## FRAUD AND CONSEQUENCE MANAGEMENT

60. The primary responsibility for preventing and detecting fraud rests with management and those charged with governance. We are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error, and to issue an auditor's report that includes our opinion. Due to the inherent limitations of an audit, there is a risk that some material misstatements, including fraud, may not be detected.
61. The MFMA and its regulations clearly stipulate that matters such as incurring unauthorised, irregular and fruitless and wasteful expenditure; the possible abuse of the SCM system (including fraud and improper conduct); and allegations of financial misconduct should be investigated. Disciplinary steps should be taken based on the results of the investigations. Our audits included an assessment of the municipality's management of consequences.
62. Below is a summary of risk factors identified during the audit that should be addressed to ensure that sufficient controls are in place to prevent material misstatements/ non- compliance due to fraud.
- Not all revenue billed may be recovered.

- Circumvention of SCM processes and awards to certain suppliers.

### Ongoing investigations

63. A total of two (2) investigations was ongoing at year-end on allegations relating to financial misconduct and fraud. Allegations for payment of ghost employees have been going on since 2014/15 financial year. The Municipal Regulations on Financial Misconduct, Procedures and Criminal Proceedings and the Disciplinary Regulations for Senior Managers require that each investigation must be completed within 30 days from the date of appointing the investigator. The table below provides a summary of investigations which had not been completed as at year-end:

Total number of ongoing investigations as at year-end	2
• Number of SCM-related investigations	0
• Number of fraud-related investigations	2
Number of investigations exceeding a period of 3 months	1

### Transgressions reported to management for investigation

64. During the previous year's audit, we reported findings relating to transgressions by officials or other role players, for management to investigate. During the current year audit, we performed follow-up tests to determine whether the matters reported were dealt with by management.
65. The table below provides a summary of the transgressions reported in the previous year and the year under review that must be investigated and disciplinary steps taken based on the results of the investigations.

Finding	Findings raised in the previous year			Findings reported in current year	
	Number of instances	Number of instances investigated	Number of instances resolved from these investigated	Number of instances	Value (R)
<b>A: Improper conduct in SCM by suppliers</b>					
Supplier submitted false declaration of interest	1	1	1	1	R10 370
<b>D: Other fraud/corruption allegations (not included above)</b>					
Monies receipted and not banked	1	1	0	1	R108 899

66. Fruitless and wasteful, irregular and unauthorised expenditure disclosed in note 37, 38 and 39 to the financial statements must be investigated to determine whether any official is liable for losses incurred as a result of this expenditure. Disciplinary steps must be taken against officials

who caused or permitted the fruitless and wasteful expenditure, irregular, unauthorised and losses incurred must be recovered from the person liable.

67. In terms of section 225 of the IESBA code, we have a responsibility to consider reporting identified and suspected non-compliance with laws and regulations to an appropriate authority. No matters were escalated to council

## USE OF CONSULTANTS

68. The audit included an assessment of the effective use of consultants. In the local government environment, the partnership between the private and public sectors has become important in driving strategic goals.
69. The total expenditure on consultants was R11 012 289.
70. No significant findings were identified.

## PUBLIC PARTICIPATION

71. As part of the audit of predetermined objectives we audit compliance with the provisions of the Municipal Systems Act relevant to community participation. There were no findings identified relating to community participation in terms of the MSA.

## CONDITIONAL GRANTS

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

- Municipal Infrastructure Grant (MIG)
- Expanded Public Works Programme (EPWP)
- Integrated National Electrification Programme (INEP)

73. No significant findings were identified:

Finding	MIG	EPWP	INEP
The grant was not spent according to the applicable grant framework			
The municipality did not evaluate its performance on programmes funded by the grant			
Funds received from DoRA grants transferred to other entities were not in line with section 17(2) of DoRA			

74. For each of the grants tested as per the table above, we selected key projects funded by the grant and audited the use of grants on the projects. The audit findings raised on each project are reported in the table below.



Key projects funded by the grant			
Summary of selected key project and result of testing	Details	Details	Details
Name of grant	<i>MIG</i>	<i>MIG</i>	<i>MIG</i>
Project funded by the grant	<i>Bergville Tarred Road</i>	<i>Makekeni Gravel Road</i>	<i>Mpameni Gravel Road</i>
Audit findings			
Planned completion target for the selected project were not achieved	No findings noted	No findings noted	No findings noted
Project stage of completion was not assessed	No findings noted	No findings noted	No findings noted
Project stage of completion assessed by the municipality is incorrect	No findings noted	No findings noted	No findings noted
Findings on the procurement of goods and services for the project	No findings noted	No findings noted	No findings noted
Misstatements on the accounting for the expenditure relating to the project	No findings noted	No findings noted	No findings noted
Payments were made for goods/services not received	No findings noted	No findings noted	No findings noted
Misstatements on the accounting of funds used through implementing agents	No findings noted	No findings noted	No findings noted
Process for appointing implementing agents did not comply with legislation	No findings noted	No findings noted	No findings noted
Implementing agents failed to comply with SCM prescripts when spending the funds	No findings noted	No findings noted	No findings noted

## ROADS INFRASTRUCTURE

### Roads infrastructure projects

75. The audit also included an understanding of planning, project management and commissioning of key roads infrastructure projects undertaken at the municipality. This included testing the timelines, spending against budget, compliance with procurement processes, appropriate recording of transactions in the financial statements and the quality of the goods and services delivered.

76. The table below summarises the audit findings on the selected key projects

Summary of the key findings		
Project name	Masenga gravel road	Qhozo gravel road
Planning and budgeting for the project		
Brief description of key project	Construction of Masenga gravel road in ward 2	Construction of Qhozo gravel road ward 5
Source of funding	Municipal Infrastructure Grant	Municipal Infrastructure Grant
Project commenced as planned	Yes	Yes
Project completed within defined duration (applicable if completed)	Yes	N/A
Status of completion (applicable if WIP)	100%	71%
Available budget for the year	R2 206 137,55	R4 116 578,75
Actual amount spent in current year	R2 093 697,21	R2 811 388,68
Total project budget (multi-year) – original / revised	R2 206 137,55	R4 116 578,75
Actual amount spent from inception to date	R2 093 697,21	R2 811 388,68
Audit findings		
Execution of the project		
Significant overspending or underspending on budget available for the year	No findings noted	No findings noted
Significant overspending or underspending on total project budget (multi-year)	No findings noted	No findings noted
Findings on the procurement of goods and services for the project	No findings noted	No findings noted
Overall quality of the project management was poor or not acceptable	No findings noted	No findings noted
Findings on consequence management	No findings noted	No findings noted

Summary of the key findings		
Project name	Masenga gravel road	Qhozo gravel road
Findings on fraud	No findings noted	No findings noted
Prior year findings not addressed (if applicable)	No findings noted	No findings noted
Quality of infrastructure		
Goods and services delivered on project of poor or sub-standard quality	No findings noted	No findings noted
Commissioning of the completed project and accounting		
Findings on commissioning of the completed project	No findings noted	No findings noted
Findings on accounting for the project (annual financial statements)	No findings noted	No findings noted
Money used for intended purpose		
Spending not aligned to stage of completion	No findings noted	No findings noted
Budget spent but project milestones not achieved	No findings noted	No findings noted
Findings on grant spending	No findings noted	No findings noted
Findings on fruitless and wasteful expenditure in relation to the project	No findings noted	No findings noted
Findings on irregular expenditure incurred on the project	No findings noted	No findings noted
Infrastructure / facility not utilised for intended purpose	No findings noted	No findings noted
Infrastructure / facility not utilised at all or under utilised	No findings noted	No findings noted

## SECTION 5: Using the work of internal auditors

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

- Reports were used for risk identification and were used to amend the nature, timing and extent of audit procedures.





## SECTION 6: Emerging risks

### Accounting, performance management/reporting and compliance matters

#### New pronouncements

##### Standards of GRAP

The ASB has issued the following GRAP <sup>1</sup> pronouncements, with effective dates as indicated: <b>GRAP pronouncement</b>	<b>Effective date</b>
GRAP 18 - <i>Segment reporting</i>	1 April 2020
GRAP 20 - <i>Related-party disclosures</i>	1 April 2019
GRAP 32 - <i>Service concession arrangements: grantor</i>	1 April 2019
GRAP 34 - <i>Separate financial statements</i>	1 April 2020
GRAP 35 - <i>Consolidated financial statements</i>	1 April 2020
GRAP 36 - <i>Investments in associates and joint ventures</i>	1 April 2020
GRAP 37 - <i>Joint arrangements</i>	1 April 2020
GRAP 38 - <i>Disclosure of interests in other entities</i>	1 April 2020
GRAP 104 - <i>Financial instruments</i> (Revised April 2019)	To be determined
GRAP 108 - <i>Statutory receivables</i>	1 April 2019
GRAP 109 - <i>Accounting by principals and agents</i>	1 April 2019
GRAP 110 - <i>Living and non-living resources</i>	1 April 2020
IGRAP 1 <i>Applying the probability test on initial recognition revenue</i> (amendments)	1 April 2020
IGRAP 17 - <i>Service concession arrangements where a grantor controls a significant residual interest in an asset</i>	1 April 2019
IGRAP 18 - <i>Recognition and derecognition of land</i>	1 April 2019
IGRAP 19 - <i>Liabilities to pay levies</i>	1 April 2019
IGRAP 20 <i>Accounting for adjustments to revenue</i>	1 April 2020
Guideline <i>Accounting for arrangements undertaken in terms of the national housing programme</i>	1 April 2019
Guideline <i>Accounting for landfill sites</i>	To be determined
Guideline <i>The application of materiality to financial statements</i>	Voluntary*
<p>* The Guideline on <i>The application of materiality to financial statements</i> was issued in April 2019. The Guideline is available for immediate consideration, to assist entities to apply the concept of materiality when preparing financial statements in accordance with Standards of GRAP. Although the application of the Guideline is voluntary, application is encouraged.</p>	

#### Subsequent events

- No matters noted.



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

78. The planned and reported performance information of selected [development priorities/objectives] was audited against the following additional criteria as developed from the Performance Management Reporting Framework:
- **Presentation and disclosure – Overall presentation:**
    - Overall presentation of the performance information in the annual performance report is comparable and understandable
  - **Relevance – Completeness of relevant indicators:**
    - Completeness of relevant indicators in terms of the mandate of the auditee, including:
      - relevant core functions are prioritised in the period under review
      - relevant performance indicators are included for the core functions prioritised in the period under review
79. Material audit findings arising from the audit against the additional criteria do not have an impact on the audit opinion of the selected objectives in this report. However, it may impact on the audit opinion in future.
80. No material findings were identified.

### SECTION 8: Ratings of detailed audit findings

81. For the purposes of this report, the detailed audit findings included in annexures A to C have been classified as follows:
- **Matters to be included in the auditor's report:** these matters should be addressed as a matter of urgency.
  - **Other important matters:** these matters should be addressed to prevent them from leading to material misstatements of the financial statements or material findings on the performance report and compliance with legislation in future.
  - **Administrative matters:** these matters are unlikely to result in material misstatements of the financial statements or material findings on the performance report and compliance with legislation.

## SECTION 9: Conclusion

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

Yours faithfully



Lungile Mngayi  
Senior Manager: KZN

11 December 2019

Enquiries:	Neville Barron
Telephone:	033 264 7410
Fax:	033 264 7596
Email:	<a href="mailto:NevilleB@agsa.co.za">NevilleB@agsa.co.za</a>

## SECTION 10: Summary of detailed audit findings

Page no.	Finding	Classification								Rating			Number of times reported in previous three years	Status of implementation of previous year(s) recommendation
		Misstatements in financial statements	Misstatements in annual performance	Non-compliance with legislation	Internal control deficiency	Service delivery	Matters affecting the auditor's report	Other important matters	Administrative matters					
	<b>Property, plant and equipment</b>													
30	Depreciation incorrectly calculated	X								X				
32	Difference between FAR and lease amount	X								X				
	<b>Commitments</b>													
34	Commitments not accurate and complete	X								X				
	<b>Procurement and contract management</b>													
38	Amendment of the contract	X		X						X				
41	Procurement split into parts			X						X				
43	Bid adjudication committee not properly constituted			X						X				
44	Awards made to suppliers and persons in service of the State	X		X						X				
	<b>Information technology</b>													
46	Disaster recovery plan not tested				X					X				
47	No service level agreement				X					X				
48	User access not terminated timeously				X					X				

## Detailed audit findings

### ANNEXURE A: MATTERS AFFECTING THE AUDITOR'S REPORT

No matters to report on.

## ANNEXURE B: OTHER IMPORTANT MATTERS

### 1. Property, plant and equipment - Depreciation

#### Legislation/ Requirement

Section 122(1) of the Municipal Finance Management Act, 2003 (Act no.56 of 2003) (MFMA) states, "Every municipality and every municipal entity must for each financial year prepare annual financial statements which fairly presents the state of affairs of the municipality or entity, its performance against its budget, its management of revenue, expenditure, assets and liabilities, its business activities, its financial results, and its financial position as at the end of the financial year."

Section 62(1) of the MFMA states, "The accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure

- that the resources of the municipality are used effectively, efficiently and economically;
- that full and proper records of the financial affairs of the municipality are kept in accordance with any prescribed norms and standards;
- that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control"

GRAP 17 paragraph 56 states that an entity shall assess at each reporting date whether there is any indication that the entity's expectation about the residual value and useful life of an asset have changed since the preceding reporting date. If any such indication exists, the entity shall revise the expected useful life and/ or residual value accordingly. The change(s) shall be accounted for as a change in accounting estimate in accordance with the Standard of GRAP on Accounting Policies, Changes in Accounting Estimate and Errors (GRAP 3).

Paragraph 64 of GRAP 17 further states that the estimation of the useful life of the asset is a matter of judgment based on the experience of the entity with similar assets. An entity considers all facts and circumstances in estimating the useful lives of assets, which includes the consideration of financial, technical and other factors.

Part 18 paragraph 18.2 of the Asset Management Policy states that depreciation may be defined as the monetary quantification of the extent to which a fixed asset is used or consumed in the provision of the economic benefits or delivery of services.

#### Audit finding

In performing the audit of assets for the current financial year, it was identified that useful lives were incorrectly revised resulting in incorrect calculation of depreciation as detailed in the table hereunder:

No.	Asset description	Asset code	Depreciation as reflected in the FAR	Recalculated depreciation	Difference
1	Mamfemfetheni community Hall and Fence	LS00014	153 809	163 933	10 124
3	New Municipal Office PTN 3 ERF 259	X0071	487 189	543 210	56 021
4	Khethani Municipal Building	X0099	214 524	222 945	8 420

No.	Asset description	Asset code	Depreciation as reflected in the FAR	Recalculated depreciation	Difference
5	Testing Centre	X0101	567 120	587 696	20 576
6	Fire & Emergency Face Brick Walls with Steel Roller	X0102	162 572	167 912	5 340
7	Main Building Face Brick Walls with IBR Roofing	X0103	274 495	285 712	11 217
8	Sidewalks on R74 Kingsway and West FaceBrick	X14029	148 681	154 629	5 949
9	Broadway StreetSurface Layer	X0137	448 661	481 117	32 456
10	Bergville Machanical Workshop	X0013	86 253	110 375	24 122
11	LangKloof Community Centre	X0041	109 654	122 299	12 646
12	LayerGolf Street Extention	GOL001	382 516	410 986	28 471
13	John Westely Street	JOH001	120 395	128 124	7 728
14	Mboromp Gravel Road	MBO001	215 959	235 458	19 500
15	President Street	N0031	85 100	91 183	6 083
16	Tatham Road	X14071	173 066	179 784	6 718
17	Nkwazini Gravel Road Phase 2	X1503	373 896	413 069	39 173
<b>Total</b>			<b>4 003 890</b>	<b>4 298 433</b>	<b>294 543</b>

Depreciation is understated and thus the carrying amounts of the assets are overstated.

#### Internal control deficiency

Management did not properly review the useful lives of assets per the requirement of GRAP before reporting.

There were no proper controls around Asset Management to ensure that the Asset Management Policy is adhered to.

#### Recommendation

It is recommended that management implement controls to ensure depreciation is appropriately calculated and reviewed to ensure accurate recording in the financial statements. The extent of misstatement should be investigated by management.

It is further recommended that the accounting officer should monitor the adherence to the policy.

#### Management response

Management has taken into account the recommendations of the Auditor General in the communication of findings.



The depreciation on the assets is systematically allocated using the asset's useful lives. Management is currently doing an investigation into the matter to ascertain the full extent of the misstatement. The adjustment will be done when the full investigation has been completed.

The Accounting Officer and the management is currently doing the full investigation on the management of Municipal Assets, the plan will be developed, and it will be reviewed by the Assets Management Committee on at Monthly bases.

Name: Mr T Gambu  
Position: Acting CFO  
Date: 30 September 2019

### Auditors conclusion

Management comments are noted. The matter will be reported on the Management Report and follow-up will be performed in the 2019/2020 audit cycle.

## 2. Difference between fixed asset register (FAR) and lease amount

### Legislation/ Regulation

GRAP 17 para 17-18 states that an item of Property, Plant and Equipment that qualifies for recognition as an asset shall be measured at its cost. Where an asset is acquired through a non-exchange transaction, its cost shall be measured at its fair value as at the date of its acquisition.

MFMA section 63 (2) (a-c) states that the accounting officer for the purposes of the above mentioned subsection take all reasonable steps to ensure that the municipality has and maintains a management a management, accounting and information system for those assets of the municipality, the municipality's assets are valued in accordance with the standard of generally recognised accounting practices and the municipality has and maintains a system of internal control of assets including an asset register as may be prescribed.

### Audit finding

Upon inspection of the finance lease asset listing against the FAR it was noted that the fair values at the date of acquisition does not agree.

Bar code	Lease commencement date as per contract	Asset description	Amount as per lease contract	Amount as per FAR	Difference
12736	29 June 2018	8 TONNER FREIGHT CARRIER FAW	R678 000	R779 025	-R101 025,00



### **Internal control deficiency**

There were no adequate controls in place to ensure that the amount recorded on the fixed asset register agrees to the fair value of an asset, as at the date of lease inception.

### **Recommendation**

Management should ensure that the amounts on the underlying records agree to the acquisition documents.

Reconciliations should be performed, on a regular basis, to ensure that the amount recognised in the financials agree to the underlying records.

### **Management response**

Having considered the content of the finding as well as our records, we note the challenge and accept the finding, management takes note of the auditor's recommendations

Name: Mr T Gambu  
Position: Acting CFO  
Date: 15 November 2019

### **Auditors conclusion**

Management comments are noted. The matter will be reported on the Management Report and follow-up will be performed in the 2019/2020 audit cycle.

## Commitment

### 3. Commitments not accurate and complete

#### Legislation/ Requirement

Section 122(1) of the Municipal Finance Management Act, 2003 (Act no. 56 of 2003) (MFMA) states, "Every municipality and every municipal entity must for each financial year prepare annual financial statements which fairly presents the state of affairs of the municipality or entity, its performance against its budget, its management of revenue, expenditure, assets and liabilities, its business activities, its financial results, and its financial position as at the end of the financial year."

Section 62(1) of the MFMA states, "The accounting officer of a municipality is responsible for managing the financial administration of the municipality, and must for this purpose take all reasonable steps to ensure

- that the resources of the municipality are used effectively, efficiently and economically;
- that full and proper records of the financial affairs of the municipality are kept in accordance with any prescribed norms and standards;
- that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control"

#### Audit finding

- (a) When comparing the amount of the contract less payment effect as at 30 June 2019, to the commitment recorded amount disclosed in the annual financial statements, the following differences were noted:

Contract no	Supplier	Project Description	Commitment as per auditor	Commitment as per auditee	Misstatement
<b>Operational Commitment</b>					
SOC05/2016	Vuco Security	Security provision	R3 403 031	R3 381 334	-R21 696
SCM 69/2016/2017	DM ICT services	Redevelopment of municipal website	R0	R138 000	R138 000
SCM 35/2018/2019	One Stop Computers	Maintenance & repairs of cctv, biometrics, queuing system	R113 750	R97 500	-R16 250
PO01308	Nathimisodile Trading cc	Purchase order	R0	R10 168	R10 168
<b>Capital Commitment</b>					
TEC12/2017	Egxen Engineering cc	Construction of Bergville tarred road phase 6	R4 469 068	R5 047 095	R578 026
TEC07/2015	Nhloso Development Consultants cc	Construction of new Bergville sport complex in ward 12	R9 114 498	R9 108 937	-R5 562
TEC02/2018	Gasolar Energy (pty) Ltd	Supply & delivery of fuel and fuel management system	R901 668	R1 195 935	R294 267

Contract no	Supplier	Project Description	Commitment as per auditor	Commitment as per auditee	Misstatement
TEC08/2019	TBA	Construction of Mpameni gravel road	R11 851 061	R10 522 675	-R1 328 385
TEC19/2016	TBA	Construction of emaswazini gravel road	R6 899 291	R6 052 010	-R847 281
TEC09/2019	TBA	Construction of mcijeni community hall	R4 303 587	R3 912 352	-R391 235
<b>Total</b>					<b>-R1 589 948</b>

(b) Furthermore, it was confirmed that the following project was not included in the commitments listing:

Contract	Supplier	Project	Commitment value
TEC 16/2016	Dodwana Construction	Ebhoweni, St Joseph, Greenpoint electrification	R2 784 537

(c) Furthermore, a comparison of the value of goods and services received per capital commitment listing and value of the project per Fixed Asset Register, under work in progress, the following differences were noted:

No	Project name	Goods and services received - Capital Commitments	VAT	Value of work done - excl VAT	Value of project expenditure - WIP	Audit difference
1	Vimbukhalo Community Hall	R3 185 406	R405 776	R2 779 630	R2 924 472	-R144 843
2	Masenga Gravel Road	R2 093 697	R273 091	R1 820 606	R1 904 046	-R83 439
3	The Construction of Ezimbokodweni Gravel Road in Ward 6	R4 804 538	R626 679	R4 177 859	R4 524 402	-R346 544
4	The Construction of Qhozo Access Road In Ward 5	R2 811 389	R366 703	R2 444 686	R2 654 182	-R209 496
5	The Construction Of Ndunwanana Community Hall	R2 123 499	R276 978	R1 846 521	R2 734 702	-R888 182
6	Construction of Ntumba Bridge	R140 543	R18 332	R122 211	R185 153	-R62 942
<b>Total</b>						<b>-R1 735 445</b>

- (d) Bergville Sport Complex: The following misstatement was identified when comparing the expenditure on the commitment schedule with the work in progress capitalised in the PPE:

Expenditure and amount capitalised (FAR)		
Amount as per the listing (Commitments)	Audit Recalculations (FAR)	Difference
70 327 430.79	65 91 565.80	4 435 864.99

Work in progress is misstated by approximately R4 435 864.99.

#### Internal control deficiency

Management did not prepare regular, accurate and complete financial and performance reports that are supported and evidenced by reliable information.

There are inadequate controls in place to ensure that the Capital commitments listing and note to the financial statements are credible.

#### Recommendation

Management should review the financial information and ensure the accuracy and completeness of the amounts disclosed in the financial statement.

#### Management response

We will respond to the findings in the order set out above.

A. Having considered the content of the finding as well as our records, we note the challenge and accept the finding, the management take note of the auditor's recommendations

B. In this matter, the project was no longer listed as a commitment to the Municipality due to the insurmountable challenges that have made the contract incapable of completion and therefore necessitating the Municipality accepting the partial performance as complete performance at this stage.

By way of background, in this project there were two project sites, which each experienced challenges. A summary is tabulated below.

<u>EBHOWENI/VAN REENEN AREA</u>	<u>ST. JOSEPHS AND GREENPOINT AREA</u>
<p>The beneficiaries are situated on the boundary of the coverage area of Free State and the KZN Eskom coverage.</p> <p>As a result, neither Eskom unit is able (or willing) to commit to the electrification and ongoing servicing of the connections.</p> <p>Eskom remains unable to provide an undertaking as to which area station will be able to facilitate these beneficiaries.</p>	<p>The existing Eskom infrastructure is not able to accommodate these connections until the infrastructure at the site is upgraded by Eskom.</p> <p>Eskom does not have any foreseeable plans to upgrade its infrastructure in the area.</p>
<p>The property owner has also refused to allow for the connections to his property in favour of the beneficiaries.</p> <p>The Municipality attempted to mediate in the matter via the ward councillor but was unable to do so.</p>	<p>The land owners have proven to be an obstacle in the process by refusing to sign of the wayleaves allowing for works to be done and barring the surveyors from conducting their works.</p> <p>There is no means of compelling the landowner to do so.</p>

C. Having considered the content of the finding as well as our records, we note the challenge and accept the finding, the management take note of the auditor's recommendations

**Misstatements identified – Bergville Sports Complex**

Upon Managements investigation it was confirmed that the total value of work in progress in the Fixed Asset Register amounts to R 69,997,424.96 not 65 891 565.80 as per the auditor's finding. The complete list of the work in progress is attached.

Name: Mr T Gambu

Position: Acting CFO

Date: 15 November 2019

**Auditors conclusion**

Management Comments noted. It was agreed that the value of the work in progress amounts to R69 997 424, 96, this resulted in a misstatement of R324 444,31. The matter will be reported on the Management Report and follow-up will be performed in the 2019/2020 audit cycle.

## Procurement and contract management

**4. Amendment of the contract not in accordance with the legislation – Bergville Sports Centre****Legislation/ Requirement**

Section 217 (1) of the Constitution of the Republic of South Africa, 1996, states that "When an organ of state in the national, provincial or local sphere of government, or any other institution identified in national legislation, contracts for goods or services, it must do so in accordance with a system which is fair, equitable, transparent, competitive and cost-effective."

Section 116(3) of the Municipal Finance Act, 2003 (Act no. 56 of 2003) (MFMA), Contracts and contract management, stipulates that a contract or agreement procured through the supply chain management policy of the municipality or municipal entity may be amended by the parties, but only after

- (a) the reasons for the proposed amendment have been tabled in the council of the municipality or, in the case of a municipal entity, in the council of its parent municipality; and
- (b) the local community has been given reasonable notice of the intention to amend the contract or agreement and has been invited to submit representations to the municipality or municipal entity.

In addition, National Treasury MFMA circular No. 62 issued in July 2013, stipulates, *inter alia*, it is recognized that, in exceptional cases, an accounting officer of a municipality or municipal entity may deem it necessary to expand or vary orders against the original contract.

The expansion or variation of orders against the original contract has, however, led to wide scale abuse of the current SCM system.

In order to mitigate such practices, accounting officers of municipalities and municipal entities are advised that, from the date of this Circular, contracts may be expanded or varied by not more than 20% for construction related goods, services and/or infrastructure projects and 15% for all other goods and/or services of the original value of the contract. Municipal Councils and Board of Directors of municipal entities are required to amend their supply chain management policies accordingly. Furthermore, anything beyond the abovementioned thresholds must be reported to council or the board of directors.

Any expansion or variation in excess of these thresholds must be dealt with in terms of the provisions of section 116(3) of the MFMA which will be regarded as an amendment to the contract.

**Audit finding**

During the December 2015, the Municipality awarded a contract of R28 957 404.38 for the construction of the Bergville sports complex to Nhloso Development Consultants through the SCM process.

DESCRIPTION	AMOUNT
Sports centre	R23 092 029.02
Contingencies	R2 309 202.90
VAT	R3 556 172.47
<b>TOTAL AWARD</b>	<b>R28 957 404.39</b>



In July 2017, the council took a resolution to extend the scope of works on the Bergville Sports complex to incorporate the construction of the Bergville Community Service Centre and the cost implications were as follows:

<b>PHASE 1: SPORTS CENTRE</b>	
<b>DESCRIPTION</b>	<b>MUNICIPAL CALCULATION</b>
Indoors	22 000 000.00
Clear view Fencing	1 500 000.00
Parking Area	3 000 000.00
Storm water and civil infrastructure	1 300 000.00
Main Soccer and rugby Fields	5 700 000.00
Additional Storm water and parking	5 318 807.09
<b>TOTAL AWARD</b>	<b>34 276 211.47</b>
INITIAL CONTRACT VALUE	- 28 957 404.39
<b>ADDITIONAL SCOPE</b>	<b>5 318 807.08</b>
<b>PHASE 2: COMMUNITY SERVICE CENTRE</b>	
<b>DESCRIPTION</b>	<b>MUNICIPAL CALCULATION</b>
Bergville CSC	21 249 116.47
Athletic tracks	6 500 000.00
2x Grand stands'	5 500 000.00
Combi Courts	800 000.00
Parking Area	2 600 000.00
<b>TOTAL AWARD</b>	<b>36 149 116.47</b>
<b>TOTAL AWARDS</b>	
SPORTS CENTRE	34 276 211.47
BERGVILLE CSC	36 149 116.47
	<b>70 425 327.94</b>
<b>TOTAL VARIATION/ADDITIONAL SCOPE</b>	
SPORTS CENTRE	5 318 807.08
COMMUNITY CENTRE	36 149 116.47
	<b>41 467 923.55</b>

#### Issues identified:

#### Reasons for the amendment

- Section 116(3)(a) of the MFMA requires that the municipality provides council with the reasons for the proposed amendment of a contract. On inspection of the submission to council, we could not identify the reasons for the amendment to the contract being tabled in council. As no reason is tabled, it does not provide a reasonable explanation

why the SCM process was not followed for the construction of the community service centre and the additional work at the sports centre.

- On inspection of the advert that was sent for public participation, the municipality only included details of 4 tenders that were going to be extended but there were no details included on what the specific extensions were to allow for public comment. Even though there was compliance in terms of section 116(3)(b)(ii) of the act, the spirit of transparency was not adhered to as required by the Constitution and the SCM regulations.

### **Circumvention of the SCM process**

- The amendment to the contract was done in a manner that circumvents the SCM process. The Constitution and the SCM regulations require that all the SCM processes be fair, equitable, transparent and cost effective to the municipality. There is no demonstration of the cost effectiveness of this process. The scope added to the existing contract included a new phase of the project (construct the Community service centre) and this cannot constitute an amendment to a contract.
- The competitive bidding process should have been followed for the construction of the community service centre as this was a project separate from the sports complex.

### **CIDB Grading**

- CIDB regulation 17 requires that the winning contractor's grading be suitable for the value of contract.
- The contractor has a CIDB Grading of 7CE which allows him to undertake work to a maximum of R40 million. The new contract value was R70 425 327.94 which is above what the contractor can undertake, suggesting that the contractor might not have had capacity to handle the contract of this magnitude.
- The CIDB requires that if the contract was awarded to a contractor who is registered at a grade lower than the required grade: -
  - the margin with which the tenderer exceeded his/her tender value range is reasonable (not more than 15%) and
  - the award of the contract does not pose undue risk to the organ of state (there must be risk assessment done).
  - The margin with which the tenderer exceeds his tender value is 76% which is not allowed, also no risk assessment was undertaken.

### **Summary**

- The total variation/increase in scope should be declared as irregular expenditure for the reasons noted above. The irregular expenditure in the AFS will be limited to the actual expenditure to date for the community service centre on the basis that the SCM process was not followed.

### **Internal control deficiency**

The SCM Manager and the CFO did not ensure that there are adequate processes in place to ensure compliance with legislation.

The financial statements were not adequately reviewed to ensure all the proper disclosures were made.





### **Recommendation**

- The financial statements should be amended accordingly.
- Management must ensure that adequate processes are implemented to ensure that legislation is correctly applied on all awards made.
- Regularly reconciliations must be performed to ensure complete disclosures in the AFS.

### **Management response**

Due to the complex nature of the matters underlying the concerns raised by the AG with regard to the Community Service Centre element of the Development as well as the issues surrounding the CIDB grading of the Service Provider, we have set out our response in the annexure attached.

### **Auditors' conclusion**

#### **CIDB Grading**

- The matter was resolved.

#### **Circumvention of the SCM process**

Management comments are noted, however:

- The amendment to the contract was done in a manner that circumvents the SCM process. The Constitution and the SCM regulations require that all the SCM processes be fair, equitable, transparent and cost effective to the municipality. This was not demonstrated.
- The construction of the Community Service Centre does not constitute an amendment to the contract to construct the sports complex.
- A competitive bidding process should have been followed for the construction of the community service centre as this was a project separate from the sports complex.
- The amendments to the financial statements are noted. The matter will be reported in the Management Report and follow-up will be performed in the 2019/2020 audit cycle.

## **5. Procurement split into parts**

### **Legislation/ Requirement**

Supply chain management regulation paragraph 12(3) states

- (a) "Goods or services may not be deliberately split into parts or items of a lesser value merely to avoid complying with the requirements of the policy.
- (b) When determining transaction values, a requirement for goods or services consisting of different parts or items must as far as possible be treated and dealt with as a single transaction."

### **Audit finding**

During the audit of procurement and contract management process it was noted that the following procurement was split into two awards:



SCM reference	Details	Date of award	Amount (R)
SCM48/2018-19 - Likamva Consultants	Sub-division at Rookdale Cemetery	2018/12/21	150 000
SCM54/2018-19 - Likamva Consultants	Subdivision at Bergville cemetery	2018/12/21	150 000
<b>Total</b>			<b>R300 000</b>

### Internal control deficiency

Management did not have adequate procedures and processes in place to ensure that supply management regulations were adhered with prior to requesting quotations to identify requisitions that could be treated as single transactions.

### Recommendation

Management should institute adequate procedures and processes to ensure that the supply chain management regulations are adhered to.

### Management response

Early in the procurement process for the sub-division of the properties for the cemeteries it became apparent that these are two separate areas completely removed from each other. Rookdale Cemetery is situated in Ward 10 and Bergville Cemetery in Ward 11

Whilst the end product might have been similar following the process, the works involved in the process for each site required that the properties be dealt with individually as separate projects.

This does not constitute non-compliance with Section 12(3) as the projects were completely separate and needed to be administered as such.

Name: Mr T Gambu

Position: Acting CFO

Date: 28 October 2019

### Auditors conclusion

Management comments are noted. However, this remains irregular expenditure as paragraph 12(3) of SCM Regulations has not been complied with.

**6. Bid adjudication committee was not constituted in accordance with SCM policy****Legislation/ Requirement**

Supply chain management regulations, paragraph 29(2) states "A bid adjudication committee must consist of at least four senior managers of the Municipality which must include:

- (a) The chief financial officer or if the chief financial officer is not available, another manager in the budget and treasury office reporting directly to the chief financial officer and designated by the chief financial officer and
- (b) At least one senior supply chain management practitioner who is an official of the Municipality and
- (c) A technical expert in the relevant field who is an official if such an expert exists."

**Audit finding**

During the audit of procurement and contract management process it was noted that the following awards were adjudicated by an adjudication committee that constituted of three senior managers and one secretary which is not in accordance with the SCM regulations:

SCM reference	Details	Date of adjudication	Award Amount	Expenditure to date
TEC12/2018 – A1 Electrical	Electrification	2018/12/04	R4 968 411	R886 908
TEC13/2018 – Thando's Electrical			R2 890 368	R581 489
TEC14/2018 – Bobcon Builders			R2 625 897	R706 313
Total			R10 484 677	R2 174 711

**Internal control deficiency**

Management did not ensure that the bid adjudication committee was constituted in accordance with the SCM regulations.

**Recommendation**

Management should institute procedures and policies to ensure that bid adjudication committees are constituted in accordance with the SCM regulations.

**Management response**

The policy does state that at least four senior managers must be part of the bid adjudication committee. At the time of adjudicating these tenders the director technical services was the acting municipal manager and could therefore not sit on the bid adjudication committee. The replacement for the director technical services in the bid adjudication committee was appointed in January 2019.

The quorum for the bid adjudication to sit is 50% plus 1, there are four members in the bid adjudication committee and therefore the quorum is three members. The above tenders were adjudicated by 3 members of the BAC, who formed a quorum.



Name: Mr T Gambu  
 Position: Acting CFO  
 Date: 05 November 2019

### Auditors conclusion

Management comments are noted. However, the bid adjudication committee was not constituted as required in terms of the supply chain management regulations. The resultant expenditure is, therefore deemed to be Irregular.

## 7. Awards made to Suppliers and Persons in service of the State

### Legislation/ Requirement

Supply chain management policy paragraph 44(a) states "Irrespective of the process followed, no award may be made to a person in terms of this Policy:

(a) Who is in service of the state"

### Audit finding

Computer Assisted Audit Techniques (CAATs) performed revealed that the following awards were made to people in service of the state:

Supplier	Director in service of the state	State organisation	Current year expenditure
Judy Magwaza Trading Enterprise	Heria Magwaza	South African Broadcasting Corporation	R3 398 392
Emakozeni Trading Enterprise Cc	Thandeka Madikane	Majuba FET College	R1 219 912
Sunlyn Pty Ltd	D Skwambane	Industrial Development Corporation of SA	R1 109 255
Ilifa Africa Engineers (Edms) Bpk	Joyce Dolly Tembe	National Home Builders Registration Council	R5 219
Work Dynamics (Pty) Ltd	LC Nene	PetroSA	R14 575
Gijima Holdings (Pty) Ltd	Mr Ashwin Hirjee Trikamjee	The KwaZulu Natal Royal Household Trust	R16 607
Eca Consulting Civil & Structural Engineers	Lungiseni Manda	Transnet Group	R140 543

### Internal control deficiency

Sufficient procedures were not exercised by management in identifying suppliers in service of the state in order to ascertain instances where false declarations have been submitted.

### Recommendation

The accounting officer should investigate the above exceptions as they are evidence of fraudulent practices being performed by the suppliers in question.

### Management response

As part of the Municipality's internal control processes the MBD4 form is provided to service providers to declare their interests; which the auditor has also confirmed. The Municipality will

explore other ways (if possible) of validating the information of the declarations as recommended by the Auditor.

Name: Mr T Gambu  
Position: Acting CFO  
Date: 05 November 2019

**Auditors conclusion**

Management's response is noted and this will be followed up in the next audit.

## Information Technology

### **8. Disaster Recovery Plan not tested.**

#### **Audit finding**

The Disaster Recovery Plan (DRP) had not been tested for the period under review.

In the absence of regular DRP testing the Municipality may not be aware of shortcomings of the planned disaster recovery and would not be able assess its effectiveness to recover critical business operations in an objective and quantifiable manner. In the event of an emergency, the Municipality may not be able to restore operations to predefined levels in a timely manner due to the lack of testing and associated refinement of the DRP.

#### **Internal control deficiency**

Management did not prioritised the testing of the Disaster Recovery Plan.

#### **Recommendation**

Management should ensure that there are sufficient resources for testing the Disaster Recovery Plan (DRP). DRP testing should be performed on a periodic basis. The results of these tests should be evaluated and benchmarked against required criteria to ensure the effectiveness of the DRP. The DRP should be updated in line of the results that were obtained from the test.

#### **Management response**

Management notes the audit finding. The last disaster recovery testing for the period under review was performed on the 18<sup>th</sup> of June 2019. The proof of the testing is attached to this response.

Name: Mr T Gambu

Position: Acting CFO

Date: 28 October 2019

#### **Auditors conclusion**

Management comments are noted. However, evidence provided by Management supported that back-ups had been performed and not that the Disaster Recovery Plan had been tested as. The matter will be reported on the Management Report.



## **9. No service level agreement and inadequate service provider monitoring for VIP Payroll**

### **Audit finding**

The municipality did not formally monitor the performance of the third party service provider who supports the VIP Payroll system and no service level agreement is in place for VIP Payroll.

In the absence of formal monitoring of service provider performance, management is not aware of any deviations from agreed upon service levels or sub-standard received from VIP Payroll consultant.

### **Internal control deficiency**

Management does not have adequate processes and procedures as well as service level agreement to monitor the service provided by VIP Payroll Consultant.

### **Recommendation**

Service level agreement should be in place and regular performance monitoring of services received should be performed against the service level agreement signed with the service provider.

### **Management response**

The management note the Audit Finding, the municipality has appointed the New payroll system which we are currently on the implementation stage and we will be live on the new system in December 2019, The item for the Municipal Manager to sign the SLA will be table in council on the 31<sup>st</sup> October 2019.

Name: Mr T Gambu

Position: Acting CFO

Date: 28 October 2019

### **Auditors conclusion**

Management comments are noted. The matter will be reported on the Management Report and follow-up will be performed in the 2019/2020 audit cycle.

**10. User access not terminated immediately after employee suspension or resignation****Audit finding**

The following employees had active user status on 06/08/2019:

Employee Name	Position	Resigned/ suspended	Month of resignation/ suspension
Yali Joyi	CFO	Resigned	21 June 2019
Sthabiso Hlatshwayo	Cashier	Suspended	Suspended during 2018/2019 financial year

Former employee and suspended employee of the municipality have access to SAGE Evolution. This result in the system being vulnerable to abuse and misuse which compromises the integrity of the information.

**Internal control deficiency**

Management does not have adequate processes and procedures for the timely removal of access for users.

**Recommendation**

Management should ensure that adequate processes and procedures are developed and implemented to ensure that employees access to IT systems is adequately monitored to ensure access is deactivated timeously for employees who resign or are suspended.

**Management response**

Management note the audit finding, the mansion two former employees in this communication their access to SAGE Evolution has been removed. The municipality going forward will immediately terminate the access to SAGE Evolution. The list of employees that have access to SAGE Evolution is attached to this response

Name: Mr T Gambu

Position: Acting CFO

Date: 28 October 2019

**Auditors conclusion**

Management comments are noted. The matter will be reported on the Management Report and follow-up will be performed in the 2019/2020 audit cycle.

## ANNEXURE C: ADMINISTRATIVE MATTERS

No matters to report.

## **Annexure D: Performance management and reporting framework**

The Performance Management and Reporting Framework (PMRF) consists of the following:

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

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

Criteria		References to PMRF per Institution	
		Municipalities	Municipal Entities
<b>Consistency: Objectives, performance indicators and targets are consistent between planning and reporting documents.</b>			
1. Reported strategic or development objectives are consistent or complete when compared to planned objectives.	Section 121(3)(f) of the MFMA Section 41 (a) - (c) & 46 of the MSA	Section 121(4)(d) of the MFMA	
2. Changes to strategic or development objectives are approved	Section 25(2) of the MSA	Section 54(1)(c) of the MFMA	
3. Reported indicators are consistent or complete when compared to planned indicators	Section 121(3)(f) of the MFMA Section 41 (a) - (c) & 46 of the MSA	Section 121(4)(d) of the MFMA	
4. Changes to indicators are approved	Section 25(2) of the MSA	Section 54(1)(c) of the MFMA	
5. Reported targets are consistent or complete compared to planned targets	Section 121(3)(f) of the MFMA Section 41 (a) - (c) & 46 of the MSA	Section 121(4)(d) of the MFMA	
6. Changes to targets are approved	Section 25(2) of the MSA	Section 54(1)(c) of the MFMA	
7. Reported achievements are consistent with the planned and reported indicator and target	Section 121(3)(f) of the MFMA	Section 121(4)(d) of the MFMA	
<b>Measurability: Performance indicators are well defined and verifiable, and targets are specific, measurable and time bound.</b>			
1. A performance indicator is well defined when it has a clear, unambiguous definition so that data will be collected consistently and is easy to understand and use.	Chapter 3.2 of the FMPPi		
2. A performance indicator is verifiable when it is possible to validate or verify the processes and systems that produce the indicator.	Chapter 3.2 of the FMPPi		



Criteria	References to PMRF per Institution	
	Municipalities	Municipal Entities
3. A target is specific when the nature and required level of performance of the target is clearly identifiable.	Chapter 3.3 of the FMPP	
4. A target is measurable when the required performance can be measured.	Chapter 3.3 of the FMPP	
5. A target is time bound when the timeframes for achievement of targets are indicated.	Chapter 3.3 of the FMPP	
<b>Relevance: Performance indicators relate logically and directly to an aspect of the Institution's mandate and the realisation of its strategic goals and objectives.</b>		
1. The performance indicator and target relates logically and directly to an aspect of the Institution's mandate and the realisation of its strategic goals and objectives.	Chapter 3.2 of the FMPP	
<b>Presentation and disclosure: Performance information in the annual performance report are presented and disclosed in accordance with the requirements contained in the legislation, frameworks, circulars and guidance.</b>		
1. Actual performance compared to planned targets and prior year performance is disclosed in the annual performance report	Section 46 of the MSA	Section 46 of the MSA
2. Measures taken to improve performance are disclosed in the annual performance report	Section 46 of the MSA	Section 46 of the MSA
3. Measures taken to improve performance are corroborated with audit evidence	Section 46 of the MSA	Section 46 of the MSA
<b>Reliability: Recording, measuring, collating, preparing and presenting information on actual performance achievements is valid, accurate and complete.</b>		
1. Reported performance occurred and pertains to the reporting entity.	Section 45 of the MSA	Section 45 of the MSA
2. Amounts, numbers and other data relating to reported performance is recorded and reported correctly.	Chapter 5 of the FMPP	Chapter 5 of the FMPP
3. All actual performance that should have been recorded is included in the reported performance information.		

## **Annexure E: Auditor-general's responsibility for the audit of the reported performance information**

1. As part of our engagement conducted in accordance with ISAE 3000, we exercise professional judgement and maintain professional scepticism throughout our reasonable assurance engagement on reported performance information for selected objective.
11. We are independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) together with the ethical requirements that are relevant to our audit in South Africa. We have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA code.

### **QUALITY CONTROL RELATING TO ASSURANCE ENGAGEMENTS**

12. In accordance with the International Standard on Quality Control 1, the Auditor-General of South Africa maintains a comprehensive system of quality control that includes documented policies and procedures on compliance with ethical requirements and professional standards.

### **REPORTED PERFORMANCE INFORMATION**

13. In addition to our responsibility for the assurance engagement on reported performance information as described in the auditor's report, we also:
  - identify and assess risks of material misstatement of the reported performance information, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. In making those risk assessments, we consider internal control relevant to the management and reporting of performance information per selected objective in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control.
  - evaluate the documentation maintained by the municipality that supports the generation, collation, aggregation, monitoring and reporting of performance indicators/measures and their related targets for the selected objective.
  - evaluate and test the usefulness of planned and reported performance information, including presentation in the annual performance report, its consistency with the approved performance planning documents of the municipality and whether the indicators and related targets were measurable and relevant.
  - evaluate and test the reliability of information on performance achievement to determine whether it is valid, accurate and complete.

## **COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE**




14. We communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also confirm to the accounting officer that we have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to bear on our independence and, where applicable, related safeguards.

## Annexure F: Assessment of internal controls











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

The internal controls were assessed as follows:

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
















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

	Improved
	Unchanged
	Regressed

	Financial statements		Performance reporting		Compliance with legislation	
	Current year	Prior year	Current year	Prior year	Current year	Prior year
<b>Leadership</b>						
<b>Overall movement from previous assessment</b>						
• Provide effective leadership based on a culture of honesty, ethical business practices and good governance, and protecting and enhancing the best interests of the entity						
• Exercise oversight responsibility regarding financial and performance reporting and						

	Financial statements		Performance reporting		Compliance with legislation	
	Current year	Prior year	Current year	Prior year	Current year	Prior year
compliance as well as related internal controls						
• Implement effective human resource management to ensure that adequate and sufficiently skilled resources are in place and that performance is monitored						
• Establish and communicate policies and procedures to enable and support the understanding and execution of internal control objectives, processes and responsibilities						
• Develop and monitor the implementation of action plans to address internal control deficiencies						
• Establish and implement an information technology governance framework that supports and enables the business, delivers value and improves performance						
<b>Financial and performance management</b>						
<b>Overall movement from previous assessment</b>						
• Implement proper record keeping in a timely manner to ensure that complete, relevant and accurate information is accessible and available to support financial and performance reporting						
• Implement controls over daily and monthly processing and reconciling transactions						
• Prepare regular, accurate and complete financial and performance reports that are supported and evidenced by reliable information						
• Review and monitor compliance with applicable legislation						
• Design and implement formal controls over information technology systems to ensure the reliability of the systems and the availability, accuracy and protection of information						



	Financial statements		Performance reporting		Compliance with legislation	
	Current year	Prior year	Current year	Prior year	Current year	Prior year
<b>Governance</b>						
<b>Overall movement from previous assessment</b>						
<ul style="list-style-type: none"> <li>Implement appropriate risk management activities to ensure that regular risk assessments, including the consideration of information technology risks and fraud prevention, are conducted and that a risk strategy to address the risks is developed and monitored</li> </ul>						
<ul style="list-style-type: none"> <li>Ensure that there is an adequately resourced and functioning internal audit unit that identifies internal control deficiencies and recommends corrective action effectively</li> </ul>						
<ul style="list-style-type: none"> <li>Ensure that the audit committee promotes accountability and service delivery through evaluating and monitoring responses to risks and overseeing the effectiveness of the internal control environment, including financial and performance reporting and compliance with legislation</li> </ul>	