

REPORT OF THE AUDITOR-GENERAL TO THE FREE STATE LEGISLATURE AND THE COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF MANTSOPA LOCAL MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2008

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the Mantsopa Local Municipality which comprise the balance sheet as at 30 June 2008, income statement and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages [xx] to [xx].

Responsibility of the accounting officer for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the specimen financial statements of the Institute of Municipal Finance Officers (IMFO) and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2007 (Act No. 1 of 2007) (DoRA). This responsibility includes:
 - designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
 - selecting and applying appropriate accounting policies
 - making accounting estimates that are reasonable in the circumstances.

Responsibility of the Auditor-General

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA) and section 126(3) of the MFMA, my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with the International Standards on Auditing and *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance on whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.
6. An audit also includes evaluating the:
 - appropriateness of accounting policies used
 - reasonableness of accounting estimates made by management
 - overall presentation of the financial statements.

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

Basis of accounting

8. The municipality's policy is to prepare financial statements in accordance with the specimen financial statements of IMFO.

Basis for qualified opinion

Cash and Bank

9. The correctness of the bank overdraft of R27 361 as reflected in the balance sheet could not be verified due differences which included the following:
- An un-reconciling difference of R2 122 135 existed between the cash book and the bank statement as at 30 June 2008.
 - Unallocated deposits amounted to R3 241 298 which represent debtors receipts not allocated to specific debtors account.

This might result in the misstatement of bank, revenue and debtors.

Proper bank reconciliations were not performed throughout the financial year which is considered to be a crucial control measure to identify and clear differences timeously.

Inventory

10. The existence and completeness of the inventory balance of R465 770 as disclosed in note 9 to the financial statements could not be verified due to deficiencies identified during the audit. It included the following:
- Differences have been identified during the physical count of inventory. No evidence could, however, be found that these differences have been cleared.
 - No records are maintained to control the movement of inventory in and out of the stores at Ladybrand, Hobhouse and Tweespruit.
 - No evidence could be submitted that regular inventory counts were conducted to identify obsolete and missing stock.
 - Supporting documentation to substantiate the value of the stock items, amounting to R26 632, could not be submitted.
 - Inventory was identified on the inventory sheets that were not valued which resulted in inventory being understated.

Alternative procedures could not be performed due to the lack of stock records and purchase vouchers and the deficiency could not be quantified.

Consumer deposits

11. No monthly reconciliation was done between the deposit register and deposit control account which resulted in the deposit control account been overstated by R1 148 613.

Expenditure

12. Documentation to support expenditure transactions amounting to R444 708 could not be submitted. The system of control over the recording and classification of these expenses were not adequate and as a result there were no alternative audit procedures that I could perform to obtain reasonable assurance that all these expense transactions had occurred and were correctly and accurately recorded and classified in the financial records of the municipality.

Creditors

13. Included in creditors as presented in the balance sheet and disclosed in note 13 to the financial statements are unallocated deposits amounting to R1 909 915. I was unable to obtain sufficient appropriate audit evidence as to the existence, completeness and valuation of this balance as at yearend. This may indicate that creditors and consumer debtors are overstated, while revenue may be understated. The VAT implications on these unallocated deposits are also uncertain and have not been considered. The records of the municipality also did not permit me to perform reasonable alternative procedures in respect of these deposits.

Centlec disclosure

14. Contrary to section 122 of the MFMA the income of R1 433 491 and the expenditure of R274 073 as disclosed in the financial statements of Centlec, were not disclosed in the income statement of the municipality. The net surplus of R1 159 418 was however disclosed as income in the income statement of the municipality.

Irregular expenditure

15. The regularity of procedures followed by a consulting firm to advise the municipality on an appropriate service provider to replace an electrical distribution installation amounting to R167 523 could not be determined. In the absence of a decisive reply by the municipality, I was not satisfied that the accounting officer did take all reasonable steps to prevent unauthorised, irregular or fruitless and wasteful expenditure and/or other losses as required by section 62(1)(d) of the MFMA. This expenditure constitutes irregular expenditure in terms of section 1 of the MFMA and it was not disclosed in the financial statements as required by section 125 of the MFMA.

Qualified opinion

16. In my opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had I been able to satisfy myself as to the matters described in the Basis for qualified opinion paragraphs, the financial statements of the Mantsopa Local Municipality as at 30 June 2008 and its financial performance and cash flows for the year then ended have been prepared, in all material respects, in accordance with the basis of accounting as set out in accounting policy note¹ and in the manner required by the MFMA and DoRA.

OTHER MATTERS

I draw attention to the following matter that relates to my responsibilities in the audit of the financial statements:

Internal controls

17. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes that gave rise to the inefficiencies in the system of internal control, which led to the qualified opinion. The root causes are categorised according to the five components of an effective system of internal control. In some instances deficiencies exist in more than one internal control component.

Reporting item	Control environment	Risk assessment	Control activities	Information and communication	Monitoring
Cash and bank	X		X		X
Inventory	X		X		X
Consumer deposits	X		X		X
Expenditure	X		X		
Creditors	X		X		
Centlec disclosure	X	X	X		X
Irregular expenditure	X	X	X		X

Control environment: establishes the foundation for the internal control system by providing fundamental discipline and structure for financial reporting.

Risk assessment: involves the identification and analysis by management of relevant financial reporting risks to achieve predetermined financial reporting objectives.

Control activities: policies, procedures and practices that ensure that management's financial reporting objectives are achieved and financial reporting risk mitigation strategies are carried out.

Information and communication: supports all other control components by communicating control responsibilities for financial reporting to employees and by providing financial reporting information in a form and time frame that allows people to carry out their financial reporting duties.

Monitoring: covers external oversight of internal controls over financial reporting by management or other parties outside the process; or the application of independent methodologies, like customised procedures or standard checklists, by employees within a process.

Non-compliance with applicable legislation

Municipal Finance Management Act, 2003 (Act No. 56 of 2003)

18. In terms of section 21 of the MFMA, the mayor of the municipality must at least 10 months before the start of the budget year, table in the municipal council a time schedule outlining key deadlines. Although a time schedule was submitted to audit, the minutes concerned could not be submitted.

19. In terms of section 11(4) of the MFMA, the accounting officer must within 30 days after the end of each quarter table in the municipal council a consolidated report of all withdrawals made during that quarter, and submit a copy of the report to the relevant provincial treasury and the Auditor-General. Contrary to the above, a copy of the report was not submitted to the Auditor-General.
20. Economic utilisation of feedlot: In terms of a Council Resolution, farming activities of the municipality were stopped and the land advertised to be rented out. Although the cattle were sold on an auction on 9 May 2008, it was noted during the audit that the feedlot which should have been rented out was still not advertised for rental. Contrary to section 62 of the MFMA, no income are being generated from a capital investment of R8 300 950.
21. Contrary to section 125(2)(e) of the MFMA, the municipality did not disclose particulars of non-compliance with the MFMA in the notes to the annual financial statements.

Matters of governance

22. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of certain key governance responsibilities, which I have assessed as follows:

Matter of governance	Yes	No
Audit committee		
• The municipality had an audit committee in operation throughout the financial year?	X	
• The audit committee operates in accordance with approved, written terms of reference.	X	
• The audit committee substantially fulfilled its responsibilities for the year, as set out in Section 166(2) of the MFMA.	X	
Internal audit		
• The municipality had an internal audit function in operation throughout the financial year.	X	
• The internal audit function operates in terms of an approved internal audit plan.	X	
• The internal audit function substantially fulfilled its responsibilities for the year, as set out in Section 165(2) of the MFMA.		X
Other matters of governance		
• The annual financial statements were submitted for audit as per the legislated deadlines in section 126 of the MFMA.		X
• The annual report was submitted to the auditor for consideration prior to the date of the auditor's report.		X
• The financial statements submitted for audit were not subject to any material amendments resulting from the audit.	X	
• No significant difficulties were experienced during the audit concerning delays or the unavailability of expected information and/or the unavailability of senior management.	X	
• The prior year's external audit recommendations have been substantially implemented.		X

Matter of governance	Yes	No
<ul style="list-style-type: none"> The Provincial SCOPA resolutions have been substantially implemented. 		X
Implementation of Standards of Generally Recognised Accounting Practice (GRAP)¹		
<ul style="list-style-type: none"> The municipality submitted an implementation plan, detailing progress towards full compliance with GRAP, to the National Treasury and the relevant provincial treasury before 30 October 2007. 	X	
<ul style="list-style-type: none"> The municipality substantially complied with the implementation plan it submitted to the National Treasury and the relevant provincial treasury before 30 October 2007, detailing its progress towards full compliance with GRAP. 	X	
<ul style="list-style-type: none"> The municipality submitted an implementation plan, detailing further progress towards full compliance with GRAP, to the National Treasury and the relevant provincial treasury before 31 March 2008. 	X	

Unaudited supplementary schedules

23. The supplementary information set out in pages [XX] to [XX] of the financial statements does not form part of the financial statements and is presented as additional information. I have not audited this schedule and accordingly I do not express an opinion thereon.

OTHER REPORTING RESPONSIBILITIES

REPORT ON PERFORMANCE INFORMATION

I have reviewed the performance information as set out on pages xx to xx.

Responsibility of the accounting officer for the performance information

24. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No.32 of 2000) (MSA)

Responsibility of the Auditor-General

25. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008* and section 45 of the MSA.
26. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.
27. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

Audit findings (performance information)

Non-compliance with regulatory requirements

28. The municipality did not develop and implement mechanisms, systems and processes for auditing the results of performance measurement as part of its internal audit processes, as required in terms of section 45 of MSA.
29. Contrary to section 46 of the MSA, a comparison of the performance of the municipality with targets set and performance in the previous financial year, as well as measures taken to improve performance, was not disclosed in the annual performance report.

Measurable objectives are materially inconsistent between annual report and integrated development plan

30. I draw your attention to the fact that the measurable objectives reported in the annual report of the municipality are materially inconsistent when compared with the predetermined objectives as per integrated development plan.

Objectives/indicators/targets reported in annual report, but not predetermined as per strategic/corporate/annual performance/integrated development plan and/or budget

31. I draw attention to the fact that objectives are reported in the annual report of the municipality, although they were not included as predetermined objectives in the integrated development plan.

Lack of sufficient appropriate audit evidence

32. I was unable to obtain sufficient and appropriate audit evidence in relation to the performance information of the municipality, as I was unable to obtain access to records substantiates the reported performance information.

APPRECIATION

33. The assistance rendered by the staff of the Mantsopa Local Municipality during the audit is sincerely appreciated.

Auditor-General
Bloemfontein

30 January 2009



A U D I T O R - G E N E R A L