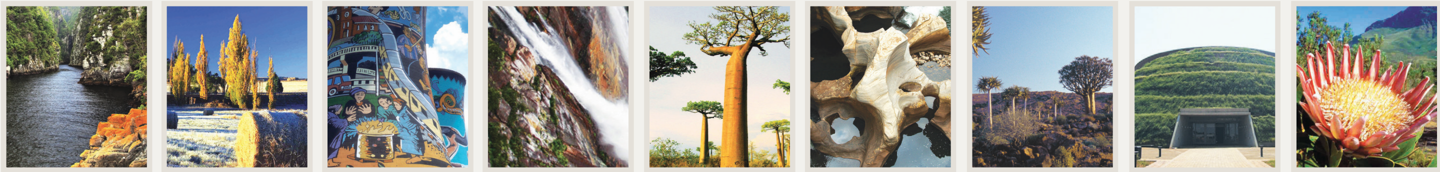


CONSOLIDATED
GENERAL REPORT ON THE LOCAL GOVERNMENT AUDIT OUTCOMES

MFMA
2015-16

AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence

AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence

MFMA
2015-16

CONSOLIDATED

GENERAL REPORT ON THE LOCAL GOVERNMENT AUDIT OUTCOMES

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

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

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

Auditor-General

Kimi Makwetu
Auditor-General

Our reputation promise/mission

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

CONTENTS

ANNEXURES

The annexures containing information on the following are available on **www.agsa.co.za** (our website):

Annexure 1: Auditees' audit outcomes; areas qualified; and findings on predetermined objectives, compliance, specific risk areas and unauthorised, irregular as well as fruitless and wasteful expenditure

Annexure 2: Auditees' financial health indicators, SCM findings and root causes

Annexure 3: Auditees' audit opinions over the past five years

Annexure 4: Assessment of auditees' key controls at the time of the audit

A This icon is used in the report to refer to the annexures

To access the content of this report on our website, simply use the **QR code scanner** on your mobile phone or tablet to scan the code.

CLEAN AUDITS 2015-16

Unqualified financial statements with no material findings on the quality of the performance report or compliance with key legislation

EASTERN CAPE

MUNICIPALITIES

Joe Gqabi District
Engcobo
Ingquza Hill
Matatiele
Nyandeni
Senqu
Umzimvubu

MUNICIPAL ENTITIES

Chris Hani Development Agency
Mandela Bay Development Agency
Ntinga OR Tambo Development Agency

FREE STATE

MUNICIPALITIES

Fezile Dabi District

MUNICIPAL ENTITIES

No municipal entity in the Free State achieved a clean audit

GAUTENG

MUNICIPALITIES

Midvaal

MUNICIPAL ENTITIES

Brakpan Bus Company
Ekurhuleni Development Company
Germiston Phase II Housing Company
Joburg City Theatres
Joburg Property Company
Johannesburg Development Agency
Johannesburg Social Housing Company
Lethabong Housing Institute
Pharoe Park Housing Company

KWAZULU-NATAL

MUNICIPALITIES

Ilembe District
Umgungundlovu District
Uthungulu District
eMnambithi / Ladysmith
Endumeni
Mandeni
Okhahlamba
uMhlabuyalingana
uMhlathuze
Umuziwabantu
Umzumbe

MUNICIPAL ENTITIES

Durban Marine Theme Park
ICC, Durban
Ilembe Management Development Enterprise
South Coast Development Agency
Ugu South Coast Tourism

LIMPOPO

MUNICIPALITIES

No municipality in Limpopo achieved a clean audit

MUNICIPAL ENTITIES

No municipal entity in Limpopo achieved a clean audit

MPUMALANGA

MUNICIPALITIES

Ehlanzeni District
Nkangala District
Steve Tshwete

NORTHERN CAPE

MUNICIPALITIES
Frances Baard District
ZF Mgcawu District

NORTH WEST

MUNICIPALITIES
No municipality in North West achieved a clean audit

MUNICIPAL ENTITIES
No municipal entity in North West achieved a clean audit

WESTERN CAPE

MUNICIPALITIES

City of Cape Town Metro
Cape Winelands District
Central Karoo District
Eden District
Overberg District
West Coast District
Bergriver
Bitou
Breede Valley
Cape Agulhas
Drakenstein
George
Hessequa
Knysna
Langeberg
Matzikama
Mossel Bay
Overstrand
Saldanha Bay
Stellenbosch
Swartland
Swellendam
Theewaterskloof
Witzenberg

MUNICIPAL ENTITIES

Cape Town International Convention Centre

1 Executive summary

1. Executive summary

The 2014-15 general report highlighted the significant progress made since 2010-11 in improving the audit outcomes in local government, but the rate of improvement was very marginal and limited in 2015-16.

The accountability that the municipal leadership must take for their actions, decisions and policies (including being answerable to the community) is critical for financial and performance management as well as respect for the law in local government. However, the limited improvement in audit outcomes over the past year shows that accountability for these important functions is not as strong as it should be. The focus of many municipal leaders was on the **local government elections** and important interventions to address vacancies and instability as well as poor control environments were postponed with the view that it would receive attention by the new administration or that the amalgamation as a result of the **re-demarcation of municipal boundaries** would address it.

Furthermore, the 2016-17 audit outcomes can be negatively affected if the new administration 'disowns' the audit outcomes of the previous years and does not follow through on the commitments made by their predecessors to improve audit outcomes. We call on the municipal leadership to ensure that accountability is given the highest priority from the start. Hence, the **central theme of this report is accountability**.

The key drivers of **internal control**, being leadership, financial and performance management as well as governance, had shown minimal improvement since the previous year. This slow response by the leadership to our consistent messages over the years to improve internal controls and address risks, was the main **root cause of poor audit outcomes**. Continued vacancies and instability in key positions as well as inadequate consequences for poor performance and transgressions further contributed to these outcomes.

As a result of these root causes not being addressed, there was **limited improvement in the audit outcomes of municipalities**, with 15% improving, 13% regressing and 67% remaining unchanged. The number of municipalities with clean audit opinions decreased, which included two metros that lost their clean audit status. Clean audit opinions represented only 19% of the total local government expenditure budget.

The audit outcomes of municipalities in **the Eastern Cape, Limpopo and Mpumalanga showed momentum in the right direction**, with the Eastern Cape showing the greatest improvement. The improvements in the Eastern Cape can be attributed to improved record keeping, the support provided by the provincial treasury and the provincial department responsible for cooperative governance (provincial Cogta), the leadership attending to audit recommendations, the implementation of the minimum competency levels, and the use of consultants. The improvements in Limpopo were as a result of increased focus to resolve audit findings in response to a strong stance taken by the premier that steps will be taken against municipal managers if audit outcomes are poor. In Mpumalanga, strong leadership, accountability and good human resource (HR) management at an increased number of municipalities had the desired effect.

The **Western Cape** continued with setting the pace by increasing their clean audit opinions to 80% of their municipalities. The focused interventions and support by the provincial leadership through the premier's coordinating forum, operation clean audit and the municipal governance review and outlook process continued to bear fruit. Although **Gauteng** continued to perform well and was the only province where 100% of the municipalities received unqualified audit opinions on their financial statements, only Midvaal could hold on to its clean audit status. Not paying sufficient attention to supply chain management (SCM) and performance reporting led to three municipalities losing their clean audit status of the previous year.

After a notable improvement in 2014-15, the audit outcomes of **KwaZulu-Natal showed a significant regression** this year. Instability and vacancies in key positions, coupled with the lack of accountability, internal control failures related to compliance with key legislation that were not adequately monitored as well as the leadership's slow response to recommendations made by internal audit units and audit committees, contributed to the regression at 14 municipalities.

The provinces with the **poorest outcomes** (based on the number of municipalities with disclaimed and adverse opinions or outstanding audits) were **North West** (35%), **the Northern Cape** (31%) and **the Free State** (29%).

There was little improvement in these provinces. Focused political will and a considerable investment in ensuring that the basics are done right are required to create a baseline from which accountability can be restored and strengthened.

The outcomes in the three main areas that we audit are as follows:

- The **audit opinions on the financial statements only slightly improved** from 60% to 62% unqualified opinions, while disclaimed and adverse opinions decreased from 13% to 10%. The revised Medium-Term Strategic Framework (MTSF) targets of 65% unqualified opinions, 20% qualified opinions and a maximum of 15% disclaimed or adverse opinions by 2018-19 can therefore be achieved. Municipalities continued to **rely on consultants**, at a cost of R838 million (2014-15: R823 million), to prepare financial statements and underlying records, and **on auditors** to identify material misstatements to be corrected. Only 31% (rather than the reported 62%) of municipalities would have received an unqualified audit opinion had we not identified the material misstatements and allowed them to make corrections. We found that at 130 municipalities (57%), the financial statements submitted for auditing included material misstatements in the areas in which consultants did work, meaning that the misstatements were identified and corrected by the audit process and not by the consultants. This remains a concern regarding the effective use of such consultants. Furthermore, the poor quality of the financial statements submitted for auditing resulted in increased audit time and cost.

  We are further concerned about the readiness of municipalities to **implement the classification framework of the Municipal Regulations on a Standard Chart of Accounts (mSCOA)** from 1 July 2017 and have shared these concerns with the National Treasury. Slow progress is being made by municipalities in preparing for the implementation – we assessed that the readiness of 73% of the municipalities was of concern while intervention was required at 11%. Various challenges, including those relating to skills, system readiness and funding, need to be addressed to ensure that the implementation does not affect the ability of municipalities to produce reliable financial statements in 2017-18.
- The audit area that showed the **greatest improvement was the quality of performance reports**, with the number of municipalities with no material findings in this regard increasing from 38% to 47%. Only 31% of municipalities would have had this positive outcome had we not identified the material misstatements and allowed them to make corrections. The increased quality of this important service delivery accountability mechanism is encouraging, but a lot of improvement is still needed. The usefulness of the information in these reports significantly improved (with the number of municipalities with findings decreasing from 45% to 38%), but almost half of the municipalities still struggled to report reliable information on service delivery.
- There was a **slight regression in the compliance with key legislation**, with the number of municipalities with no material findings decreasing from 20% to 18%. The lapse in oversight and controls in the area of compliance was evident in a number of areas, including SCM and consequence management, leading to increased irregular expenditure.

Irregular expenditure had increased by just over 50% since the previous year to R16,81 billion – the highest since we started tracking the values. The amount could be even higher, as a third of the municipalities disclosed that the full amount was not known and 24% were qualified as the amount they disclosed was incomplete. The top 10 contributors to irregular expenditure were responsible for 42% of the irregular expenditure – the majority of which involved water and sanitation infrastructure projects and grant money. There is thus a need for increased oversight of this portfolio, which should be given priority attention.

The irregular expenditure does not necessarily represent wastage or mean that fraud has been committed – this needs to be confirmed through investigations to be done by the council – but losses could already have arisen or may still arise if follow-up investigations are not undertaken. The track record of local government in **dealing with irregular expenditure** and ensuring that there is accountability is poor. The year-end balance of irregular expenditure that had accumulated over many years and had not been dealt with (through recovery, condonement or write-off) was R41,7 billion. The poor follow-up was not limited to irregular expenditure – 54% of the municipalities that incurred unauthorised, irregular and/or fruitless and wasteful expenditure in 2014-15 had not completed all investigations by the end of 2015-16.

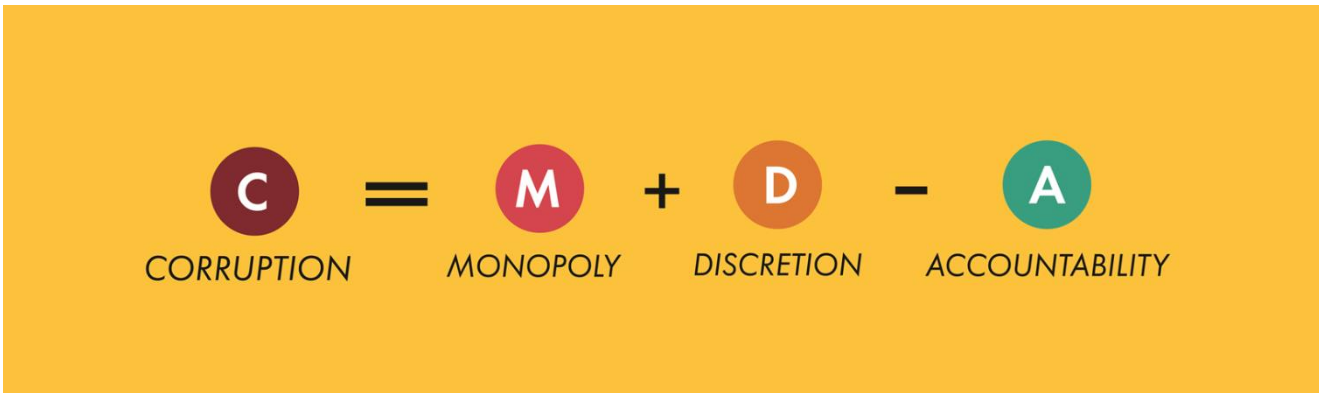
The significant increase can be **attributed overall to a weakening in SCM** at municipalities, particularly in the areas of competitive bidding (46%) and obtaining three quotations (56%), which led to irregular expenditure.

The management of contracts also regressed (44%) and there had been no improvement in addressing the concerns we have raised year after year about contracts being awarded to employees, councillors, their families and other state officials as well as documents going missing when we want to audit a procurement process. Municipalities were also dragging their feet in preparing for the implementation of the **SCM reforms** introduced by the National Treasury, which include a central supplier database and the eTender portal. Although these reforms should have been implemented from 1 July 2016, 63% of municipalities either had not started using the database or portal or had not updated their SCM policies by then.

Last year, we reported 1 648 instances of suppliers submitting false declarations of interest as part of the procurement processes, but 47% of the municipalities did not investigate any of the cases we reported to them – this year, we reported 2 015 instances. Instances of employees not declaring interests had an even lower investigation rate, with 64% of the municipalities not investigating any of the cases. In 2015-16, we reported **poor and non-compliant consequence management practices** at 61% of the municipalities – an increase from the 53% in the previous year.

Municipalities with poor consequence management practices are often prone to corruption or fraud, as a result of municipal officials not being held accountable, as illustrated in the figure below.

Figure 1: Corruption formula



If a person has monopoly over goods or services and has the discretion to decide whether someone gets such goods or services or how much someone receives, and there is no accountability whereby others can see what that person is deciding, we will tend to find corruption.

Fruitless and wasteful expenditure was 21% lower in 2015-16 than in the previous year at R901 million. **Unauthorised expenditure** remained almost at the same level as in the previous year at R12,77 billion. In total, 55% of the overspending related to non-cash items – in other words, estimates of depreciation or impairment that were not correctly budgeted for. It is important for municipalities to correctly budget for these non-cash items and to show the true financial state of the municipality.

The poor quality of financial statements submitted to us for auditing and the continuing reliance on consultants for financial reporting services call into question whether municipalities' in-year reporting and management of finances are solid. Signs of **poor financial management** were apparent in the budget preparation and monitoring processes (resulting in unauthorised expenditure) and the financial viability of municipalities, which continued to weaken year on year. In 2015-16, we rated the **financial health** of 65% of the municipalities as either concerning or requiring intervention. The most concerning indicators over the past two years were municipalities spending more than the resources they had available (thus incurring a net deficit), current liabilities exceeding current assets at year-end (net current liability position), debtors not paying or taking very long to pay their debt, and creditors not being paid on time. In total, 27% of municipalities were in a particularly **poor financial position** by the end of 2015-16, with material uncertainty with regard to their ability to continue operating in the foreseeable future.

As local government does not generate enough revenue to fund all its operations and capital projects, national government provides conditional grants to municipalities for specific purposes. Our audit of the management of the **municipal infrastructure grant** (MIG), the **urban settlement development grant** (USDG) and the **public transport network grant** (PTNG) confirmed that the funds were fully utilised and were used for their intended purpose at the vast majority of municipalities. The main concerns with the projects funded by the MIG were that the targets set for 35% of the projects were not achieved or the municipalities had not assessed their performance against the targets as well as non-compliance with SCM prescripts on 29% of the projects.

Our audits included an assessment of aspects of the provision of water and sanitation as well as road infrastructure by local government. The work on water and sanitation was an extension of the performance audit report we published in November 2016 on water infrastructure. The performance report can be found on our website at www.agsa.co.za.

Water and sanitation infrastructure projects were mostly funded by grants, which were not fully utilised at 22% of the receiving municipalities, while there were isolated cases (six) where municipalities used the grants for other infrastructure projects and even to fund operating expenditure. Our main findings were that the projects did not always address the cause of the backlog in the provisioning of water and sanitation, projects at some municipalities were running behind schedule, and non-compliance with SCM prescripts in procuring goods and services for the projects. Over half of the municipalities responsible for providing water did not have the basic policies and plans in place to ensure that **maintenance of water infrastructure** took place. At 34%, conditional assessments of the infrastructure were not done to inform maintenance plans and budgets, with 24% of municipalities not budgeting anything for maintenance. It does then not come as a surprise that 41% of municipalities experienced water losses above the norm of 30% in 2015-16 – the average water losses for these municipalities were 52%. In total, 9% did not even disclose their water losses.

Poor policies and plans as well as inadequate maintenance were also again observed at the municipalities responsible for **road infrastructure**. Just over half of these municipalities did not have policies or maintenance plans, or did not implement them. At 20%, no conditional assessment was done of the roads to inform maintenance plans and budgets.

In 2015-16, **vacancies** in the positions of municipal manager, chief financial officer (CFO) and head of the SCM unit increased, most notably those of CFOs (vacancies at 27% of municipalities). As the contracts of these key officials come to end in 2016-17, the instability created by the vacancy rate at the end of 2015-16 could increase. We call on the political leadership to carefully consider the impact of instability and a loss of skills – especially since significant progress has been made by these officials in achieving the prescribed competency levels. Other areas with regard to resource management that need attention are the **financial management capacity** of municipalities (the capacity at 52% of municipalities is of concern while urgent intervention is needed at 8%); and the **management of consultants** (poor performance management and monitoring was identified at 60% of municipalities – an increase from the previous year – while the inadequate transfer of skills was identified at almost half of the municipalities).

Information technology (IT) controls ensure the confidentiality, integrity and availability of state information, enable service delivery and promote security in local government. The strength of financial management controls is dependent on IT controls and it is thus essential for good IT governance, effective IT management and a secure IT infrastructure to be in place. Although the status of IT controls had improved since the previous year, only 18% of municipalities were assessed as having good IT controls and continued focus is needed in the areas of security management, user access management and IT continuity. The employment of a chief information officer (CIO) or IT manager with the required qualifications and experience had a positive impact at 56% of the municipalities.

The **assurance provided** by senior management, mayors, councils and municipal public accounts committees (MPACs) remained at low levels and showed little improvement in the past year, while that of municipal managers regressed. Although internal audit units and audit committees had the highest assurance levels, little progress had been made in the past year and they had little impact on the audit outcomes at more than half of the municipalities.

The **national Department of Cooperative Governance (DCoG), provincial Cogtas, treasuries and offices of the premier** are responsible to support and strengthen the capacity of municipalities.

In total, 90% did not provide the level of assurance required. The MTSF and the back-to-basics (B2B) programme placed specific responsibilities on the cooperative governance departments and treasuries, but our audits showed that the oversight and support provided by the cooperative governance departments were inadequate and the level of support at provincial level was uneven, resulting in differing outcomes and responses to the MTSF and B2B programme. National and provincial government need to pay urgent attention to our findings and the commitments they made to support local government to ensure that the goals of these initiatives are achieved.

In this report, we propose the use of the **'plan+do+check+act' cycle** (as illustrated in figure 2 below) to continuously improve the processes, outcomes and services of municipalities and thereby strengthen accountability.

Figure 2: Plan+do+check+act cycle

We provide a number of recommendations to contribute to this improvement process, of which the main ones are outlined below:

PLAN: Spend sufficient time and consult widely to clearly **define the targets** that should be achieved by the municipality in terms of audit outcomes, service delivery (including project delivery and infrastructure maintenance) and financial health using, among others, audit action plans, the new integrated development plan, service delivery and budget implementation plans, annual budgets, and maintenance and project plans. These targets should be specific, measurable, achievable, relevant and time bound. **Responsibilities** for achieving the targets should be allocated and **sufficient time and resources** should be provided to ensure that performance is managed through robust internal control and strong financial management.

DO: Good **internal control** is the key to ensuring that municipalities deliver on their priorities in an effective, efficient and economical manner, produce quality financial statements and performance reports, and comply with applicable legislation – especially in the area of procurement and contract management.

It is the responsibility of municipal managers, senior managers and municipal officials to implement and maintain effective and efficient systems of internal control; hence, is it crucial that the **key positions** of municipal manager, CFO and head of the SCM unit are filled with people with the required competencies. Stability in these positions also correlated with good audit outcomes. Municipalities with poor audit outcomes should strengthen their financial and performance management systems through ensuring that the **basics** for a good internal control environment are in place, namely effective leadership, audit action plans, proper record keeping, daily and monthly disciplines, and the review and monitoring of compliance.

CHECK: A key element of internal control is **monitoring** by the different assurance providers to ensure that internal controls are adhered to, risks are managed, and outcomes are achieved. We urge the new administration to ensure that all the assurance providers understand their roles, are equipped to perform their functions and are given the authority their role requires, and that the outcome of their monitoring and oversight is appropriately responded to.

ACT: Accountability means that those performing actions or making decisions are answerable for them, but also that there should be consequences for transgressions, lack of action and poor performance. Municipalities should implement **consequence management** for officials who fail to comply with applicable legislation, while appropriate and timely action must be taken against transgressors. A less tolerant approach should be followed by all parties, including those charged with governance and oversight, which will result in accountability being enforced and consequences instituted against those who intentionally fail to comply with legislation.

Our country's constitution stipulates that local government should provide a democratic and an accountable government for local communities. We believe that the newly elected mayors and councillors and the administration that supports them are ready to accept their responsibilities and are willing to be held accountable for the performance of the municipalities they now govern.

Leading up to the finalisation and launch of this report, engagements took place in all the provinces. These sessions were convened by the premiers with members of the executive council (MECs), mayors, municipal managers and councillors. There was overwhelming support for the key control engagements that focused on the status of accounting records. We have also undertaken to provide feedback to leadership structures on the progress (or lack thereof) achieved through these engagements. We were encouraged by the tone and undertaking to act on our recommendations and observations.

Consequences and accountability featured as prominent elements of these engagements and we trust that all those concerned will act on their commitments and help restore trust in the ability of municipalities to look after their finances well. This will enable them to progressively meet their service commitments to citizens.

My office remains committed to working tirelessly within our mandate to strengthen financial and performance management in local government in South Africa, emphasising the need to do the basics right. We wish the new political leadership and administration well for the new term and encourage all stakeholders involved in local government to intensify their efforts to ensure that communities experience an improvement in the way their municipalities operate.

NOTES

2 Introduction

2.1 Introduction

The **local government elections** took place on 3 August 2016, just over a month after the 2015-16 year-end and a few weeks before the financial statements and performance reports had to be submitted for auditing. The **re-demarcation of municipal boundaries** also came into effect shortly after the 2016 elections, which resulted in the amalgamation of 39 municipalities, effectively closing down the administration and political structures of 21 municipalities. These two major events had an impact on the 2015-16 results, contributing to the slow progress made in improving audit outcomes since the previous year. The political leadership at some municipalities was more focused on the election and little was done to improve the vacancies and instability in local government with the view that this would receive attention in 2016-17, or that the amalgamations would address it. The political leadership and municipal officials did not prioritise addressing weaknesses in the control environment. The opportunity has already presented itself where the new leadership in local government has a chance to prioritise these matters over the next five years of their term.

The 2014-15 general report provided an overview of the audit outcomes and our messages since 2010-11, and we highlighted that the audit outcomes in 2011-12 had significantly regressed after the 2011 elections. This was as a result of instability following changes in the political leadership and at the level of municipal manager and senior management, including the non-renewal of contracts.

A closer assessment of the matters raised during the analyses of these outcomes is the following:

- Financial management
- SCM
- Maintenance of the accounting records
- Follow-through on action plans
- Supporting documentation
- HR controls and management of consultants
- IT controls
- mSCOA

All of the above matters can be addressed decisively over the term of this administration.

In this context, we introduced quarterly key control engagements with all municipalities in the 2016-17 financial year. The main thrust of this intervention is the evaluation and review of the status of accounting records. The objective is to appraise management and the leadership of the areas of significant audit risk that require their priority action. It is hoped that this will be a sufficient red-flag mechanism to enable swift management reaction before major disasters materialise in the control of finances.

In local government, the political leadership and municipal officials must achieve their municipalities' objectives while acting in the public interest at all times and consistently adhering to the requirements of legislation and government policies. **Acting in the public interest** implies that municipalities' primary consideration should be improving the lives of citizens. **Accountability** is the principle that municipal leaders are answerable to the public and take responsibility for their actions, decisions and policies. Municipalities should be able to demonstrate the appropriateness of all of their actions and should have mechanisms in place to encourage and enforce adherence to ethical values and to respect the rule of law. These concepts of public interest and accountability are entrenched in the country's constitution and the legislation that governs local government.

The MTSF defines the overall outcome for local government (outcome 9) to be 'a responsive, accountable, effective and efficient developmental local government system'. This is the target that municipalities are working towards.

In order to achieve this, we propose the use of the **'plan+do+check+act' cycle**. This cycle, also known as the Deming cycle, is used courtesy of the International Organization for Standardization. It is a repetitive, four-stage approach for continually improving processes, products and services. The cycle encourages a commitment to continuous improvement, which is consistent with the recommendations we have been communicating in the past few years to improve audit outcomes through our reports. As illustrated in figure 1, following this approach will ensure a solid foundation for accountability in the work of municipalities.

Figure 1: Plan+do+check+act cycle – committing to accountability

PLAN: In the context of improved audit outcomes, the **target should be defined** and time and resources should be allocated to ensure that performance is managed through robust internal control and strong financial management.

DO: Municipalities should have and sustain **performance management systems** that facilitate effective and efficient delivery of planned services. A strong system of **financial management** is essential for the implementation of policies and the achievement of intended outcomes, as it will enforce financial discipline, strategic allocation of resources, efficient service delivery, and accountability.
Risk management and internal control are important and integral parts of a financial and performance management system, and are crucial to the achievement of outcomes. These two parts consist of an ongoing process designed to identify and address significant risks to achieving outcomes.

CHECK: A key element of internal control is monitoring by the different assurance providers to ensure that internal controls are adhered to, risks are managed, and outcomes are achieved.

ACT: Accountability means that those performing actions or making decisions are answerable for them, but also that there should be consequences for transgressions, a lack of action and poor performance.

Focused attention on improving financial and performance management and compliance with legislation to achieve better audit results will contribute to achieving the MTSF targets for local government, resulting in a better life for citizens.

Committing to accountability and following the plan+do+check+act cycle will assist the new political leadership and administration to have a positive impact on their municipalities from the first year.

The rest of our report provides a view of the audit outcomes for 2015-16 and their movement since the previous year as well as recommendations for improvement (in section 10), which link to the cycle described above. We focus on municipalities throughout the report, but summarise the key audit outcomes of municipal entities in section 11.

We use icons in this report to indicate the following:

A References to the annexures

Proposed recommendations to assist auditees to improve their audit outcomes

Examples to illustrate the effects of weaknesses

When studying the figures and reading the report, please note that the percentages are calculated based on the completed audits of 263 municipalities, unless indicated otherwise. Movement over a period is depicted as follows:

Improved

Unchanged / Slight improvement / Slight regression

Regressed

2.2 Status of internal control

Good **internal control** is the key to ensuring that municipalities deliver on their priorities in an effective, efficient and economical manner, produce quality financial statements and performance reports, and comply with applicable legislation – especially in the area of procurement and contract management. It is the responsibility of municipal managers, senior managers and municipal officials to implement and maintain effective and efficient systems of internal control.

Figure 1 shows the status of the different drivers of internal control over the past three years and the movement since the previous year. We determined the movements taking into account either increases in good controls or reductions in controls requiring intervention.

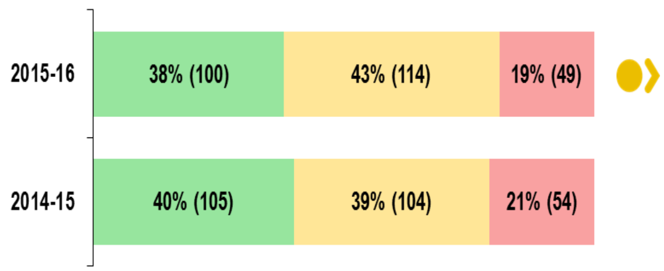
Figure 1: Drivers of internal control

As illustrated in figure 1, all three drivers of internal control had shown little improvement since the previous year, with leadership even showing a slight regression. This corresponds to the limited improvement in audit outcomes and regressions at some municipalities as detailed in section 3.1.

Basic controls

In figures 2 to 6, we deal with a number of basic controls that should receive specific attention.

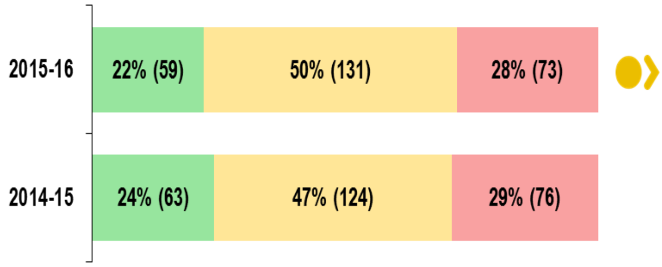
Figure 2: Effective leadership



In order to improve and sustain audit outcomes, municipalities require **effective political and administrative leadership** that is based on a culture of honesty, ethical business practices and good governance, which protects and enhances the interest of the municipality.

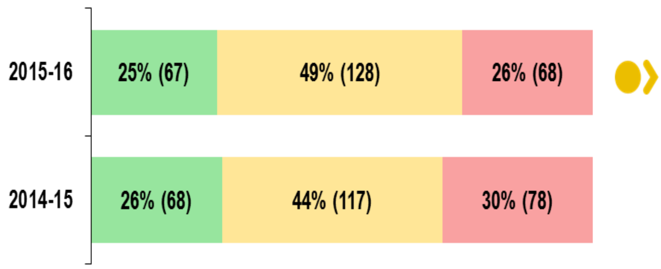
The leadership culture controls had remained unchanged overall, despite the slight reduction in good controls and those requiring intervention.

Figure 3: Audit action plans



The controls relating to **audit action plans** had regressed slightly. The reason for this was that in many cases audit action plans responded only to our audit findings and did not always address the associated root causes, while not all audit action plans that had been drawn up were fully implemented. Furthermore, audit action plans did not sufficiently take into account recommendations relating to other role players, such as internal audit units and audit committees, or risks arising from municipalities' own risk-assessment processes.

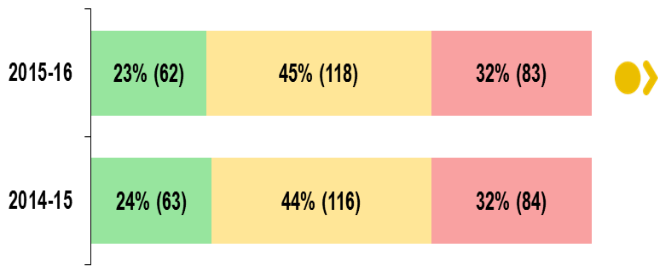
Figure 4: Proper record keeping



Record-keeping controls had improved slightly due to a reduction in the number of municipalities whose controls required intervention; however, the number of municipalities with good controls in this area remained low.

Proper and timely record keeping ensures that **complete, relevant and accurate information** is accessible and available to support financial and performance reporting. Sound record keeping will also enable senior management to hold staff accountable for their actions. A lack of documentation affects all areas of the audit outcomes.

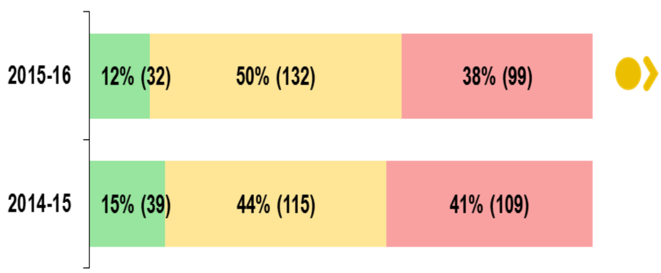
Figure 5: Daily and monthly controls



Controls should be in place to ensure that **transactions are processed in an accurate, complete and timely manner**, which in turn will reduce errors and omissions in financial and performance reports.

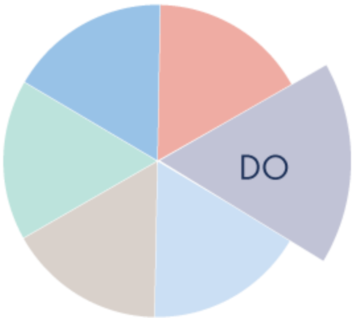
There was a slight regression in daily and monthly controls due to a slight decrease in municipalities with good controls.

Figure 6: Review and monitor compliance



The controls relating to **monitoring compliance** slightly regressed and continued to be the poorest control area at municipalities. Many municipalities did not comply with legislation (as detailed in section 4.2), while most of the irregular expenditure incurred was still identified during the audit process. This indicates that the internal controls of most municipalities not only failed to prevent non-compliance with legislation, but also failed to timeously detect the deviations, some of which were only detected during, and responded to following, our audits.

Details of HR management, consultants and IT controls, which also form part of the basic controls and are critical to internal control, are discussed later on in this report.



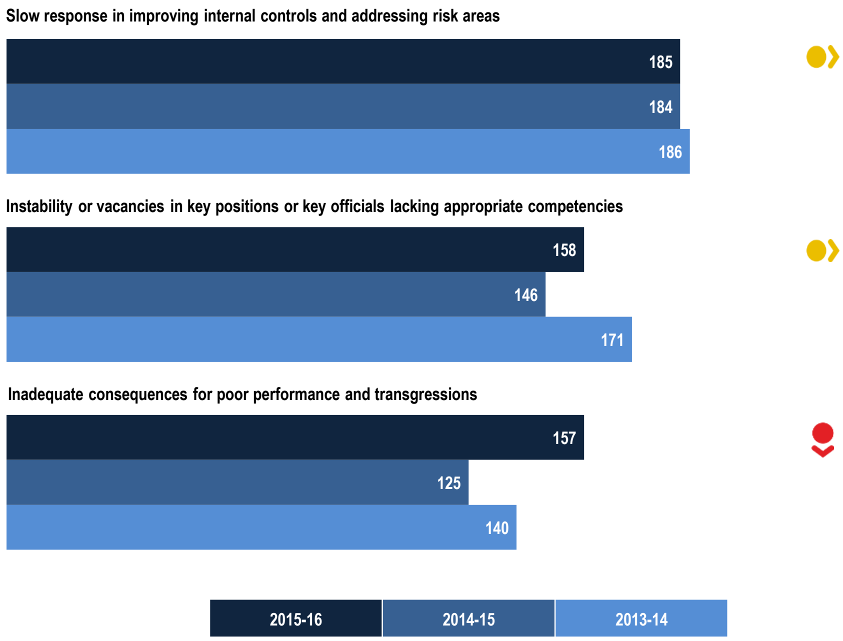
Strong internal controls are the key to unlocking improvements in local government. If underlying weak internal controls are not addressed, it increases the risk of the misappropriation of funds, unreliable financial and performance reporting as well as non-compliance with legislation. On the other hand, a sound internal control environment that is monitored in a robust manner by the different assurance providers (as further discussed in section 9) will enable **effective, efficient and economical service delivery**, **accurate and reliable financial and performance reporting** as well as **compliance with legislation**. This in turn will facilitate accountability and transparency in the management of public funds.

2.3 Root causes

The main root causes of municipalities' continuing inability to improve internal controls and obtain better audit results are discussed below.

Our message on these root causes has remained constant over the years. As illustrated in figure 1, however, there had been **little improvement** in the response to root causes since the previous year and a definite **increase in municipalities where the root cause of poor audit outcomes was inadequate consequences**.

Figure 1: Status of overall root causes



Slow response in improving internal controls and addressing risk areas

The most common root cause was that management (accounting officers and senior management), the political leadership (mayors and councils) and oversight structures (MPACs and portfolio committees) **did not respond with the required urgency** to our messages about addressing risks and improving internal controls. Our message and its delivery have been consistent for a number of years, but the slow response to this message and to the initiatives taken by national and provincial government is standing in the way of improvements in audit outcomes.

The **main reasons for the slow response** in 2015-16 were the following:

- All municipalities had audit action plans but for some it was focused on the short term – to only fix the problems that resulted in audit report findings. There was no capacity or even competency to address the gaps at some of the municipalities, while a small number of municipalities only paid attention to our recommendations and the action plan during the audit.
- Unfortunately, there were municipalities where the leadership had no desire to improve internal controls, as the lack of controls (especially with regard to record keeping) enabled an environment conducive to corruption.
- Some municipalities did not aspire to a clean audit opinion and were content with an unqualified audit opinion with findings, with no commitment to address poor performance reporting and non-compliance.
- Municipalities continued to rely on the auditors and consultants to assist them at year-end to fix the financial statements and the performance report. As a result, there was little motivation to improve the municipal capacity in this regard.
- The attention of officials and the political leadership at some municipalities was diverted by the local government elections in that their main focus was on campaigning.
- Officials and the political leadership of the municipalities that were to be amalgamated were not motivated to correct errors or prevent them from happening again.

Instability or vacancies in key positions or key officials lacking appropriate competencies

Vacancy levels and instability in key municipal positions did not receive the required attention in 2015-16, although there was a definite move towards obtaining the **minimum competency requirements** for these positions (as detailed in section 6.1). The high demand for consultants and support from national and provincial government, however, serves as evidence of the remaining competency gap. Where competencies were confirmed, a lack of leadership and accountability existed to ensure that municipal officials performed the duties for which they were appointed.

We continued to see the negative impact of instability and prolonged vacancies in key positions on the audit outcomes.

Inadequate consequences for poor performance and transgressions

The low level of action in response to the high levels of non-compliance, poor audit outcomes, SCM transgressions and unauthorised, irregular as well as fruitless and wasteful expenditure **demonstrated a lack of consequences** in local government for poor performance and transgressions.

It is important that officials who deliberately or negligently ignore their duties and contravene legislation should be dealt with decisively through performance management and by enforcing the legislated consequences for transgressions. If they are not held accountable for their actions, the perception is created that such behaviour and its results are acceptable and tolerated. Section 4.2.4 provides more detail in this regard.

The objectives of municipalities and improved audit outcomes will not be achieved if poor internal controls and instability are not addressed (**DO**) and the leadership and officials are not held accountable through implementing consequences for transgressions, a lack of action and poor performance (**ACT**).

3 Status of progress on the audit outcomes

3.1 Overall audit outcomes

Local government consists of 278 municipalities and 51 municipal entities. We analyse the audit outcomes of municipalities in sections 3 to 10 and those of municipal entities in section 11.

We set the cut-off date for inclusion of the audit outcomes in this report as 15 January 2017. By this date, 15 audits were still outstanding. More information in this regard is provided in section 3.2.

Figure 1 reflects the audit outcomes of the 278 municipalities, while table 1 analyses the movement in audit outcomes per type of municipality from the previous year.

Figure 1: Slight improvement in audit outcomes since the previous year

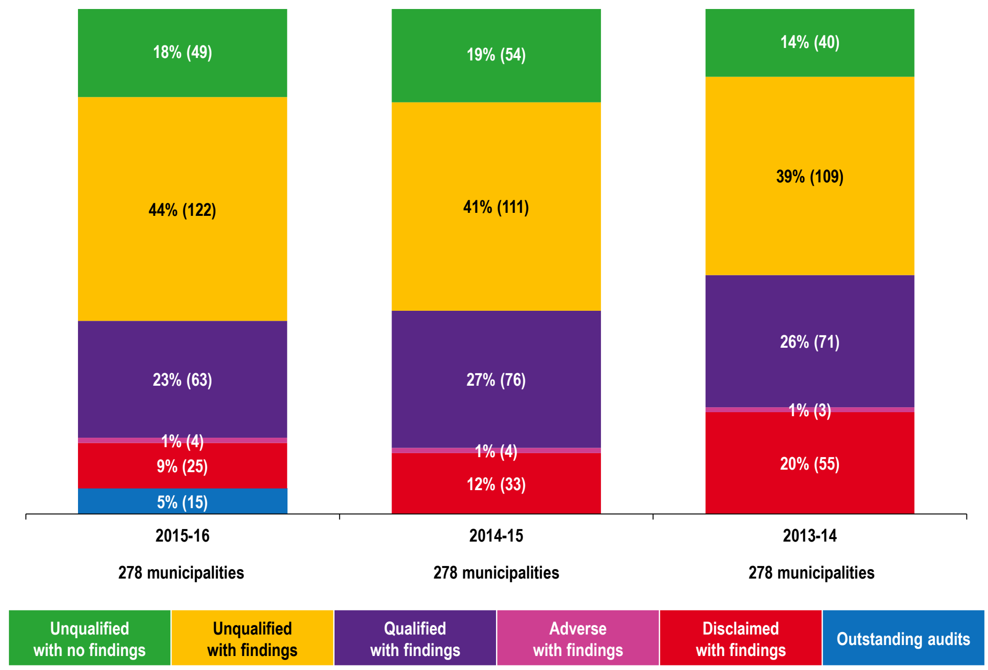


Table 1: Movement in audit outcomes from 2014-15 to 2015-16

Movement → / Audit outcome ↓	42 Improved	185 Unchanged	36 Regressed	15 Outstanding audits
Unqualified with no findings = 49	2 (DM), 7 (LM)	1 (MET) 12 (DM) 27 (LM)		
Unqualified with findings = 122	3 (DM), 16 (LM) 2 (LM)	2 (MET) 11 (DM) 75 (LM)	2 (MET) 4 (DM) 7 (LM)	1 (MET) 2 (LM)
Qualified with findings = 63	1 (LM) 8 (LM)	2 (MET) 4 (DM) 38 (LM)	1 (LM) 3 (DM), 6 (LM)	3 (LM)
Adverse with findings = 4	2 (DM), 1 (LM)		1 (LM)	
Disclaimed with findings = 25		2 (DM) 11 (LM)	1 (LM) 10 (LM) 1 (DM)	9 (LM)

MET – metropolitan municipality DM – district municipality LM – local municipality
Colour of number indicates audit opinion from which municipality has moved

There has only **been a slight improvement in the overall audit outcomes**. In total, 42 (15%) of the municipalities improved their outcomes – seven district municipalities and 35 local municipalities; 36 (13%) regressed – including two of the metros; and 185 (67%) remained unchanged.

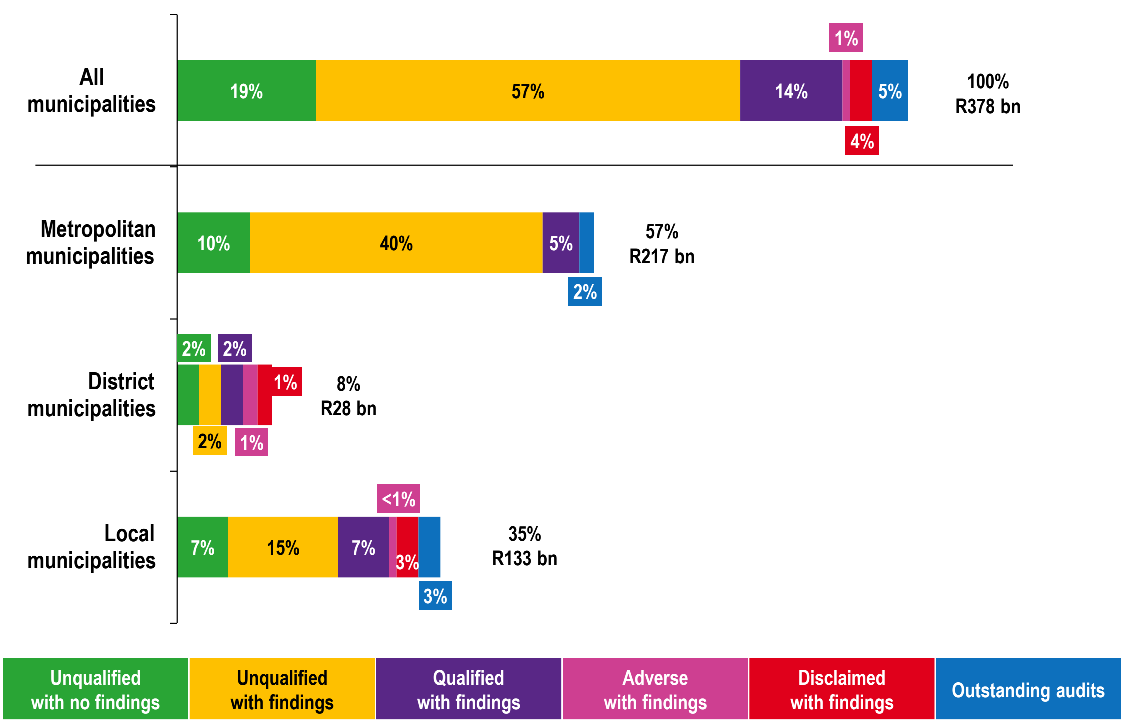
The slow rate of improvement in 2015-16 can be attributed to the lack of improvements in internal controls, the root causes not being addressed as well as the distraction – and in some cases instability – created by the elections that took place in the year. The re-demarcation of municipal boundaries that led to the amalgamation of 39 municipalities also created instability in the affected municipalities, with changes in the administration and some not having functioning councils or officials willing to take responsibility for the outcomes in the audit period. Only 15% of the **municipalities affected by the re-demarcation** showed an improvement in audit outcomes, while 23% regressed, the outcomes of 3% were outstanding, and the outcomes of the remainder (59%) were unchanged (of which three had disclaimed opinions).

In total, 82% (40) of the **municipalities with clean audit opinions** in 2014-15 obtained this outcome again in 2015-16, which is an encouraging sign that improvements at these municipalities are sustainable. Unfortunately, 14 municipalities lost their clean audit status and only nine moved into this category, resulting in an overall decrease in municipalities with clean audit opinions. Metros and district municipalities should be leading by example in the local government sphere, yet only one metro (City of Cape Town) and 14 district municipalities (32% of the total district municipalities) received clean audit opinions.

Overall, 88 (72%) of the 122 municipalities that received an **unqualified audit opinion with findings** in 2015-16 had recorded the same opinion in 2014-15. Only nine of these municipalities could progress to a clean audit this year. Although some progress had been made towards financially unqualified audit opinions (as detailed in section 4.1), municipalities still need to address their material findings on the quality of the performance reports and compliance with legislation.

The **municipal budget** in 2015-16 was R378 billion, of which R310 billion was operating expenditure and R68 billion was capital expenditure. Figure 2 reflects the audit outcomes of the different categories of municipalities versus their budget allocations, rounded to the nearest billion.

Figure 2: Audit outcomes versus budget allocations



As can be seen in figure 2, the 49 municipalities with clean audit opinions represented only 19% of the total local government expenditure budget. However, it is encouraging that 76% of the budget was accounted for in financial statements that fairly presented the finances of the municipalities and could be relied upon by the users thereof. Almost 60% of the local government budget is managed by metros and 49% of citizens reside in metropolitan areas. If the remaining weaknesses in metros can be addressed, it will have a significant impact.

Figures 3 and 4 show the **provincial audit outcomes** of 2014-15 compared to 2015-16 for all auditees (including municipal entities) and for municipalities, respectively. Movement of 5% and less is indicated as follows:

Slight improvement

Slight regression

Figure 3: Provincial audit outcomes in 2015-16 compared to 2014-15 (all auditees)

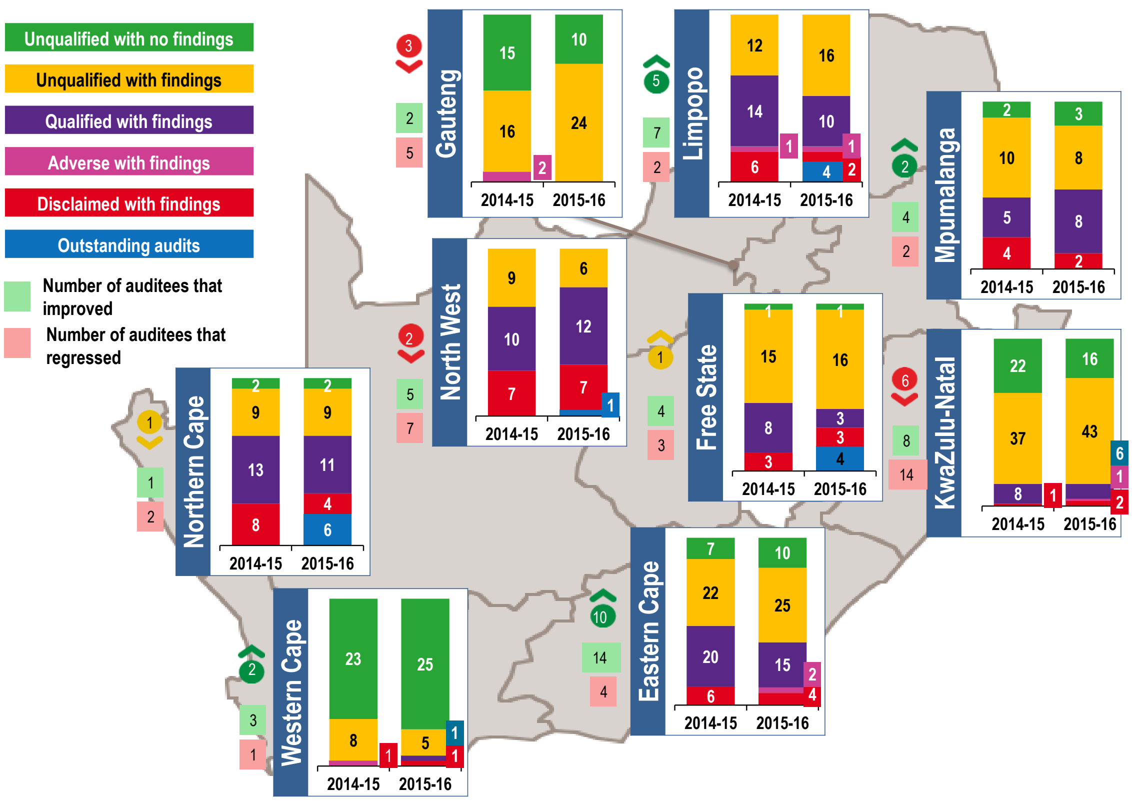
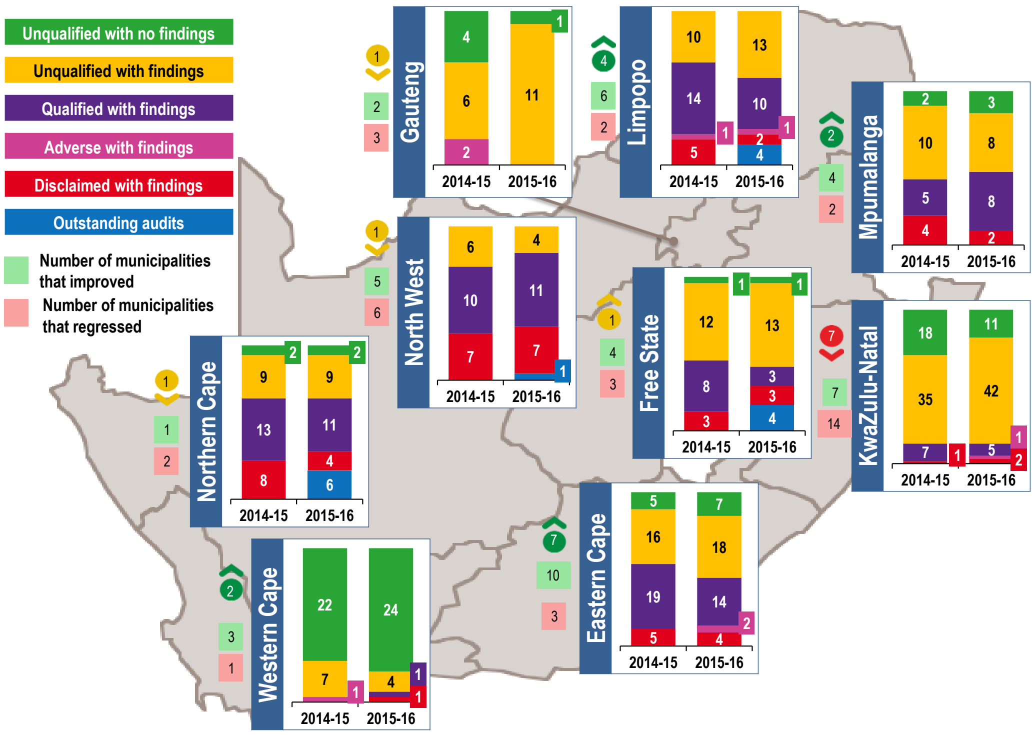


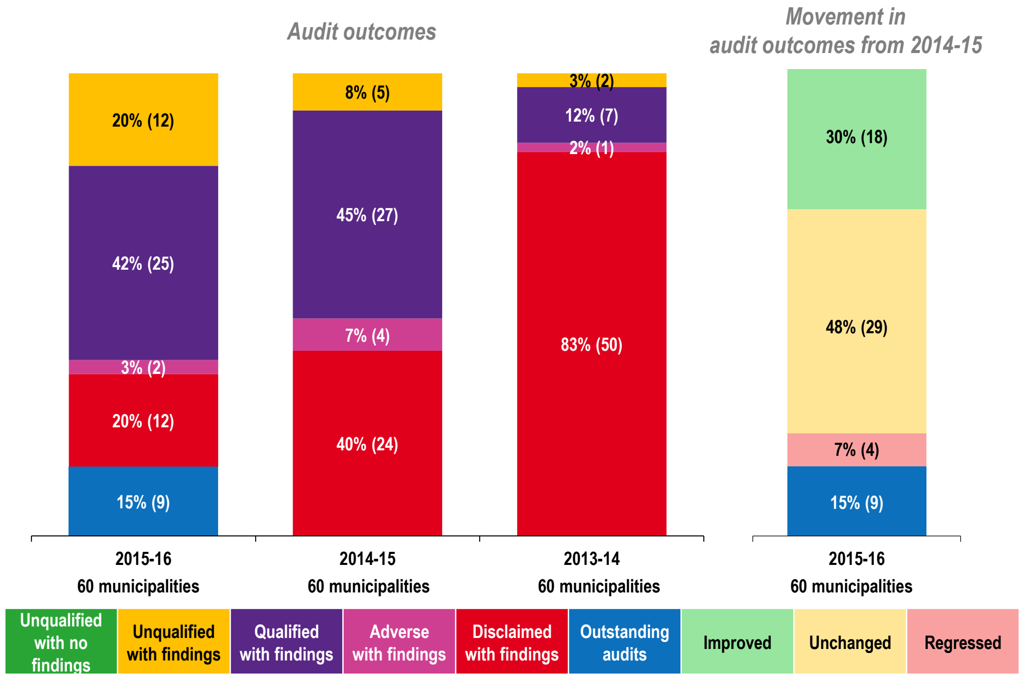
Figure 4: Provincial audit outcomes in 2015-16 compared to 2014-15 (municipalities)



The **audit outcomes of four provinces had improved** since the previous year, with the Eastern Cape showing the greatest improvement. The outcomes of **KwaZulu-Natal regressed significantly** and the remainder of the provinces either slightly improved or slightly regressed. The provinces with the highest number of municipalities with clean audit opinions in 2015-16 were the Western Cape (80%), KwaZulu-Natal (18%) and the Eastern Cape (16%). The provinces with the poorest outcomes (based on the number of municipalities with disclaimed and adverse opinions or outstanding audits) were North West (35%), the Northern Cape (31%) and the Free State (29%). The provincial summaries in section 12 provide detail on the reasons for the movements in audit outcomes in the provinces.

We identified **60 municipalities** in our 2013-14 general report that **required special intervention by national and provincial role players to improve their audit outcomes**. Figure 5 depicts the movement in the audit outcomes of these municipalities.

Figure 5: Movement in audit outcomes of 60 identified municipalities requiring special intervention



As can be seen in figure 5, the audit outcomes of **only 30% of the identified municipalities had improved** since the previous year. However, the number of disclaimed and adverse opinions had decreased significantly since 2013-14 at these municipalities.

In 2015-16, 41 (68%) of the identified municipalities **received assistance from national and provincial role players**. Table 2 shows the extent of support provided and our assessment of whether the assistance is making a difference in the audit outcomes of the municipality (some of the municipalities received support from more than one role player).

Table 2: Support provided and assessment of the impact

Assistance provided by	Municipalities that received assistance	Assistance had no impact	Assistance had limited impact	Assistance contributed to improved audit outcomes
National Treasury and provincial treasuries	40 (67%)	15%	50%	35%
Provincial Cogtas	28 (47%)	21%	58%	21%
Offices of the premier	6 (10%)	17%	66%	17%
Salga	9 (15%)	33%	56%	11%

Despite receiving assistance from more than one role player, Ba-Phalaborwa and Vembe District (both in Limpopo) still regressed to a disclaimed opinion. Five municipalities (Inxuba Yethemba in the Eastern Cape, Mafube in the Free State, Emalahleni in Mpumalanga, and Mamusa and Ventersdorp both in North West) received disclaimed opinions for the past three years in spite of interventions by the provincial treasuries, provincial Cogtas and the National Treasury.

The assistance provided by national and provincial role players is making a difference at some municipalities even if it does not always translate into improved audit outcomes. However, the coordination between the different role players and the quality of the assistance provided need attention in some provinces. Section 8 provides more detail on the levels of support in the different provinces by their treasuries and Cogtas in pursuit of the achievement of the MTSF and implementation of the B2B programme – there we also raise concerns about inadequate support and monitoring by the departments of cooperative governance and the resulting impact on municipalities. Section 12 provides further information at provincial level on the impact of provincial government on municipalities.

Improvements in **audit outcomes** can be achieved if all elements of the **PLAN**+**DO**+**CHECK**+**ACT** cycle are implemented. Section 10 provides recommendations in this regard.

3.2 Outstanding audits

We set the cut-off date for inclusion of the audit outcomes in this report as 15 January 2017. By this date, **15 audits had not been completed** (5% of our total municipal audits), compared to six audits that had been outstanding at the same time last year.

Tables 1 and 2 provide detail on the **reasons for the audits not having been finalised.**

Table 1 lists the four audits that had not been completed by the date of this report and provides the reasons for the late finalisation.

Table 1: Outstanding audits

No.	Province	Municipality	Reason
1	Limpopo	Thabazimbi	No financial statements submitted
2	Northern Cape	Magareng	No financial statements submitted
3		Phokwane	No financial statements submitted
4		Renosterberg	No financial statements submitted

Table 2 includes the **11 audits that were finalised after 15 January** – it provides the reasons for the late finalisation, the outcomes of the audit and the unauthorised, irregular as well as fruitless and wasteful expenditure incurred (the 2014-15 amounts are indicated in *italics*). The practice to submit financial statements late in an attempt to improve or sustain the previous year's audit outcomes should not be encouraged.

Table 2: Audits subsequently finalised

Number	Municipality	Province	Reason for late finalisation of audit	Movement from previous year's audit outcome	2015-16 audit outcomes: Audit opinion	2015-16 audit outcomes: Predetermined objectives	2015-16 audit outcomes: Compliance with legislation	2014-15 audit outcomes: Audit opinion	2014-15 audit outcomes: Predetermined objectives	2014-15 audit outcomes: Compliance with legislation	2015-16 Unauthorised, irregular and fruitless and wasteful expenditure: Unauthorised expenditure Amount R million	Irregular expenditure Amount R million	Fruitless and wasteful expenditure Amount R million
1	Mangaung Metro (consolidated audit)	FS	Late submission of financial statements (14 December 2016) and qualification matters had to be addressed	Unchanged		R	R		R	R	654,7 *(987,1)*	8,3 *(8,1)*	0,7 *(0,21)*
2	Maluti-A-Phofung (consolidated audit)	FS	Late submission of financial statements (6 March 2017)	Improved		R	R		R	R	746,5 *(953,5)*	117,55 *(30,8)*	143,94 *(73,6)*
3	Matjhabeng	FS	Late submission of financial statements (18 October 2016)	Improved		R	R		R	R	812,4 *(443,3)*	305,7 *(226,1)*	150 *(151,8)*
4	Phumelela	FS	Late submission of financial statements (11 October 2016)	Unchanged		R	R		R	R	95,7 *(162,3)*	9,9 *(5,9)*	6 *(3,7)*
5	Greater Giyani	LP	A number of audit issues related to property and equipment and the cash flow statement had to be addressed	Unchanged		A	R		R	R	13 *(0)*	7,3 *(16,8)*	7,6 *(0,03)*
6	Mogalakwena	LP	Late submission of financial statements (2 November 2016)	Improved		R	R		R	R	121 *(45,3)*	487,5 *(175,5)*	0,3 *(0,39)*
7	Mutale	LP	Late submission of financial statements (27 October 2016)	Unchanged		R	R		R	R	0 *(0)*	2,2 *(0,18)*	0,1 *(2)*
8	Dikgatlong	NC	Late submission of financial statements (7 October 2016)	Improved		R	R		R	R	61 *(114,5)*	13,2 *(0)*	3,7 *(1,4)*
9	Gamagara	NC	Outstanding issues on assets resulting from uncertainties of ownership between Gamagara and Tsantsabane had to be addressed	Improved		R	R		R	R	179,2 *(63,3)*	63,5 *(204,6)*	0,6 *(0,005)*
10	Tsantsabane	NC	Late submission of financial statements (27 October 2016)	Improved		R	R		R	R	26 *(6,2)*	4,5 *(3,9)*	4,7 *(1,3)*
11	Rustenburg (consolidated audit)	NW	Delayed commencement of the audit and lack of municipality's capacity to deal with the high volume of audit findings	Regressed		R	R		R	R	427,6 *(13,4)*	759 *(3 061,6)*	0,9 *(0,54)*

Unqualified with findings | **Qualified with findings** | **Adverse with findings** | **Disclaimed with findings** | **Addressed (A)** | **Repeat (R)**

A

Annexure 1 lists all auditees with their current and prior year audit outcomes, while annexure 3 lists the audit outcomes for the past five years. Both annexures indicate which municipalities were identified as requiring special intervention.

4 Status of financial management

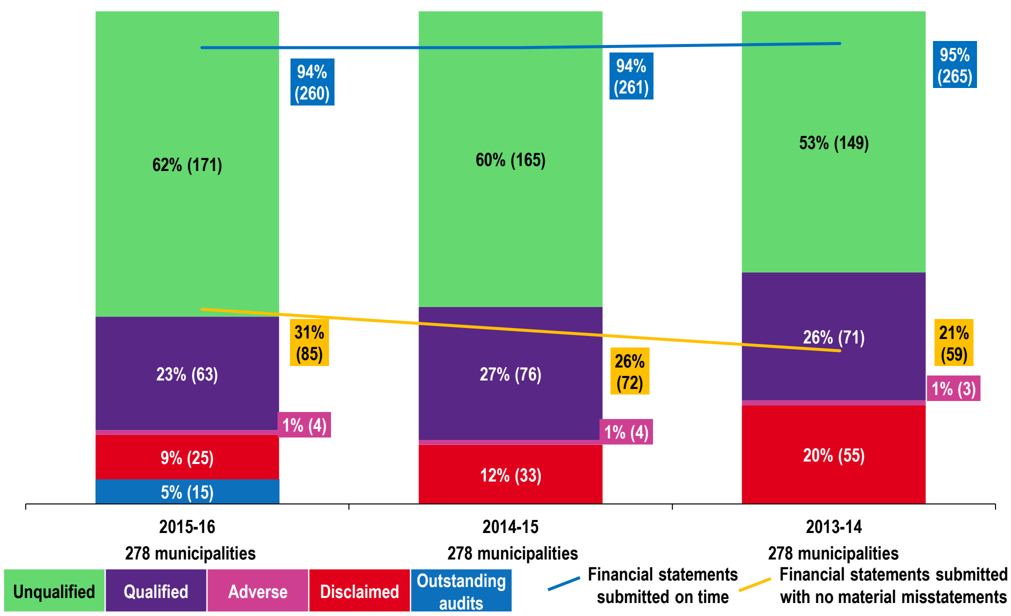
4. Status of financial management

The effect of poor internal controls on financial management is reflected and demonstrated in this section.

4.1 Financial statements

Figure 1 provides a three-year overview of audit opinions on the financial statements, the percentage of municipalities that had submitted their financial statements for auditing by the legislated date (blue line), and the percentage of municipalities that submitted financial statements that were not materially misstated (orange line).

Figure 1: Audit of financial statements



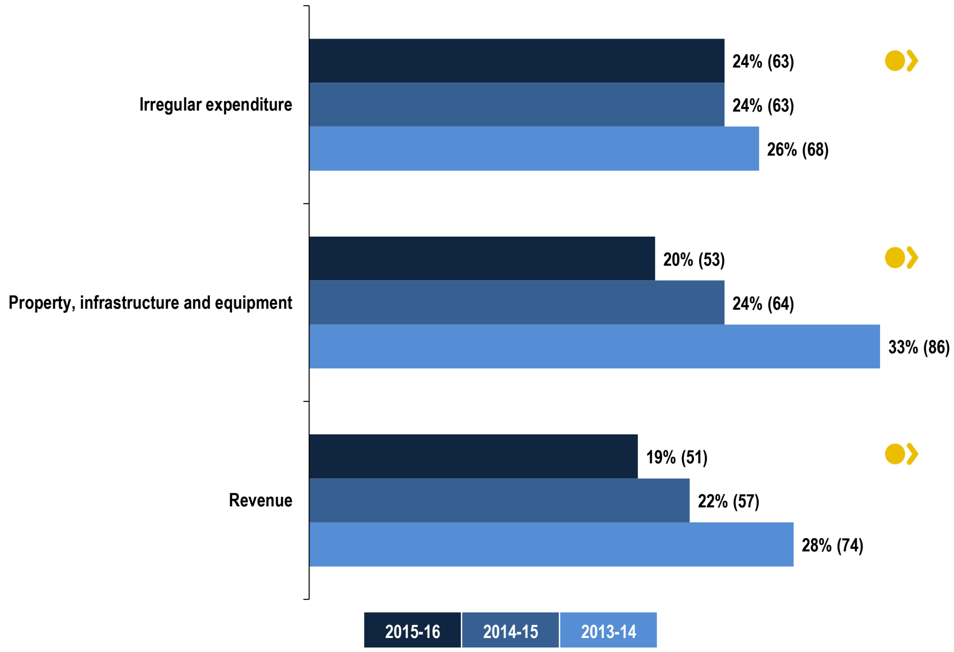
As can be seen in figure 1, 94% of the municipalities had **submitted their financial statements** for auditing by 31 August 2016 (or by 30 September 2016 in the case of consolidated financial statements), as required by legislation. Overall, the submission rate was the same as in the previous year. The rate improved in North West (from 91% to 100%), but regressed in the Free State (from 88% to 75%) due to municipalities submitting financial statements late in an attempt to improve or sustain their previous year's audit outcomes. By the cut-off date for inclusion of the audit outcomes in this report of 15 January 2017, four municipalities had not submitted their financial statements (refer to section 3.2 for more detail).

Figure 1 further shows that the **audit opinions on the financial statements** had slightly improved since the previous year to 62% unqualified opinions. Only 31% of the municipalities were able to provide us with financial statements that contained **no material misstatements** in 2015-16, which is a slight improvement from the 26% in 2014-15. This means that 86 municipalities (31%) received a financially unqualified audit opinion only because they **corrected all the misstatements** we had identified during the audit. A total of 92 municipalities were unable to make the necessary corrections to their financial statements, which resulted in qualified, adverse or disclaimed audit opinions. The main reason for not making such corrections was the unavailability of information, or incomplete information or documentation to determine the correct amounts to be reflected in the financial statements.

The slight increase in financial statements being submitted with no material misstatements was most prominent in the Eastern Cape, the Free State and the Western Cape. Although there has been a marginal increase, the **quality of submitted financial statements remains concerning** and points to a lack of implementation of basic financial disciplines such as regular reviews of financial information during the year, a lack of in-year reporting as well as reliance on auditors and consultants to identify errors in the financial statements.

Figure 2 shows the three most common financial statement qualification areas of the municipalities whose financial statements were qualified, and the progress made in addressing these areas from the previous year.

Figure 2: Three most common financial statement qualification areas



The main reason for municipalities being qualified on **irregular expenditure** was that not all irregular expenditure had been disclosed, or sufficient evidence could not be obtained that all irregular expenditure had been disclosed.

The number of municipalities qualified in this area had remained unchanged since the previous year. Gauteng was the only province with no municipalities being qualified on irregular expenditure. The Free State and the Western Cape had the lowest number and the Eastern Cape, North West and Limpopo the highest number of municipalities that were qualified on irregular expenditure in 2015-16.

The main reason for municipalities being qualified on **property, infrastructure and equipment** was that the value of assets recorded in the financial statements was incorrect, or we could not confirm the value at which these assets had been recorded.

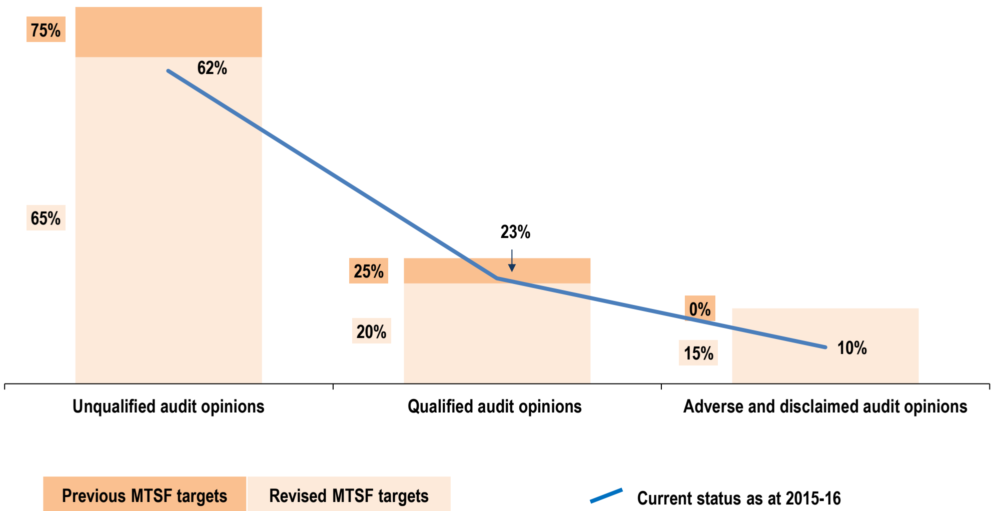
The number of municipalities whose financial statements were qualified on property, infrastructure and equipment had only slightly decreased since the previous year. We noted improvements at municipalities in the Eastern Cape, the Free State, Gauteng and North West. The improvement at some municipalities could be attributed mainly to increased reviews and monitoring of action plans addressing the previous year's qualification areas as well as assistance provided by consultants. Municipalities in the Northern Cape continued to struggle, as the province again had the highest number of municipalities (14) qualified on property, infrastructure and equipment.

The main reason for municipalities being qualified on **revenue** was that they failed to disclose all the revenue earned in their financial statements, disclosed revenue that was not earned, or could not submit sufficient evidence that all the revenue had been disclosed.

The number of municipalities qualified in this area had slightly decreased since the previous year. The qualifications were most common in North West (14 municipalities – an increase from the previous year) and the Northern Cape (11 municipalities). The municipalities in the Eastern Cape, Gauteng and Mpumalanga improved in this area – mainly due to the appointment of consultants to assist in addressing prior year qualifications.

Figure 3 shows the government's previous and revised **MTSF targets** for improving audit outcomes in pursuit of sound financial and administrative management compared to the current audit outcomes. The ministers responsible for finance and for cooperative governance are in charge of the actions and outcomes in this area, while the DCoG's **B2B strategy** contains a further commitment in this regard.

Figure 3: Current audit outcomes positioned against Medium-Term Strategic Framework targets



During 2013-14, chapter 9 of the MTSF included the baselines for audit outcomes (based on the interim audit outcomes during May 2014) and the MTSF targets for 2019 as follows:

1. Baseline set at 50% unqualified audits; 2019 target set at a minimum of at least 75% of municipalities with unqualified audit opinions.
2. Baseline set at 25% qualified audits; 2019 target set at a maximum of 25% municipalities with qualified audit opinions.
3. Baseline set at 20% adverse and disclaimed audit opinions; 2019 target set at no municipalities with adverse and disclaimed audit opinions.

New targets were set in the revised chapter 9 of the MTSF to increase the number of municipalities that have unqualified audit opinions to at least 65%, decrease the number of municipalities that have qualified audit opinions to below 20%, and decrease the number of municipalities that have adverse and disclaimed audit opinions to below 15%. As illustrated in figure 3, these targets are in reach with 62% unqualified audit opinions, 23% qualified audit opinions and 10% adverse and disclaimed audit opinions. However, the instability caused by changes in the administration and the amalgamation of some municipalities as well as the introduction of mSCOA (as further detailed in section 4.5) could still have a negative impact.

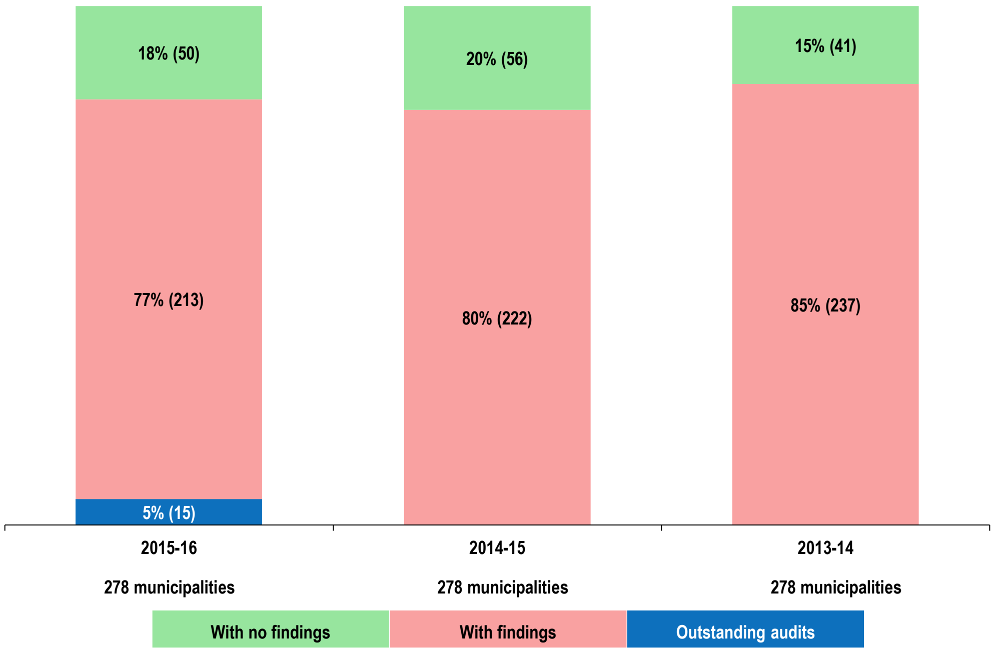
We again raise a **warning signal** that continued reliance on the auditors to identify corrections to be made to the financial statements to obtain an unqualified audit opinion is not a sustainable practice. Over the years, this has placed undue pressure on the audit teams to meet legislated deadlines for the completion of audits, with an accompanying increase in audit fees. The over-reliance on consultants is a further warning signal of a lack of capacity and skills in local government to produce unqualified financial statements. Refer to section 6.2 for further details on the extent of the use of consultants.

A Annexure 1 lists all auditees and the areas qualified.

4.2 Compliance with key legislation

Figure 1 depicts the number of municipalities that had material findings on compliance over the past three years.

Figure 1: Municipalities with findings on compliance with key legislation



For completed audits, the number of municipalities with **material findings had slightly increased** since the previous year from 79% to 81% – the increase was most evident at district municipalities (from 61% to 66%) and metros (from four to six). The compliance outcomes for municipalities in the Eastern Cape, Mpumalanga and the Western Cape slightly improved, but those in Gauteng and KwaZulu-Natal regressed. The reasons for the regressions were the slow response and lack of accountability by senior management to address internal control deficiencies and to implement action plans. In addition, municipalities did not have mechanisms to identify applicable legislation and changes thereto or processes to ensure the monitoring of compliance.

Our audits in 2015-16 did not include an assessment of the financial impact of the non-compliance by municipalities. Based on the nature of the compliance findings, however, we determined that 200 (94%) of the municipalities with material findings on compliance in 2015-16 had **findings with a potential negative financial impact or findings that could cause a financial loss** for the municipality or government. It is the role of municipal management and the council to investigate non-compliance and the impact thereof, which could include financial loss through excessive expenditure (uneconomical use of funds), fruitless and wasteful expenditure, lost revenue, failure to recover debt, and avoidable penalties and interest.

Figure 2 shows the compliance areas with the most material findings in the current year and the progress made in addressing these from the previous year.

Figure 2: Most common areas of non-compliance

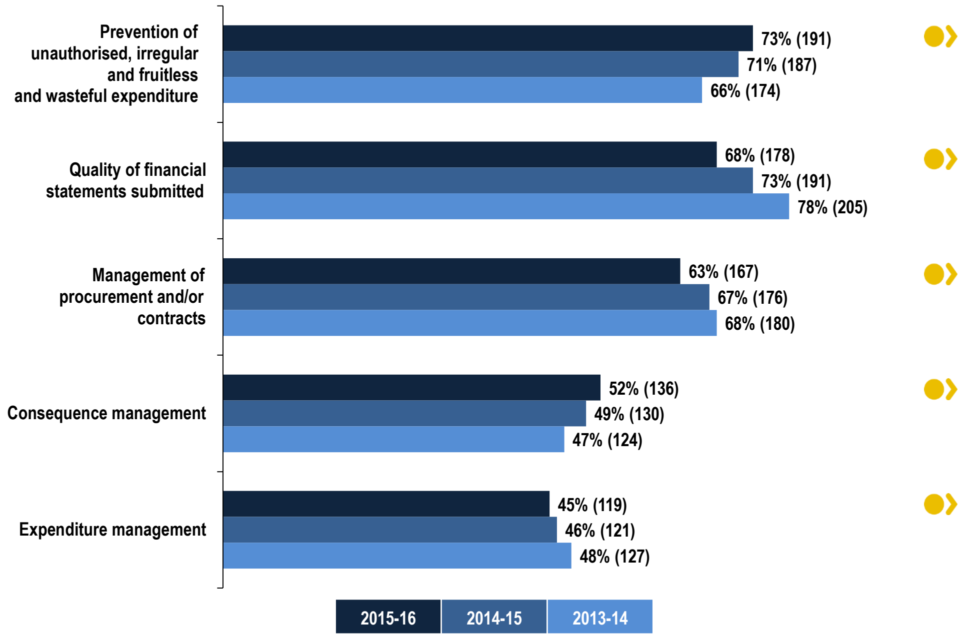


Figure 2 illustrates that over the past three years, the prevention of unauthorised, irregular as well as fruitless and wasteful expenditure, material misstatements in submitted financial statements and the management of procurement and contracts have consistently been the areas in which we raised the most compliance findings.

There had been a slight regression in the **prevention of unauthorised, irregular and fruitless and wasteful expenditure** from the previous year. Sections 4.2.1 to 4.2.3 provide more information on the movements in this area.

We report the poor quality of the financial statements we receive in the audit reports of some auditees as a material finding on compliance, as it also constitutes non-compliance with the Municipal Finance Management Act (MFMA). The finding is only reported if the financial statements we received for auditing included **material misstatements** that could have been prevented or detected if the auditee had an effective internal control system. We do not report a finding if the misstatement resulted from an isolated incident or if it relates to the disclosure of unauthorised, irregular or fruitless and wasteful expenditure identified after the financial statements had been submitted.

Slightly fewer municipalities than in 2014-15 had material findings on compliance with legislation in respect of **procurement and contract management** (also referred to as SCM). Section 4.2.1 provides more information on the findings and movement in this area.

Legislation is clear on the **consequences of non-compliance with legislation** and the steps to be taken to deal with such transgressions. Figure 2 indicates a slight increase in the number of municipalities with non-compliance in this area since 2014-15. The most common finding in 2015-16 was that irregular expenditure was not investigated to determine if any person is liable for the expenditure, which was the case at 117 municipalities. Of these municipalities, 91 (78%) also did not investigate unauthorised as well as fruitless and wasteful expenditure to determine if any person is liable for the expenditure. Section 4.2.4 provides further details on consequence management.

Municipalities continued to struggle with **expenditure management**. The most common finding was that municipalities did not pay creditors within 30 days or an agreed-upon period at 41% of the municipalities, which is a slight improvement compared to the previous year's 44%. We provide more information in section 4.3 on the indicators of financial health of municipalities.

4.2.1 Irregular expenditure caused by weaknesses in supply chain management

Irregular expenditure

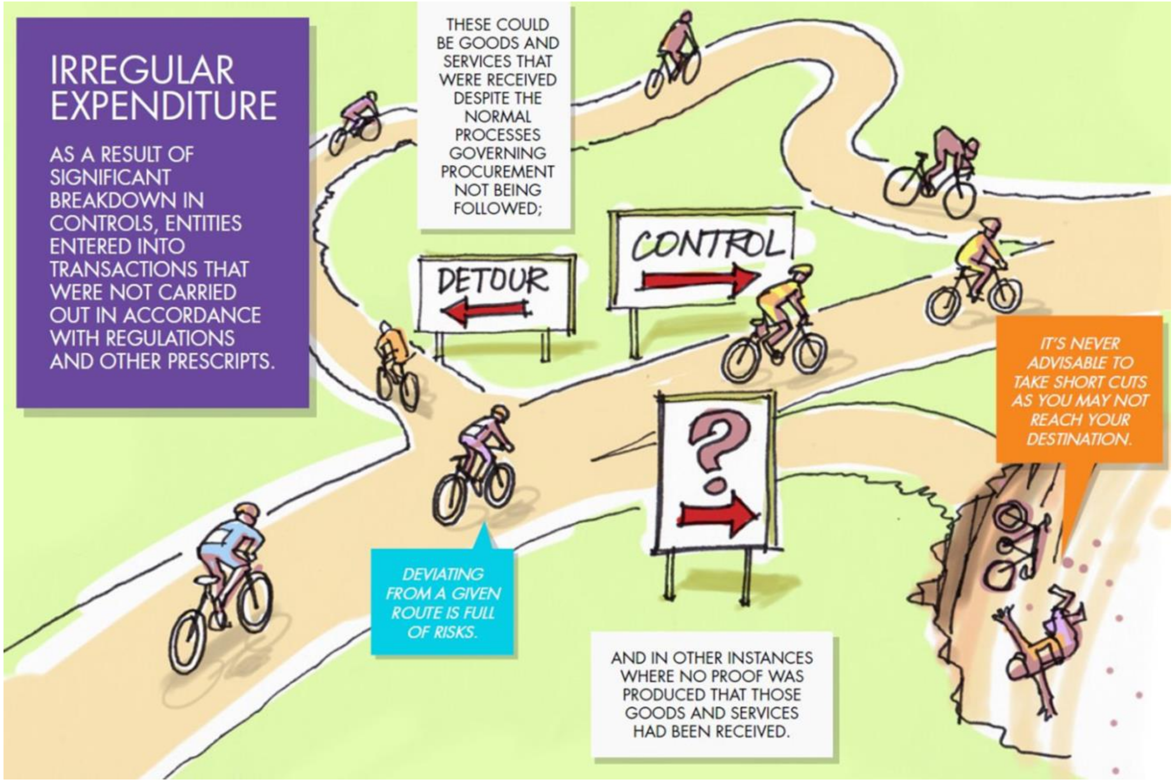
Irregular expenditure is expenditure that was **not incurred in the manner prescribed by legislation**; in other words, somewhere in the process that led to the expenditure, the municipality did not comply with the applicable legislation.

Such expenditure does **not necessarily mean that money had been wasted or that fraud had been committed**. It is an indicator of non-compliance in the process that needs to be investigated by the council to determine whether it was an unintended error, negligence or done with the intention to work against the requirements of legislation. Such legislation requires, for example, that procurement should be fair, equitable, transparent, competitive and cost-effective.

Through council's **investigation**, it is also determined who is responsible for the non-compliance and what its impact was. Based on the investigation, the next steps are determined. One of the steps can be condonement if the non-compliance had no impact and negligence was not proven. Alternatively, if negligence was proven, the steps can be disciplinary action, recovery of any losses from the implicated officials, or even cancelling a contract or reporting it to the police or an investigating authority.

Figure 1 illustrates that irregular expenditure can be as a result of a 'detour', meaning that the transactions were not in accordance with legislation but goods and services were received and there were no losses or fraud. However, such non-compliance can still be an indicator of more serious weaknesses.

Figure 1: Illustration of irregular expenditure

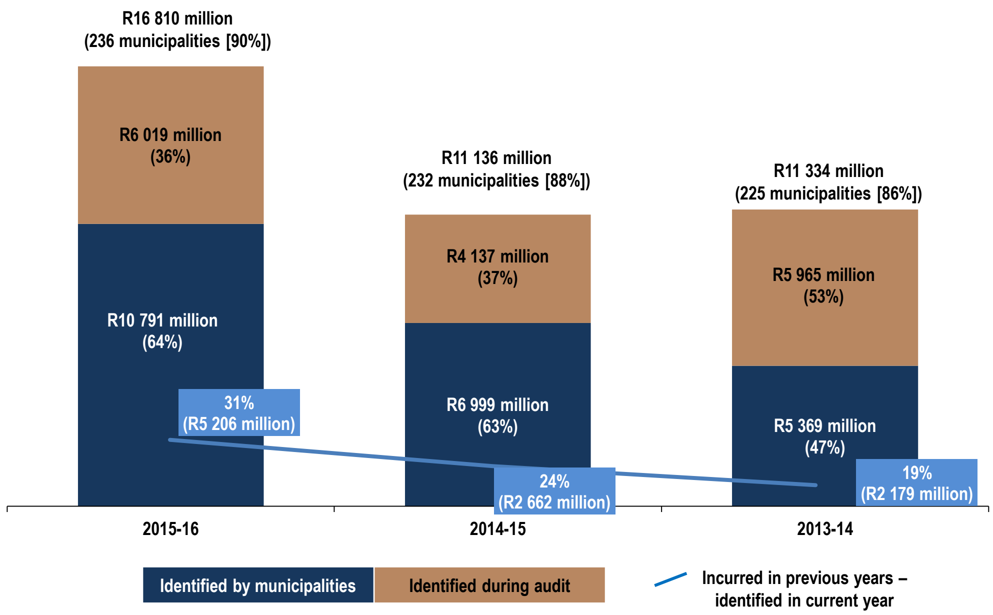


The MFMA is clear that **municipal managers are responsible** for preventing irregular expenditure. It also stipulates the process to be followed when it does occur, as described above.

In order to promote transparency and accountability, municipalities **must disclose all irregular expenditure identified (whether by the municipality or through the audit process)** in their financial statements and detail how it was resolved; in other words, how much was investigated, recovered or condoned.

Figure 2 shows the three-year trend in irregular expenditure based on the amounts disclosed in the financial statements of the municipalities. It also indicates the percentage of irregular expenditure identified by municipalities versus that identified by the audit process as well as the proportion of irregular expenditure disclosed that had been incurred in previous years (blue line).

Figure 2: Three-year trend in irregular expenditure



As can be seen in figure 2, **irregular expenditure had increased by 51%** (R5 675 million) from the previous year – the irregular expenditure in 2015-16 was the highest since we started tracking the values. The number of municipalities incurring such expenditure had increased to 236. A total of 217 (92%) of these 236 municipalities had **also incurred irregular expenditure in the previous year**.

Municipalities in the Eastern Cape, North West, KwaZulu-Natal and Mpumalanga were the **main contributors to the significant increase in irregular expenditure**. These provinces also had the highest amounts of irregular expenditure in 2015-16, as indicated below:

- Eastern Cape – R5 657 million (increased by 60%)
- North West – R2 520 million (increased by 117%)
- KwaZulu-Natal – R2 361 million (increased by 50%)
- Mpumalanga – R2 279 million (increased by 162%)

Figure 2 further shows that 69% of the irregular expenditure was as a result of non-compliance in the current year, but 31% of the irregular expenditure was the result of **acts of non-compliance in previous years**. This is typically due to one of the following scenarios:

1. Payments were made in the current year on a contract that was irregularly awarded in a previous year – if the non-compliance was not investigated and condoned, the payments on these multi-year contracts will continue to be viewed and disclosed as irregular expenditure.
2. Non-compliance in previous years was only identified in the current year and all the related expenditure (even from the previous years) was disclosed in the current year.

If we determine that a municipality did not fully disclose all of its irregular expenditure in the financial statements, the disclosure is qualified if material. To address such a qualification, municipalities typically do a very detailed review of their processes in previous years to identify all the irregular expenditure and correctly disclose it –

as per scenario 1 above. In total, R1 206 million (2014-15: R776 million) of the irregular expenditure as shown in figure 2 was as a result of **municipalities fully recognising their previous years' irregularities to address these qualifications**. It is encouraging that the full disclosure of irregular expenditure is being addressed, as it improves transparency and accountability.

As detailed earlier on in this section, inadequate action taken by municipal managers to **prevent irregular expenditure** was one of the most common material findings on compliance. We reported the findings on compliance as material at 184 municipalities (70%) (2014-15: 177 [67%]), based on the fact that they incurred irregular expenditure in 2015-16 and the previous year, a recurrence of the transgressions that had caused the irregular expenditure, and our assessment that adequate controls and processes would have prevented it.

Figure 2 also shows that we had identified 36% of the irregular expenditure of 2015-16 during the audit process (a slight improvement from the previous year), which means that some municipalities **did not have adequate processes to detect and quantify all irregular expenditure**.

Completeness of irregular expenditure

In 2015-16, 88 municipalities (33%) disclosed in their financial statements that they had incurred irregular expenditure, but the **full amount was not known** as it was still being investigated. In 2014-15, 87 municipalities (33%) had made this disclosure.

A total of 63 municipalities (24%) were qualified on the **completeness of the disclosure** of irregular expenditure in their financial statements, both in 2015-16 and 2014-15.

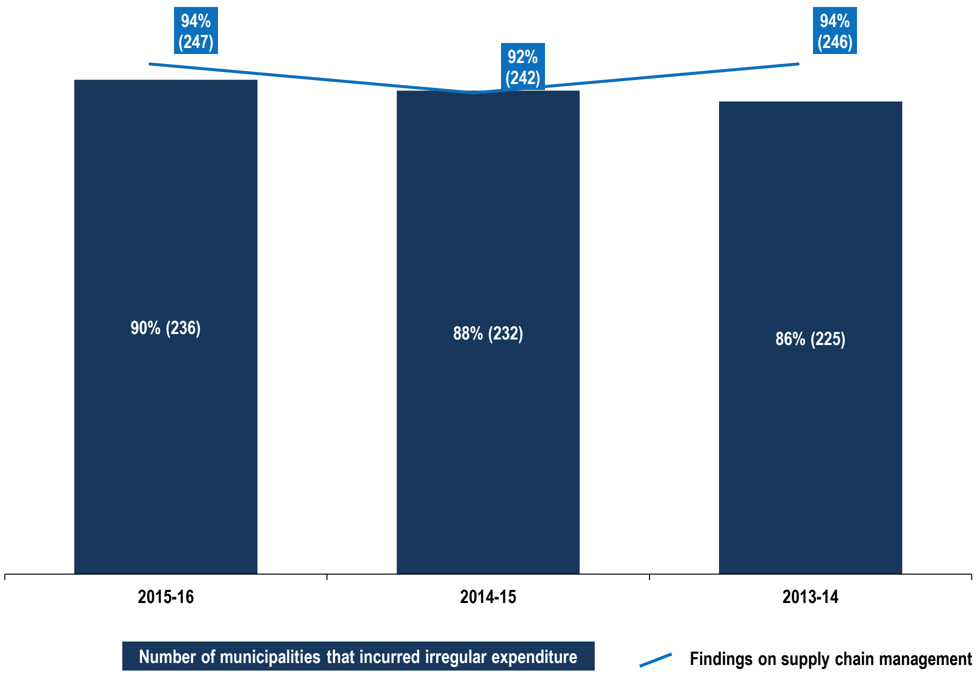
This means that the amount of irregular expenditure for 2015-16 **could have been higher** if the full amounts had been known and disclosed.

What caused these high levels of irregular expenditure?

As part of our audits of SCM in 2015-16, we tested 6 520 contracts (with an approximate value of R53 941 million) and 11 383 quotations (with an approximate value of R670 million), referred to as 'awards' in the rest of this report. Section 13.1 describes the scope of our SCM audits.

Figure 3 shows the number of municipalities where we reported findings on compliance with SCM legislation (whether reported in the audit report or only in the management report) and the number of municipalities that incurred irregular expenditure over three years.

Figure 3: Correlation between irregular expenditure and supply chain management findings



Although not all non-compliance with SCM legislation results in irregular expenditure, figure 3 **highlights the correlation between poor SCM practices and the high occurrence of irregular expenditure** at municipalities. There are slightly more municipalities with SCM findings than irregular expenditure, as – typically – SCM findings such as inadequate measures to monitor the performance of contractors would not result in irregular expenditure.

In total, **R16 523 million (98%) of the irregular expenditure in 2015-16 was as a result of non-compliance with SCM legislation**. The following were the main areas of SCM non-compliance as disclosed by the municipalities in their financial statements, with an indication of the estimated value of the irregular expenditure:

- Procurement without a competitive bidding or quotation process – R6 931 million (42%) (2014-15: 31%, R3 279 million)
- Non-compliance with procurement process requirements – R8 595 million (52%) (2014-15: 62%, R6 661 million)
- Non-compliance with legislation relating to contract management – R997 million (6%) (2014-15: 7%, R784 million).

(We discuss the typical findings in these areas later on in this section.)

The **significant increase** in irregular expenditure from the previous year can be attributed overall to a weakening in SCM at municipalities, in particular in the areas of competitive bidding and obtaining three quotations, as detailed further on in this section. In addition, instability or vacancies in senior management positions, SCM non-compliance resulting from the centralisation or outsourcing of procurement to implementing agents, and inappropriate discretion by management all played a major role in the significant increase in irregular expenditure.

Table 1 shows the municipalities that were the **main contributors (42%) to irregular expenditure in 2015-16**. The corresponding figures for 2014-15 are shown in *italics*.

Table 1: Highest contributors to irregular expenditure

Municipality	Amount (million)	Nature
OR Tambo District (EC)	R1 569 *(2014-15: R94)*	The irregular expenditure related mainly to various awards for water and sanitation projects, e.g. the Flagstaff sewer rectification project and the Tsolo wastewater treatment project. At the Tsolo wastewater treatment project, the irregular expenditure of R74,1 million was due to inappropriate reliance on SCM regulation 32 that allows participation in a contract arranged by another organ of state. The grant portion of irregular expenditure was approximately R39,58 million (3%).
Nelson Mandela Bay Metro (EC)	R1 286 *(2014-15: R1 348)*	The irregular expenditure included two awards for housing developments amounting to R216 million and various awards for sewerage infrastructure projects and water projects, e.g. the Fish Water Flats wastewater contract treatment works project and the tri-annual contract relating to construction. The SCM failures in this regard included awards to suppliers owned or managed by state employees as well as inappropriate deviations from the SCM process. The grant portion of irregular expenditure was approximately R939 million (73%).
Ngaka Modiri Molema District (NW)	R912 *(2014-15: R56)*	Payments were made on multi-year contracts that had previously been identified as irregular. A significant part related to the construction of water and sanitation infrastructure assets funded from the MIG.
Mbombela (MP)	R755 *(2014-15: R107)*	Multiple contracts were extended even though it was not impractical to invite competitive bids. A total of R26 million related to irregular expenditure funded by grants.
City of Tshwane Metro (GP)	R653 *(2014-15: R1 010)*	The expenditure mostly related to a Wi-fi contract (R293 million) where the supplier was appointed without following competitive bidding processes. A BRT tender (R189 million) was also awarded to a contractor not qualified to deliver the service. In total, R517 million (79%) related to irregular expenditure funded by grant money.
Bushbuckridge (MP)	R570 *(2014-15: R72)*	The irregular expenditure was mainly due to various awards that did not comply with SCM legislation, including water and sanitation projects, electrification of villages, provision of accommodation for councillors (e.g. advance rent payments), and road infrastructure (e.g. paving of internal streets – Mkhuhlu phase I(V)(B)). In total, R454 million (80%) related to irregular expenditure funded by grants.
Alfred Nzo District (EC)	R405 *(2014-15: R188)*	The expenditure mostly related to water supply or infrastructure projects, e.g. the Matatiele water supply scheme project amounting to R34,6 million, where the tender was not advertised and the winning bidder did not supply a tax clearance certificate. Approximately 18% (R71,9 million) of the irregular expenditure related to grants.

Municipality	Amount (million)	Nature
Buffalo City Metro (EC)	R370 *(2014-15: R479)*	The irregular expenditure related mostly to the building of the Nompumelelo community hall (R2,5 million) and the upgrading of internal roads (R222,5 million). In neither of these projects, a competitive bidding process had been followed. The estimated value of irregular expenditure where grant money was used, was R160 million (43%).
uThukela District (KZN)	R304 *(2014-15: R324)*	The expenditure was mainly due to non-compliance with SCM legislation on various awards, which included water and sanitation projects, project management services (e.g. Agri Park) as well as the compilation of asset registers and financial statements, which were mostly multi-year contracts. The previous management was dismissed due to fraud and corruption relating to these multi-year contracts.
Mafikeng (NW)	R304 *(2014-15: R35)*	The expenditure was due to various deviations in the procurement process, including issues with tax clearance certificates, BBBEE certificates and the calculation of preference points. The estimated value of irregular expenditure where MIG money was used, was R43 million (14%). This mainly related to projects for the upgrading of roads, including the main roads in Madibe and Mooipan.

These municipalities are among those that had incurred **irregular expenditure for the past three years**. As apparent from table 1, grant money was irregularly spent. We are also concerned about the irregular spending of money relating to water and sanitation projects by six of the top 10 contributors. Section 4.4 details findings relating to key projects funded by conditional grants, while section 5.2 includes findings on water and sanitation projects.

We did not investigate the irregular expenditure, as that is the role of the council. Through our normal audits, however, we confirmed that **goods and services were received** for R12 585 million (76%) of the R16 523 million in irregular expenditure relating to SCM compliance, despite the normal processes governing procurement not having been followed. However, we could not confirm that these goods and services had been procured at the best price and that value was received for the money spent.

Irregular expenditure incurred should be dealt with by the council. We therefore recommend that councils:

- properly investigate all instances of irregular expenditure to determine if any official is liable for the expenditure
- recover the resultant loss if the investigation determined that an official was liable, unless the council certifies it as irrecoverable and disciplinary processes follow
- condone irregular expenditure resulting from the contravention of council policies or by-laws, or request condonation from the National Treasury of contraventions of the MFMA or its regulations – only if the non-compliance had no impact or negligence was not proven
- report all cases of irregular expenditure that constitutes a criminal offence to the South African Police Service.

Supply chain management

We have been auditing and reporting on weaknesses in SCM for a number of years and our messages have been consistent on the need to pay urgent and focused attention to improving the SCM processes.

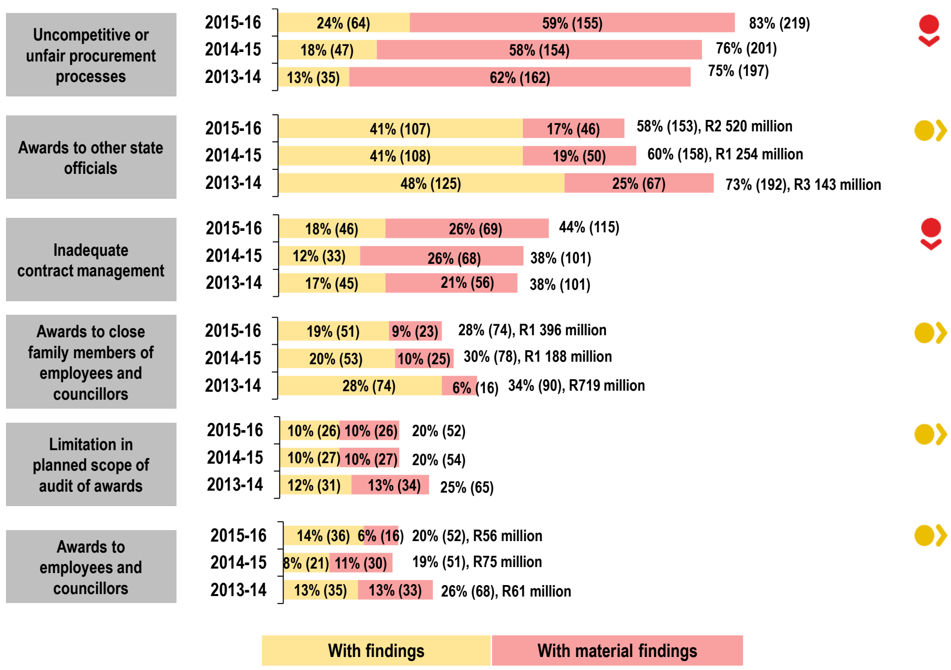
Figure 4 depicts the number of municipalities that had SCM findings and those where we have reported material findings on compliance in the audit report since 2013-14.

Figure 4: Status of supply chain management

Slightly fewer municipalities than in the previous year had no SCM findings. The Free State and KwaZulu-Natal had regressed from the previous year and only Gauteng had improved with regard to municipalities with no SCM findings. Although slightly fewer municipalities than in the previous year had material findings, it remains concerning that over 60% of the municipalities did not comply materially with SCM legislation. Although the SCM findings of 30% of the municipalities were not material enough to be reported in the audit report, the control weaknesses that allowed the non-compliance to occur should be addressed to prevent a regression in audit outcomes in future.

Figure 5 provides a three-year overview of all the SCM areas in which municipalities had findings, the number of municipalities where the findings raised were material enough to be reported in the audit report, as well as the extent of awards made to employees and close family members of employees.

Figure 5: Findings on supply chain management



The level of total SCM findings (material plus non-material findings) had shown little movement in any of the SCM areas since the previous year, except in the areas of **uncompetitive or unfair procurement processes and inadequate contract management**, which had regressed since the previous year. The remainder of this section provides more detail on the nature of the findings and the status of reforms.

Limitation in planned scope of audit

In 2015-16, we were unable to audit awards to the value of R2 765 million at 52 municipalities because the municipalities **could not provide us with evidence that awards had been made in accordance with the requirements of SCM legislation**, as the documentation either did not exist or could not be retrieved as a result of poor document management.

Table 2 lists the extent of limitations in local government over three years.

Table 2: Extent of limitations on planned audits

Province	2015-16		2014-15		2013-14		Movement - 2015-16 from 2014-15
	Number of municipalities	Amount R million	Number of municipalities	Amount R million	Number of municipalities	Amount R million	
Eastern Cape	10	1 410	15	377	19	341	
Free State	5	38	1	0	7	54	
Gauteng	1	307	4	1 250	3	85	
KwaZulu-Natal	7	447	6	183	8	191	
Limpopo	6	234	6	54	5	66	
Mpumalanga	4	40	9	653	5	186	
Northern Cape	5	5	4	13	6	31	
North West	13	284	8	299	10	440	
Western Cape	1	0	1	11	2	21	
Total	52	2 765	54	2 840	65	1 415	

While the number of municipalities where limitations were experienced in 2015-16 had decreased only slightly from the previous year, there was a more visible improvement in Gauteng, Mpumalanga and the Eastern Cape. The value of these limitations varied over the three years, as it depends on the value of the relevant contracts awarded in the year.

These limitations had the following impact:

- The procurement processes could not be audited by us, the internal auditors or investigators.
- There was no evidence that municipalities had followed a fair, transparent and competitive process for all awards. Should unsuccessful bidders request information on the process, also for possible litigation purposes, it would not be available.
- We could not determine whether these awards were irregular and, as a result, could not determine the true extent of irregular expenditure.
- Our general report, audit reports and management reports did not reflect the true extent of non-compliance with SCM, irregularities and possible fraud.
- Poor record management created an environment in which it was easy to commit and conceal improper or illegal conduct.

Awards to employees, councillors, close family members and other state officials

There had also been little movement in the number of municipalities with awards to **suppliers in which employees or their close family members had an interest** or awards to **suppliers in which other state officials had an interest**.

SCM regulation 44 prohibits the awarding of contracts and quotations to persons (employees, councillors or other state officials), or entities owned or managed by them, if they are in the service of the municipality or if they are in the service of any other state institution. Such expenditure is also considered irregular.

Suppliers owned or managed by employees of any other state institution made false declarations in awards of R1 964 million at 110 municipalities (e.g. suppliers owned by employees at a government department made a false declaration when applying for the tender at a municipality). Suppliers owned by family members of employees of the municipality also made false declarations in awards of R454 million at 29 municipalities.

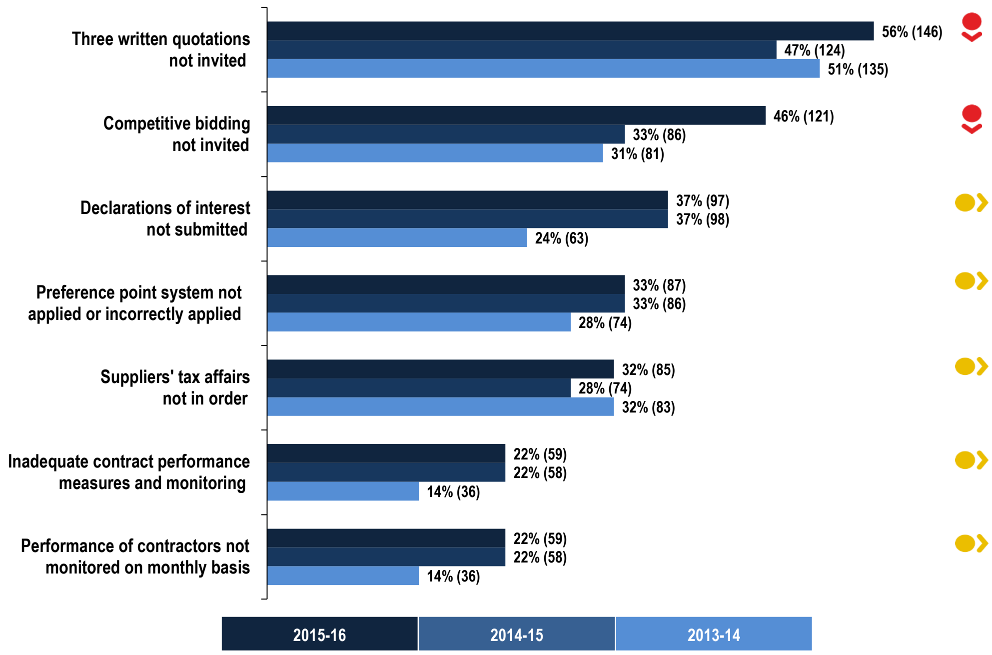
At 24 municipalities, employees failed to declare their own interest in awards of R23 million either as part of the procurement processes or through annual declarations. At 46 municipalities, employees failed to declare their family members' interest in awards of R806 million.

The possibility of undue influence cannot be discounted, especially if the person, including SCM officials, could have influenced the procurement processes for these awards, which could have created opportunities for irregularities. We again point out that a **failure by suppliers to declare the interest of employees and other state officials constitutes a fraudulent act**, which should be investigated and dealt with in accordance with legislation. Section 4.2.4 provides more information on how municipalities have dealt with this in the last three years.

Procurement processes and contract management

Figure 6 provides a three-year overview of the most common findings on procurement processes and contract management – all of which can have a potential negative financial impact. All, except the findings on inadequate performance measures and monthly monitoring of contractors, lead to irregular expenditure.

Figure 6: Most common findings on procurement processes and contract management



The most common findings for the past three years relate to **deviations from the prescribed procurement processes**. Three written quotations or competitive bids were not invited to enable the selection of a supplier based on a competitive and fair process. Although such deviations are allowed, we found that it had often not been approved; or, if approved, the deviation was not reasonable or justified.

The regression in this regard is concerning and points to a breakdown in controls, mainly caused by inappropriate management discretion (e.g. deviating from following a competitive bidding process without justifiable reason) and poor planning. In some instances, municipalities also tended to appoint service providers they knew or had used in the past by deviating from the competitive bidding process. The Preferential Procurement Regulations make provision for the promotion of local production and content. These regulations are aimed at supporting socio-economic transformation. In 2015-16, we audited whether procurement at 223 municipalities took place in accordance with legislative requirements **to procure certain commodities from local producers**. We identified non-compliance in this regard on awards amounting to R421 million at 39 (17%) of these municipalities. The provinces where we raised the most of these findings were Mpumalanga (eight municipalities), Limpopo (six municipalities) and the Eastern Cape (six municipalities). We will continue to increase our audit focus on this important government initiative.

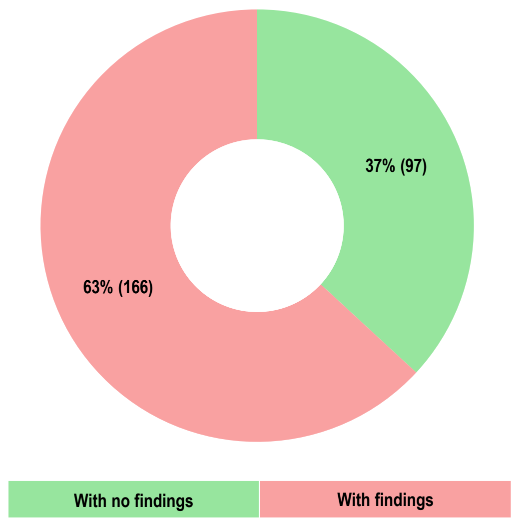
Readiness for supply chain management reforms

The National Treasury, through the Office of the Chief Procurement Officer, is accelerating reforms that will make it easy for business and government to transact and to ensure that government purchases what it needs at the right time, at the right price, in the correct quantities and delivered to the right location. These reforms include establishing the **central supplier database** of government and the **eTender portal** to be used by all organs of state.

As part of our audits, we assessed the readiness of municipalities to implement these SCM reforms. Our focus was on the use of the central supplier database and the eTender portal, which was compulsory from 1 July 2016.

Figure 7 shows the state of readiness of municipalities regarding the implementation of the SCM reforms.

Figure 7: Readiness of municipalities for supply chain management reforms



The following were the most common findings with regard to SCM reforms:

- The SCM policy at 143 municipalities (54%) was not updated to invite competitive bids through the eTender portal.
- The SCM policy at 138 municipalities (52%) was not updated to invite quotations from suppliers registered on the central supplier database.
- A total of 138 municipalities (52%) had not started inviting bids through the eTender portal as at the 2015-16 year-end.
- A total of 117 municipalities (44%) still used their own database of prospective suppliers, which was not synchronised with the central supplier database.

The SCM weaknesses require immediate and focused action to ensure that the principles of fairness, transparency, completeness, equity and cost-effectiveness in procurement processes are consistently applied, and to address the very high amounts of irregular expenditure incurred annually. As the SCM reforms were introduced to address many of the SCM weaknesses in local government, it is critical that these reforms are implemented by municipalities and monitored at provincial and national level.

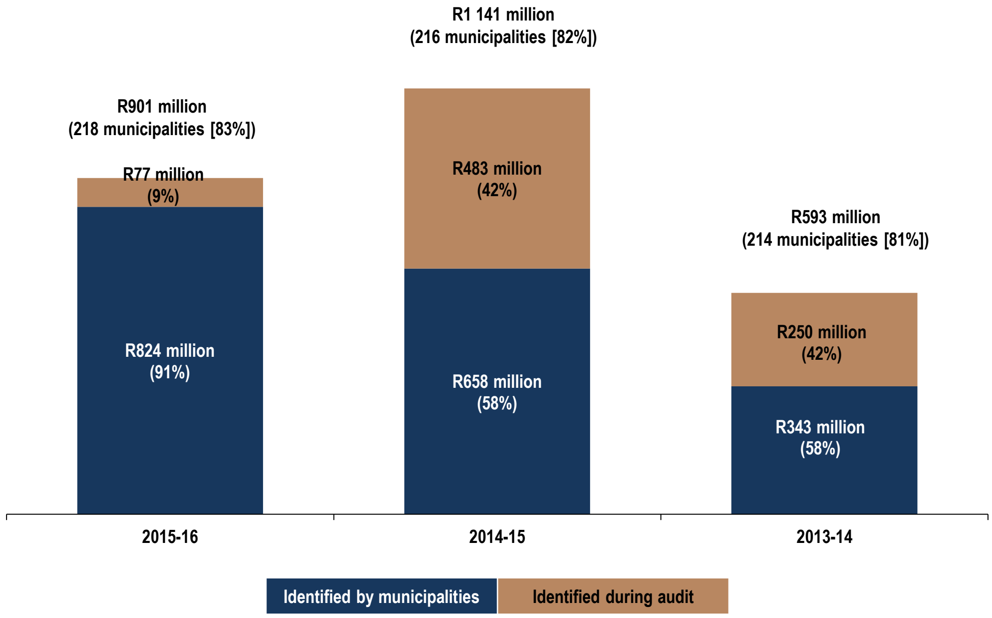
A Annexure 1 shows the auditees with irregular expenditure, while annexure 2 lists those with findings on SCM.

4.2.2 Fruitless and wasteful expenditure

Fruitless and wasteful expenditure refers to expenditure that was made in vain and could have been avoided had reasonable care been taken. Such expenditure includes interest, the payment of inflated prices, and the cost of litigation that could have been avoided.

Figure 1 depicts the extent of fruitless and wasteful expenditure over the past three years and the proportion thereof that was identified during the audit and not by the municipality.

Figure 1: Three-year trend in fruitless and wasteful expenditure



As shown in figure 1, the **amount of fruitless and wasteful expenditure** had decreased by 21% since the previous year, while the number of municipalities that incurred this type of expenditure had slightly increased.

A total of 201 municipalities (92%) incurred fruitless and wasteful expenditure in both the current and the previous year, of which 136 had incurred such expenditure for the past five years.

The amount of fruitless and wasteful expenditure incurred by municipalities in the Eastern Cape, Limpopo and North West had decreased from the previous year, while the amount incurred by municipalities in KwaZulu-Natal (61%), the Northern Cape (59%) and the Western Cape (145%) had increased by more than 50% in each of these provinces.

The general **nature of the fruitless and wasteful expenditure** related to the following:

- Interest and penalties on overdue accounts and late payments – R814 million (90%) (2014-15: R638 million [56%]). The poor financial health of municipalities as further described in section 4.3 was the main contributor in this regard.
- Litigation and claims – R23 million (3%) (2014-15: R55 million [5%]).
- Other (e.g. cancellation fees for accommodation and unsuccessful implementation of software) – R64 million (7%) (2014-15: R448 million [39%]).

Of the R901 million incurred in 2015-16, only R7 million (1%) was incurred by municipalities to **avoid further fruitless and wasteful expenditure** or losses that often relate to the cost of cancelling irregular contracts or the contracts of non-performers.

The following municipalities were the **main contributors** (51%) to fruitless and wasteful expenditure in 2015-16. The corresponding figures for 2014-15 are shown in *italics*.

Table 1: Highest contributors to fruitless and wasteful expenditure

Municipality	Amount (million)	Nature
Ngwathe (FS)	R74 *(2014-15: R51)*	Payment of interest and penalties on overdue accounts and late payments.
Emalahleni (MP)	R74 *(2014-15: R95)*	In total, 99,6% of the expenditure related to interest and penalties, while the remainder related to Land Scheme Management Act expenditure.
Nelson Mandela Bay Metro (EC)	R58 *(2014-15: R423)*	A total of 47% of the expenditure related to interest and penalties, while approximately 46% related to civil claims from vehicle accidents as well as expenditure with regard to flights, accommodation and recruitment service providers.
Msukaligwa (MP)	R47 *(2014-15: R13)*	Payment of interest and penalties on overdue accounts and late payments.
Thaba Chweu (MP)	R44 *(2014-15: R36)*	Payment of interest and penalties on overdue accounts and late payments.
Nala (FS)	R39 *(2014-15: R26)*	A total of 59% of the expenditure related to interest and penalties, while approximately 41% related to completed infrastructure assets that were no longer usable.
Kouga (EC)	R35 *(2014-15: R2)*	Payment of interest and penalties on overdue accounts and late payments.
Naledi (NW)	R30 *(2014-15: R18)*	Payment of interest and penalties on overdue accounts and late payments.
Govan Mbeki (EC)	R29 *(2014-15: R28)*	Payment of interest and penalties on overdue accounts and late payments.
Lekwa (MP)	R27 *(2014-15: R25)*	Payment of interest and penalties on overdue accounts and late payments.

These municipalities are among those that had incurred fruitless and wasteful expenditure for the past three years, with Ngwathe, Nelson Mandela Bay Metro, Thaba Chweu, Nala, Kouga, Govan Mbeki and Lekwa doing so for the past five years.

As detailed earlier on in this section, **inadequate action taken** by municipal managers to prevent fruitless and wasteful expenditure was one of the most common material findings on compliance. We reported the findings on compliance as material at 144 municipalities (55%) (2014-15: 138 [52%]) based on the fact that they incurred fruitless and wasteful expenditure in the year under review as well as in previous years, a recurrence of the action that had caused the fruitless and wasteful expenditure, and our assessment that adequate controls and processes would have prevented it.

Figure 1 further illustrates that we had identified only 9% of the fruitless and wasteful expenditure amount during the audit process, which means that most municipalities had adequate processes to detect and quantify all fruitless and wasteful expenditure, as required by legislation. This is an improvement from the previous year.

Fruitless and wasteful expenditure incurred should be dealt with by the council. We therefore recommend that councils:

- properly investigate all instances of fruitless and wasteful expenditure to determine if any official is liable for the expenditure
- recover the resultant loss if the investigation determined that an official was liable, unless the council certifies it as irrecoverable and disciplinary processes follow.

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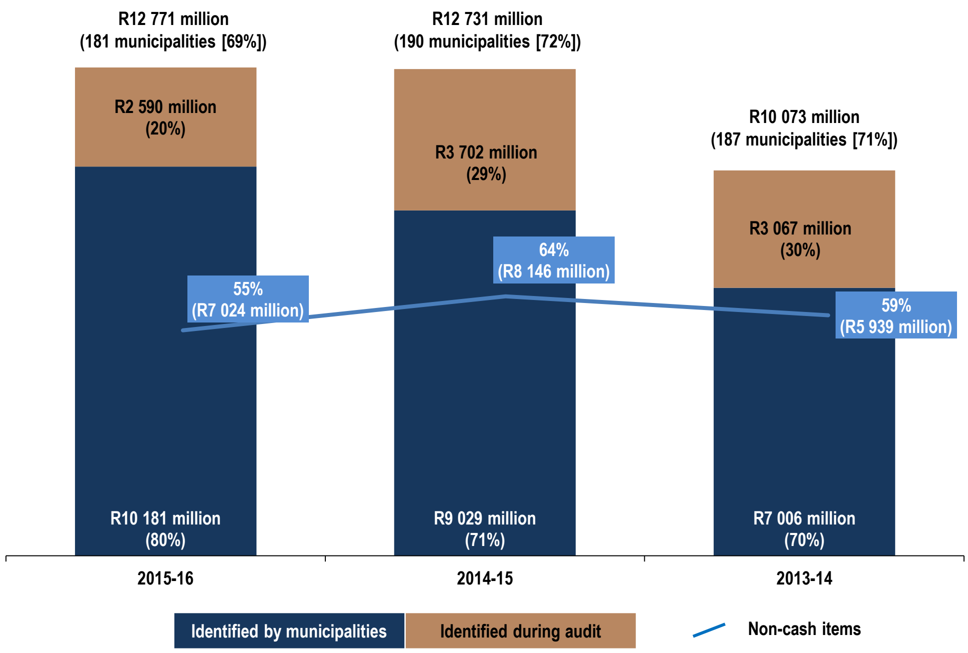
Annexure 1 shows the auditees with fruitless and wasteful expenditure.

4.2.3 Unauthorised expenditure

Unauthorised expenditure refers to expenditure incurred by municipalities outside the budget approved by the council or not in accordance with the conditions of a grant.

Figure 1 depicts the extent of unauthorised expenditure over the past three years and the proportion thereof that was identified during the audit and not by the municipality. It further reflects the percentage of unauthorised expenditure that relates to non-cash items for the three-year period.

Figure 1: Three-year trend in unauthorised expenditure



As reflected in figure 1, the **amount of unauthorised expenditure** had remained at almost the same level as in the previous year. Despite the increase of less than 1% in the amount of total unauthorised expenditure incurred since the previous year, there was a significant increase in the amount of unauthorised expenditure incurred by municipalities in KwaZulu-Natal (43%), Gauteng (40%) and the Northern Cape (22%), which is concerning. At an overall level, this was offset by a significant decrease in the amount of unauthorised expenditure incurred by municipalities in the Western Cape (65%), the Eastern Cape (41%) and North West (30%).

A total of 158 (87%) of the 181 municipalities had also incurred unauthorised expenditure in the previous year.

Overspending of the budget or main sections within the budget was the reason for 99% (2014-15: 97%) of the unauthorised expenditure. Poorly prepared budgets, inadequate budget control and a lack of monitoring and oversight were some of the reasons for the overspending.

Municipal budgets also make provision for items that do not involve actual cash inflow or outflow. We term these **non-cash items**, which include accounting entries such as reducing the value at which assets are reflected in the financial statements (asset impairments) and providing for other types of potential financial losses. This is not actual expenditure but rather an accounting requirement that enables municipalities to assess the true value of their assets (such as equipment or debtors). It is important for municipalities to correctly budget for these non-cash items to build up reserves for the replacement of assets and to show the true financial state of the municipality.

As shown in figure 1, 55% of the overspending that had caused the unauthorised expenditure did not represent actual payments in excess of the budget, but rather these estimates that had been incorrectly budgeted for. This is a decrease when compared to the previous year. It is of concern that the budgets of some of these municipalities might have been manipulated to show a surplus by incorrectly showing the true extent of the non-cash items in the budget. At year-end these amounts are audited and are thus shown at the correct value, which then results in unauthorised expenditure.

Thirty-one municipalities (17%) incurred unauthorised expenditure of R939 million (7%) only because of such non-cash items.

The following municipalities were the **main contributors** (51%) to unauthorised expenditure in 2015-16. The corresponding figures for 2014-15 are shown in *italics*.

Table 1: Highest contributors to unauthorised expenditure

Municipality	Amount (million)	Nature
City of Tshwane Metro (GP)	R1 914 *(2014-15: R786)*	Overspending of the budget / main sections within the budget – 43% of which related to non-cash items. The expenditure can mainly be attributed to employee-related cost, debt impairment, depreciation, finance charges, bulk purchases, contracted services, transfers and grants, and losses on the disposal of property, plant and equipment.
Emalahleni (MP)	R831 *(2014-15: R233)*	A total of 98% related to overspending of the budget / main sections within the budget – 91% of which related to non-cash items. In total, R14 million of the R75 million relating to cash items was as a result of unspent grants that were not cash-backed.
Madibeng (NW)	R796 *(2014-15: R1 258)*	Overspending of the budget / main sections within the budget – 74% of which related to non-cash items. The expenditure can be attributed to depreciation, impairment, finance costs, general expenses, expenses related to contracted services, repairs and maintenance.
City of Johannesburg Metro (GP)	R693 *(2014-15: R959)*	Overspending of the budget / main sections within the budget – 68% of which related to non-cash items. Apart from non-cash items such as depreciation, the overspending can mainly be attributed to transportation-related expenses, health-related expenses, emergency services expenditure, and expenses related to group finance.
Newcastle (KZN)	R674 *(2014-15: R0)*	Overspending of the budget / main sections within the budget – 87% of which related to non-cash items. The municipality incurred unauthorised expenditure mainly as a result of bad debts written off and the revaluation of assets. The impact of this could not be accurately estimated during the preparation of the adjustment budget.
Emfuleni (GP)	R461 *(2014-15: R453)*	Overspending of the budget / main sections within the budget – 53% of which related to non-cash items. The overexpenditure can mainly be attributed to debt impairment, depreciation, personnel costs, finance costs, and general expenditure.
Vhembe District (LP)	R302 *(2014-15: R258)*	Overspending of the budget / main sections within the budget – 74% of which related to cash items (mostly repairs and maintenance) – and 26% of which related to non-cash items, such as debt impairment, depreciation and/or amortisation.

Municipality	Amount (million)	Nature
Polokwane (LP)	R287 *(2014-15: R232)*	Overspending of the budget / main sections within the budget – 100% of which related to non-cash items, such as debt impairment and fair value adjustments.
Westonaria (GP)	R269 *(2014-15: R279)*	Overspending of the budget / main sections within the budget – 91% of which related to non-cash items. This overspending can mainly be attributed to debt impairment of property rates by mines due to their objection and council not budgeting for this expenditure.
Ngaka Modiri Molema District (NW)	R252 *(2014-15: R407)*	Overspending of the budget / main sections within the budget– none of which related to non-cash items. The expenditure can be attributed to finance costs, expenses related to contracted services, general expenses as well as transfers and subsidies.

These municipalities (except for the City of Johannesburg Metro, Newcastle and Emfuleni) are among those that had incurred such expenditure for the past three years. The City of Johannesburg Metro and Emfuleni had incurred such expenditure in the past two years, while Newcastle incurred such expenditure only in the current year. The City of Tshwane Metro, Polokwane and Ngaka Modiri Molema District had incurred unauthorised expenditure for the past five years.

As detailed earlier on in this section, inadequate steps taken by municipal managers to prevent unauthorised expenditure constituted one of the most common material findings on compliance. We reported the findings on compliance as material at 145 municipalities (55%) (2014-15: 148 [56%]) based on the fact that they had incurred the same type of unauthorised expenditure in the current and previous years as well as our assessment that adequate controls and processes would have prevented it.

Figure 1 also shows that we had identified 20% of the unauthorised expenditure amount during the audit process, which means that some municipalities did not have adequate processes to detect and quantify all unauthorised expenditure. This is, however, an improvement from the previous year.

Unauthorised expenditure incurred should be dealt with by the council. We therefore recommend that councils:

- properly investigate all instances of unauthorised expenditure to determine if any official is liable for the expenditure
- recover the resultant loss if the investigation determined that an official was liable, unless the council certifies it as irrecoverable and disciplinary processes follow
- authorise it through an adjustment budget.

A

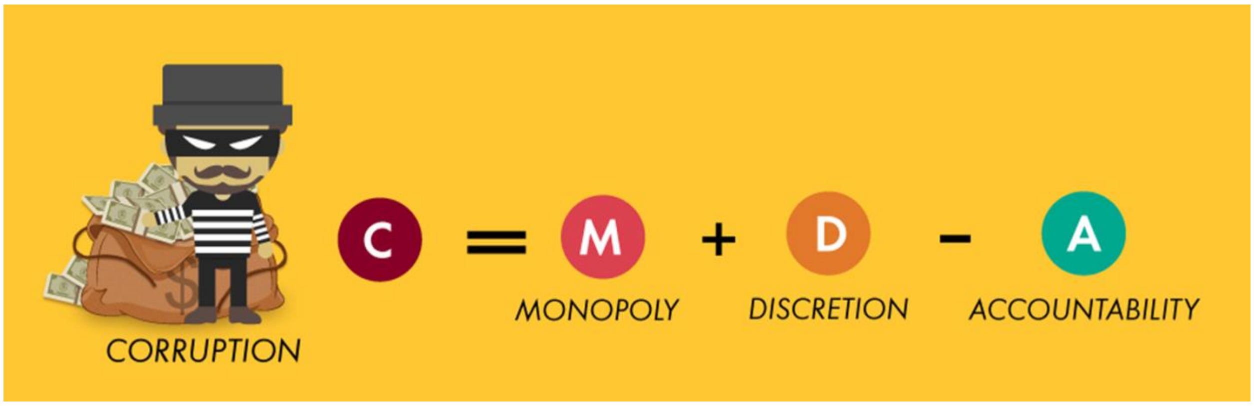
Annexure 1 shows the auditees with unauthorised expenditure.

4.2.4 Fraud and consequence management

The MFMA and its regulations clearly stipulate that management should investigate 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 and possible fraud. Appropriate actions should be taken based on the outcomes of these investigations.

Municipalities with **poor consequence management** practices are often prone to corruption or fraud, as a result of municipal officials not being held accountable. Figure 1 below demonstrates the need for strong accountability based on a formula on corruption developed by Robert Klitgaard.

Figure 1: Corruption formula



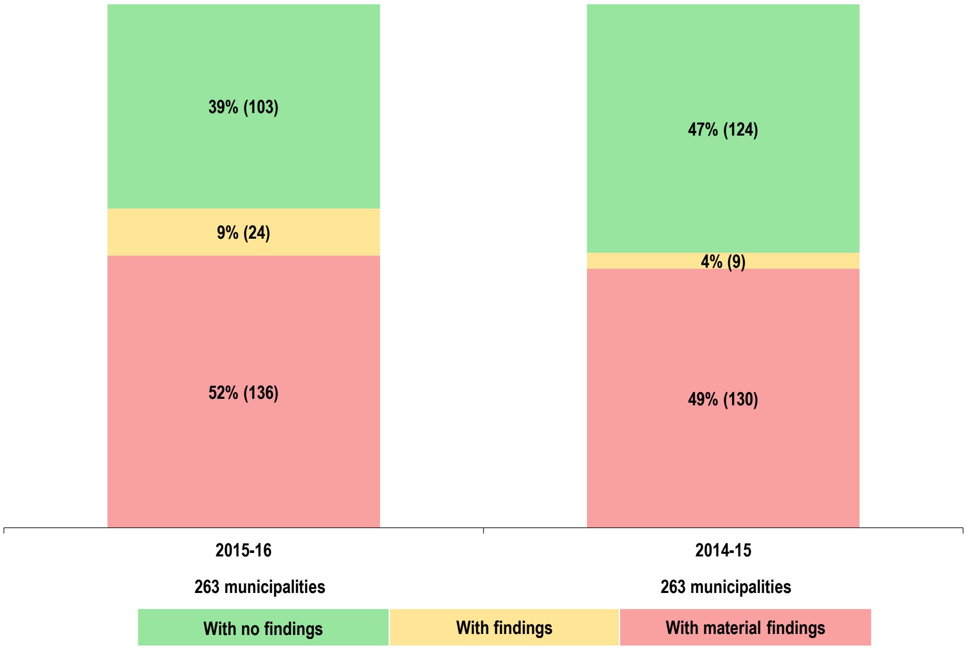
Corruption arises when officials are given sole power (**monopoly**) to make consequential decisions (**discretion**) without adequate oversight or control (**accountability**). In local government, municipalities are tasked with the responsibility of providing a number of services that cannot be provided by any other service provider, such as water and sanitation. When making financial decisions, municipalities have a certain degree of discretion. In some cases, they decided to deviate from procurement processes as a result of, for example, bad planning. Should the accountability culture in a municipality not be strong, these actions can create an environment that is conducive to corruption.

This section provides our observations and findings on how municipalities managed allegations of misconduct and fraud, and how they dealt with unauthorised, irregular as well as fruitless and wasteful expenditure.

Non-compliance with legislation on consequence management

Figure 2 shows the extent of non-compliance with legislation in respect of consequence management – 'with material findings' means that the non-compliance was so significant that we reported it in the audit reports of those municipalities, while 'with findings' means that there was non-compliance but to a lesser degree.

Figure 2: Status of consequence management



The **level of compliance with legislation on consequence management had regressed** since the previous year, mostly as a result of regressions in Mpumalanga (33%), Gauteng (25%) and KwaZulu-Natal (16%). The provinces with the highest number of municipalities with non-compliance findings in 2015-16 were the Eastern Cape (32), KwaZulu-Natal (28), North West (22) and Limpopo (19). The most common findings were the following:

- Fruitless and wasteful expenditure identified in the prior year was not investigated at 122 municipalities.
- Irregular expenditure identified in the prior year was not investigated at 120 municipalities.
- Unauthorised expenditure identified in the prior year was not investigated at 104 municipalities.

The remainder of this section provides more insights into the non-compliance and overall consequence management practices.

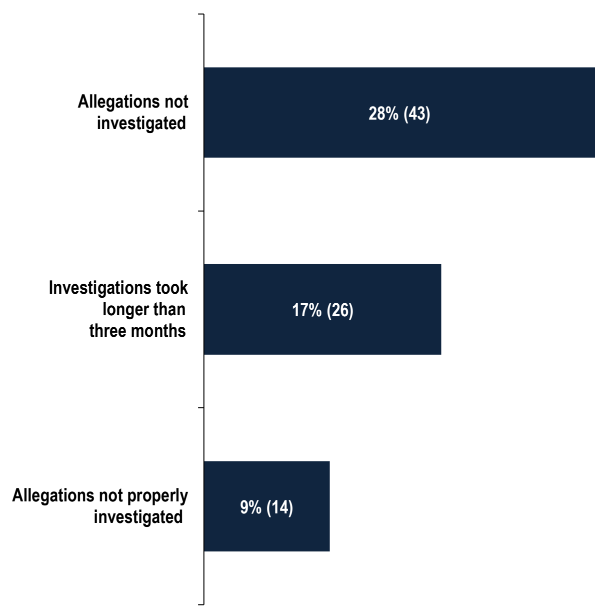
Reporting and follow-up of allegations of financial and supply chain management misconduct and fraud

Our audits showed that 38% of the municipalities **did not have all the required mechanisms for reporting and investigating transgressions or possible fraud**, such as policies, codes of conduct, fraud reporting mechanisms, and record keeping of processes. The following were the most common findings in this regard:

- A disciplinary board had not been established at 73 municipalities.
- There was no fraud hotline at 53 municipalities.
- No policies for investigations existed at 50 municipalities.

This contributed to the fact that 52% of municipalities had findings on **inadequate follow-up of allegations of financial and SCM misconduct and fraud**. Such allegations were made in the previous year at 151 municipalities where they were required to take appropriate action regarding these allegations. Figure 3 reflects our findings on how these allegations were dealt with.

Figure 3: Follow-up of allegations of financial and supply chain management misconduct and fraud



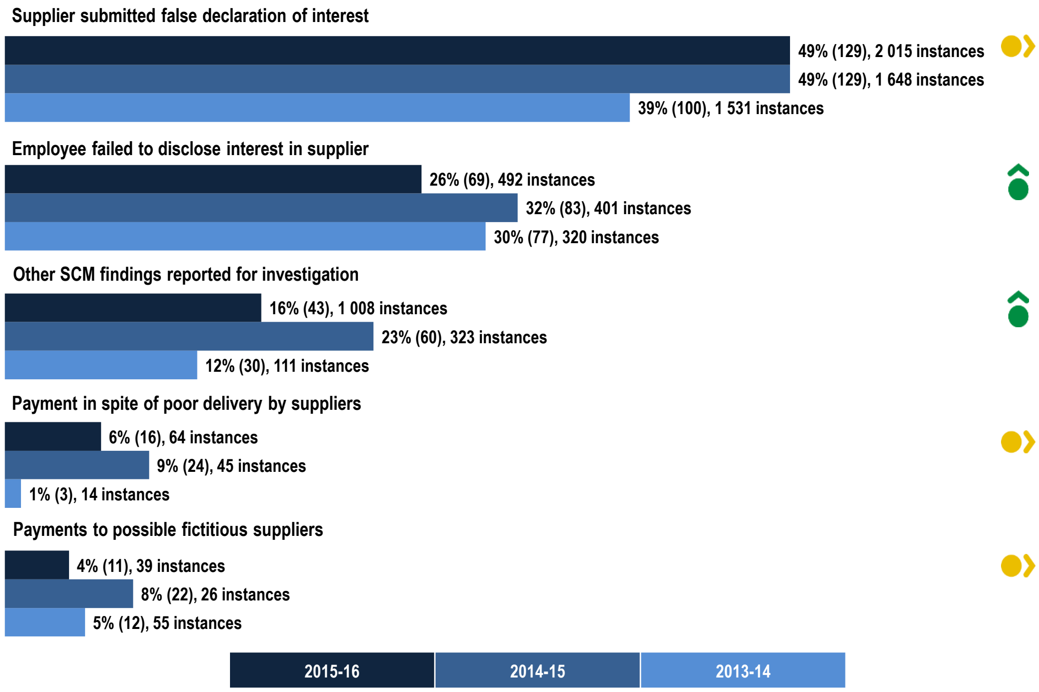
These findings were mostly in North West (18 municipalities), the Eastern Cape (13 municipalities), KwaZulu-Natal (12 municipalities) and Mpumalanga (12 municipalities).

Supply chain management findings reported for investigation

We report all our findings on SCM compliance and weaknesses to management for follow-up. If there are **indicators of possible fraud or improper conduct in the SCM processes**, we recommend that management conduct an investigation. The findings recommended for investigation are highlighted in the executive summary of our management reports to ensure that the municipal manager, mayor and audit committee take note thereof.

Figure 4 illustrates the extent of SCM findings we had reported to management for investigation.

Figure 4: Supply chain management findings reported to management for investigation



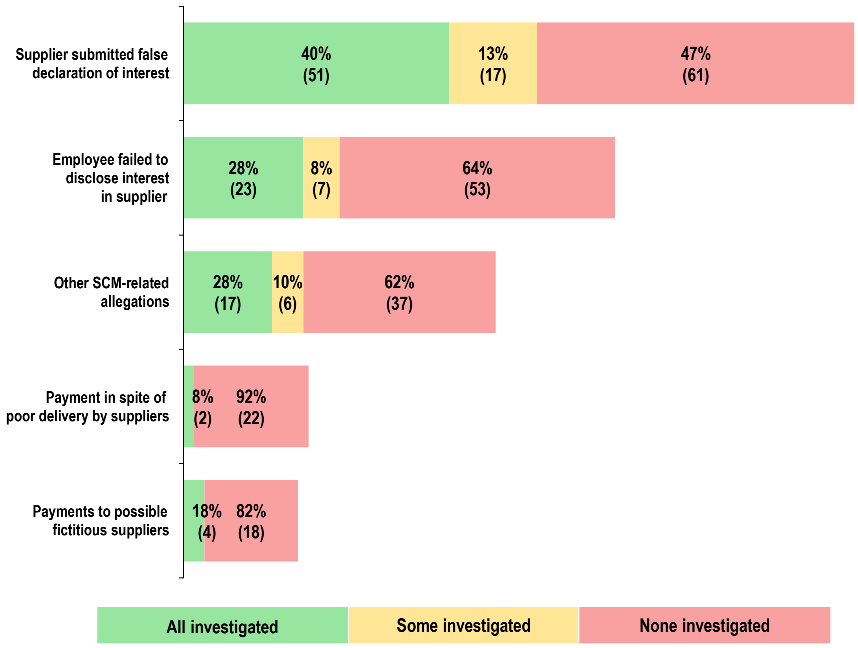
In 2015-16, we reported these types of findings at 161 municipalities (61%), which is a slight improvement from the 165 municipalities (63%) in 2014-15. In total, 74% of the 165 municipalities that had such findings in 2014-15 had similar findings in 2015-16.

As detailed in section 4.2.1, awards were made to **suppliers who submitted fraudulent declarations**. The submission of fraudulent declarations by suppliers at nearly half of the municipalities is concerning. This was most common in KwaZulu-Natal (34 municipalities), the Eastern Cape (22 municipalities), Mpumalanga (15 municipalities) and Limpopo (15 municipalities). The municipalities with the highest instances of the submission of fraudulent supplier declarations were eThekwini Metro (377 suppliers), City of Johannesburg Metro (80 suppliers), City of Cape Town Metro (68 suppliers) and Ekurhuleni Metro (59 suppliers).

There had been little improvement in the type of findings reported since the previous year, except with regard to employee declarations and other SCM findings reported for investigation. This was as a result of municipal management not investigating our findings and ensuring that there were consequences for non-compliance and transgressions.

Figure 5 shows whether all, some or none of the previous year's SCM findings reported for investigation had been investigated.

Figure 5: Follow-up of the previous year's supply chain management findings

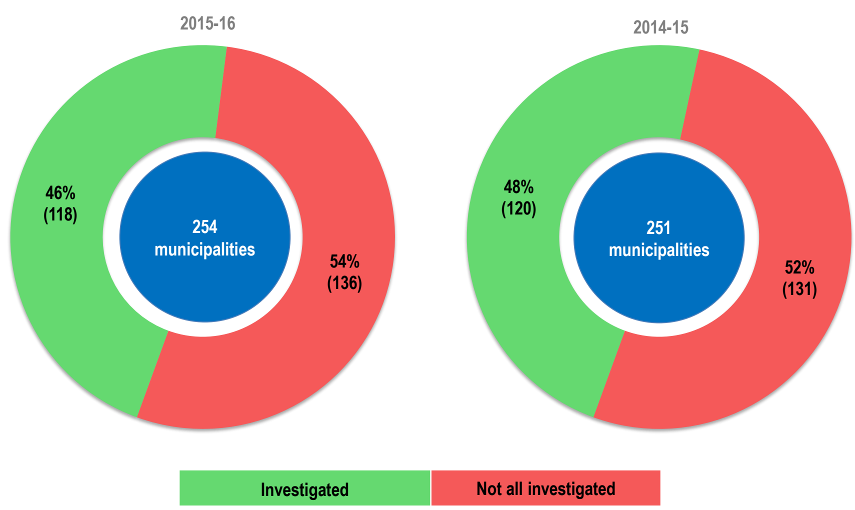


Although 56 of the 165 municipalities (34%) investigated all of the SCM findings reported for investigation in the previous year, the fact that 82 municipalities (50%) had not done so is concerning. The provinces with the highest number of municipalities where none of the SCM findings reported for investigation in the previous year had been investigated were the Eastern Cape (21), North West (17) and KwaZulu-Natal (12).

Investigation and follow-up of unauthorised, irregular and fruitless and wasteful expenditure

Figure 6 shows the overall status of investigations at the municipalities that had incurred unauthorised, irregular and fruitless and wasteful expenditure in the previous year.

Figure 6: Investigation of unauthorised, irregular and fruitless and wasteful expenditure



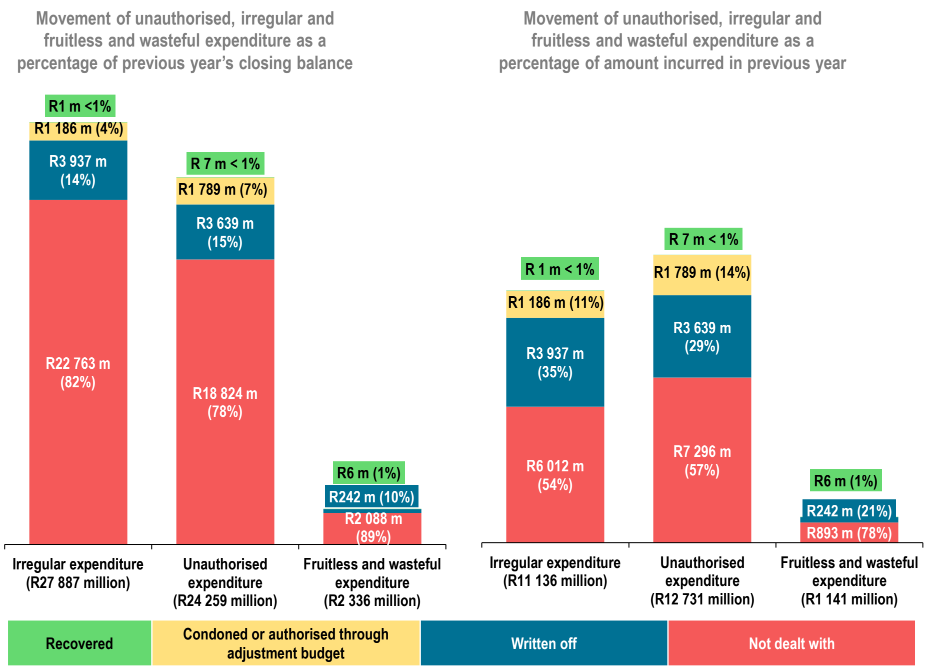
At over 50% of the municipalities, the **council failed to conduct the required investigations into all instances** of unauthorised, irregular and fruitless and wasteful expenditure reported in the previous year, which is a slight regression from the previous year. A total of 112 of the 131 municipalities (85%) that did not conduct investigations in 2014-15 again did not do so in 2015-16.

Of particular concern is that sufficient **steps were not taken to recover, write-off, approve or condone** unauthorised, irregular and fruitless and wasteful expenditure as required by legislation. As explained in section 4.2.1, irregular expenditure must be investigated to determine who is responsible and what the impact of the non-compliance was. Based on the outcome of the investigation, the next steps are determined and can include condonement or recovery of the expenditure. A similar process should be followed for unauthorised and fruitless and wasteful expenditure.

As a result, the year-end balance of irregular expenditure that had accumulated over many years and had not been dealt with totalled R41,7 billion, while that of unauthorised expenditure was R34,3 billion and that of fruitless and wasteful expenditure was R2 990 million.

Figure 7 shows that only a small portion of unauthorised, irregular and fruitless and wasteful expenditure of the previous years and the current year had been properly dealt with in the current year.

Figure 7: Movement in unauthorised, irregular and fruitless and wasteful expenditure balances



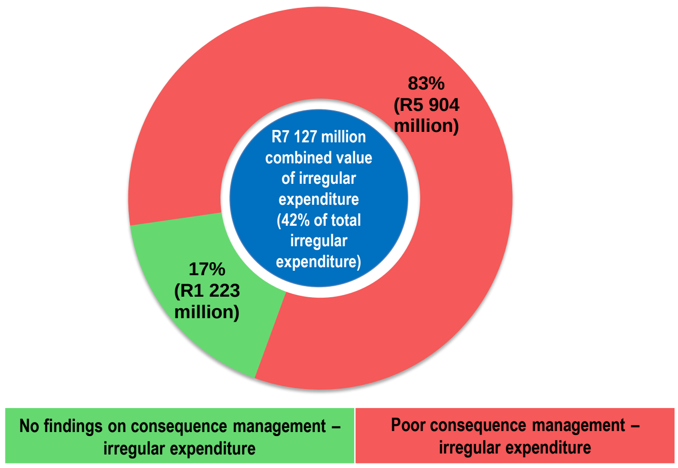
Over 50% of the unauthorised, irregular and fruitless and wasteful expenditure incurred in the previous year had not been properly dealt with.

The fact that municipalities cannot condone their own irregular expenditure played a role in the accumulation of this expenditure. Municipalities have to request condonement from the 'owners' of the legislation that had been transgressed, mostly the National Treasury. This typically requires additional information and takes some time to be considered. Some of the expenditure had also been incurred a number of years ago and the persons responsible were no longer in the service of the municipality or information was no longer available. In these cases, the municipalities should seek guidance from the National Treasury on how to deal with the expenditure.

Highest contributors to irregular expenditure linked to poor consequence management

Figure 8 highlights the correlation between poor consequence management practices and the highest contributors to irregular expenditure, as detailed in section 4.2.1.

Figure 8: Correlation between poor consequence management practices and the highest contributors to irregular expenditure



Eight of the 10 highest contributors to irregular expenditure had poor consequence management practices relating to irregular expenditure as well as to at least fruitless and wasteful expenditure or unauthorised expenditure.

As long as the political leadership and municipal officials do not make accountability for transgressions a priority, irregular expenditure, unauthorised expenditure and fruitless and wasteful expenditure as well as fraud and misconduct will continue to be widespread in local government. The majority of the municipalities have the required policies and processes to ensure that transgressions and fraud are identified and acted upon, but chose not to use it – a clear indicator of a lack of commitment to accountability.

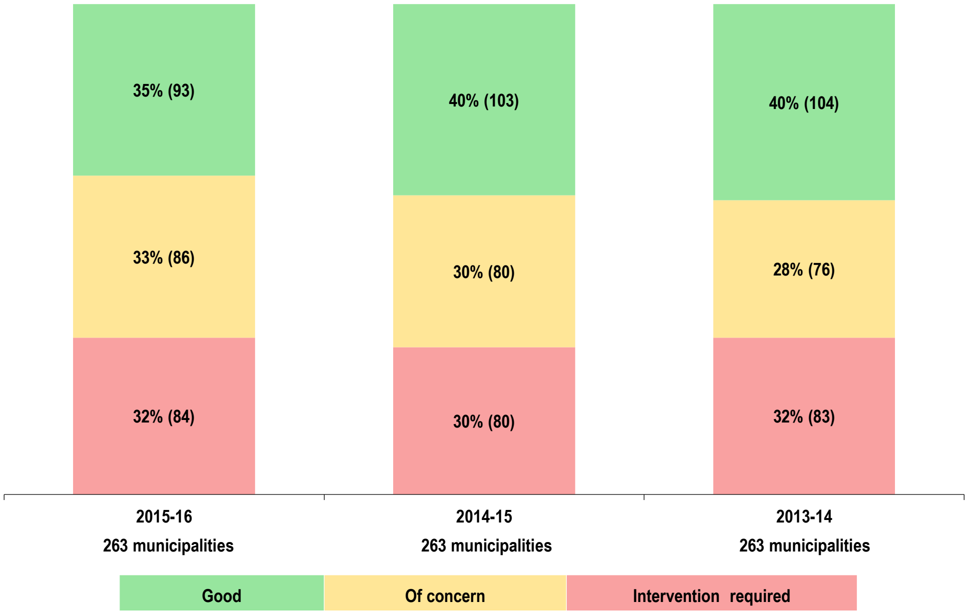
4.3 Financial health

Our audits included a high-level analysis of 10 financial indicators to provide management with an overview of selected aspects of their current financial management and to enable timely remedial action where the municipality's operations and service delivery may be at risk. We also performed audit procedures to assess whether there were any events or conditions that might cast significant doubt on a municipality's ability to continue its operations in the near future. Based on the analysis, each municipality was given an overall assessment as follows:

Good	Two or fewer unfavourable indicators
Of concern	More than two unfavourable indicators
Intervention required	Significant doubt that operations can continue in future and/or where municipalities received a disclaimed or adverse opinion, which meant that the financial statements were not reliable enough for analysis

Figure 1 shows our assessment of the **financial health of municipalities** over the past three years. The 2013-14 and 2014-15 figures have been restated to take into account changes in the indicators used to assess the financial health of municipalities.

Figure 1: Number of municipalities with indicators of financial health risks (overall)

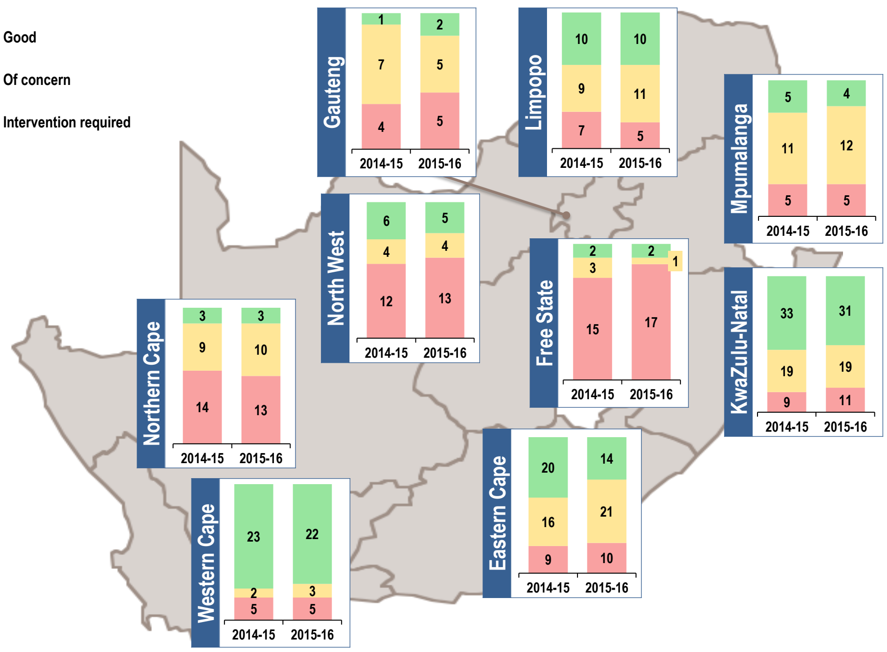


The number of municipalities we assessed as having a good financial health status had slightly decreased since 2014-15, with the municipalities in Gauteng, Limpopo and KwaZulu-Natal being the main contributors to the regression. The regression can be attributed to inadequate processes to ensure sound financial management and the poor economic conditions prevailing in the country over the past several years, which are characterised by high consumer debt and resultant debtor default.

The slight increase in the number of municipalities in the 'intervention required' category since 2014-15 was as a result of the increase in municipalities that had going concern uncertainties.

Figure 2 indicates the number of municipalities per province with indicators of financial health risks.

Figure 2: Provincial overview of municipalities with indicators of financial health risks

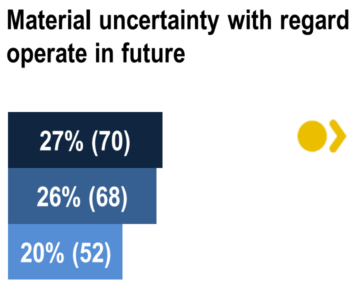


We provide further details below of the main financial indicators used for these assessments over the three-year period. The following legend applies to the figures shown:

2015-16	2014-15	2013-14

Figure 3 reflects the number of municipalities that in the past three years disclosed in their financial statements that a **material uncertainty** existed with regard to their ability to operate in the foreseeable future (in other words, as a going concern) or had received a financially qualified opinion because such disclosures were not included.

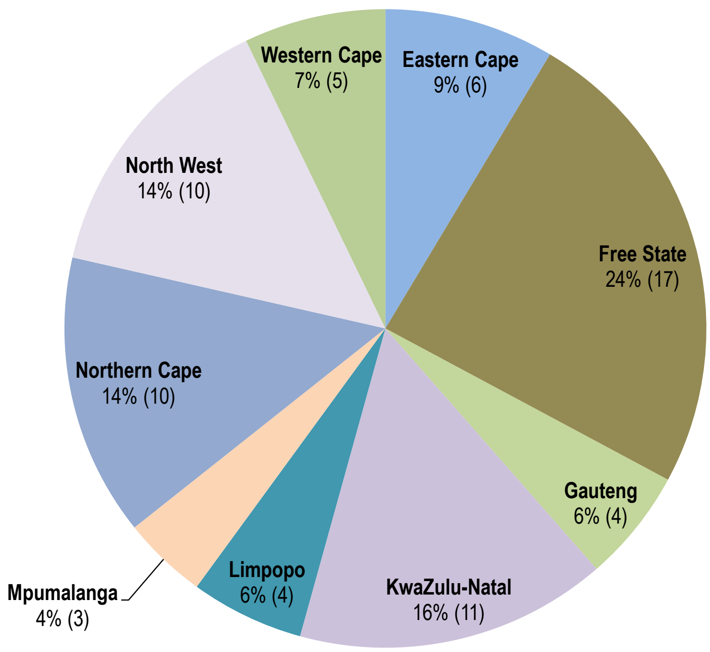
Figure 3: Going concern uncertainty



A **going concern uncertainty** existed at more than a quarter of the municipalities in 2015-16 – a slight increase from the previous year. Regressions were most notable in the Free State and Gauteng. Seventeen (85%) of the municipalities in the Free State had a going concern uncertainty. These municipalities faced significant cash-flow constraints, as they did not maximise the collection of outstanding amounts from consumers, which contributed to overdue payments to large creditors such as Eskom and water boards for their bulk purchases.

Figure 4 shows the provincial overview of the 70 municipalities where a going concern uncertainty existed.

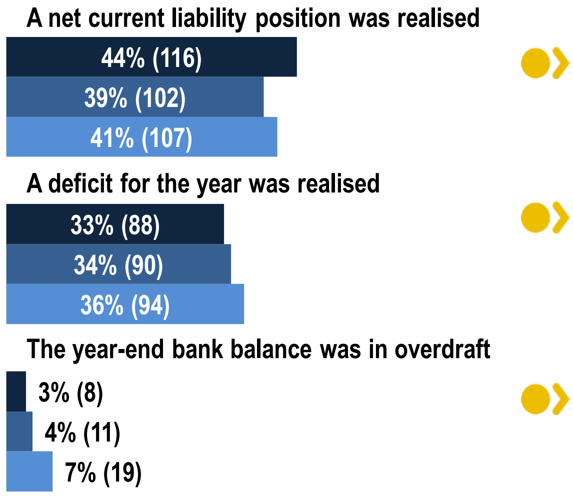
Figure 4: Provincial overview of going concern uncertainty



The regression overall was the result of poor debt collection, cash-flow constraints and a lack of effective and efficient revenue-generation and debt-collection strategies. Improvements from disclaimed opinions to unqualified or qualified opinions further made the financial statements more reliable for assessing going concern uncertainty, which also contributed to the movements.

Figure 5 shows some of the typical indicators of going concern uncertainty over the past three years, in addition to the revenue management and creditor-payment period indicators detailed later on in this section.

Figure 5: Sustainability indicators



There had been a slight improvement since 2014-15 in the number of municipalities that spent more than their available financial resources (resulting in a **net deficit**), while those whose current liabilities exceeded their current assets at year-end (**net current liability position**) showed a slight regression over the same period.

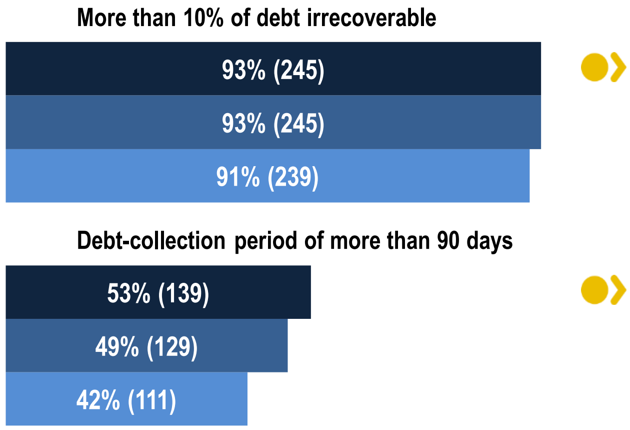
The municipalities in Limpopo and North West were the main contributors to the slight improvement relating to the net deficit. While some municipalities improved in North West, 50% of the municipalities in the province still incurred a deficit. The Free State had the highest number of municipalities with a deficit (70%).

Municipalities in Gauteng, KwaZulu-Natal and Mpumalanga were the main contributors to the slight regression with regard to the net current liability position, which was caused by cash-flow problems (mainly due to poor debt collection and the inability to pay creditors).

The number of municipalities with year-end **bank balances in overdraft** had decreased slightly since the previous year.

One of the main reasons for the failing financial health of municipalities is inadequate **revenue management**. The main indicators over the past three years in this regard are reflected in figure 6.

Figure 6: Revenue management

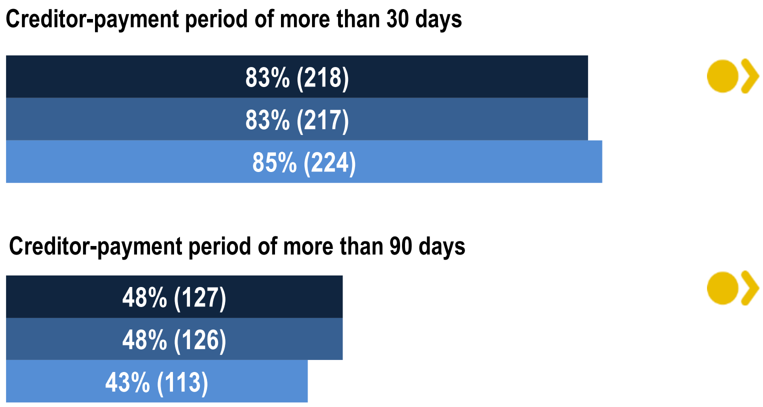


Just over 90% of municipalities estimated in their financial statements that more than 10% of the outstanding amounts owed to them would not be paid, which remained unchanged over the two-year period.

As part of our analysis, we calculated the average number of days it took municipalities to **collect debt** they deemed to be recoverable. Just over half of the municipalities had an average debt-collection period of over 90 days in 2015-16. This is a slight regression from the previous year. Municipalities in the Eastern Cape, the Free State, Gauteng, Limpopo and KwaZulu-Natal were the main contributors to the regression. The reasons for the poor revenue management were a lack of the right skills in finance units, the poor economic climate as well as inadequate systems to account for revenue, which not only affected debt collection but also the ability to account correctly for debtors in the financial statements.

Extended collection periods put the cash flow of municipalities under significant pressure, which in turn meant that they took longer to pay their creditors. Figure 7 shows the number of municipalities with an average **creditor-payment period** of more than 30 days and more than 90 days over the three-year period.

Figure 7: Creditor-payment period



The number of municipalities with extended payment periods over 30 and over 90 days showed no movement at 83% and 48%, respectively. While the movement remained stagnant, over 60% of the municipalities in the Free State, Mpumalanga, the Northern Cape and North West had average extended payment periods of over 120 days. Only three municipalities in the Western Cape had such long payment periods. Municipalities with extended creditor-payment periods are running the risk of key suppliers discontinuing their services, which may have a significant impact on service delivery.

Our analysis of financial health shows a continuing weakening in local government finances as a result of the poor collection of revenue from debtors, cash-flow problems and the current poor economic climate at a time when municipalities are under increasing pressure to provide basic services while financial resources are dwindling.

According to a report published in March 2017 by the National Treasury entitled *The state of local government finances and financial management as at 30 June 2016*, the inability of municipalities to generate own revenue has led to high reliance on the conditional grants from national and provincial government to fund capital programmes. Based on their analysis of 273 municipalities, conditional grants funded more than 75% of the capital budget of 125 municipalities (46%). At only 91 (33%), the funding was less than 30%. This further continued to place the fiscus under pressure.

4.4 Management of grants

Municipalities annually receive conditional grants from the national revenue fund as approved in terms of the Division of Revenue Act (DoRA). Municipalities may only use a conditional allocation for its stated purpose in accordance with the requirements of the framework for each grant and for projects or programmes included in their business plans.

Our audits included testing compliance with DoRA and the individual grant frameworks, evaluating how the funding was used, and assessing the management of the projects funded by the grants.

In this section, we present the results of these audit tests for the **MIG**, the **USDG** and the **PTNG**. We also look at overall **compliance by municipalities with DoRA**. More information on our audits as well as the purpose of, and conditions attached to, these grants is included in section 13.1.

Municipal infrastructure grant

The DCoG introduced the **MIG** in 2004-05 to improve poor communities' access to basic service infrastructure by providing specific capital finance for basic municipal infrastructure backlogs.

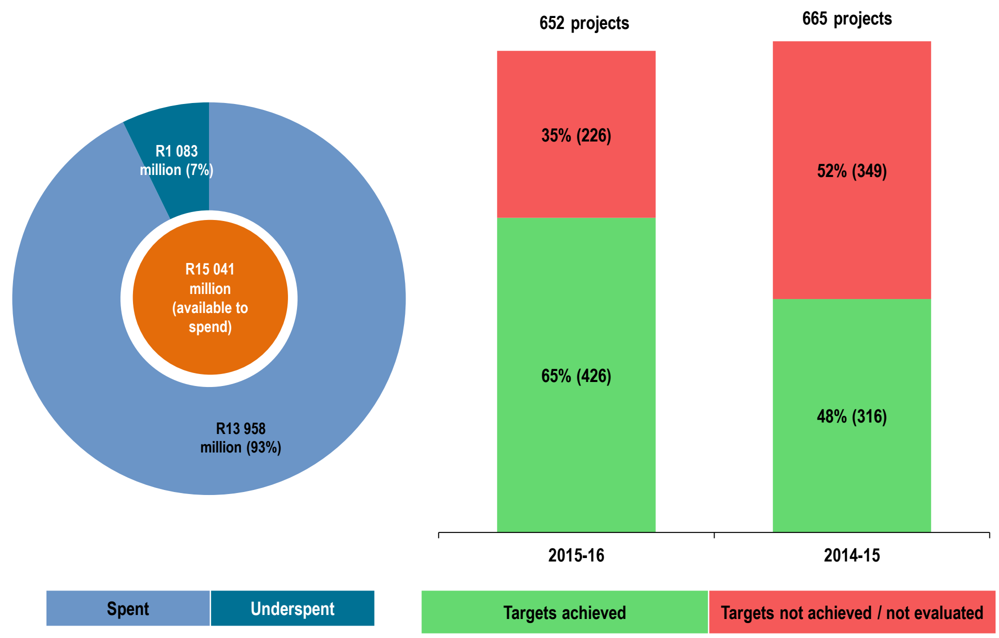
In 2015-16, R14,96 billion was allocated in terms of DoRA for the MIG to 247 municipalities. This section includes the analysis of only 234 municipalities for which audits had been completed by the cut-off date. The MIG allocated to these 234 municipalities amounted to R14,14 billion. Due to unspent funds rolled over from the previous financial year, the municipalities had R15,04 billion to spend on infrastructure projects funded from the MIG. Table 1 shows the MIG spending per province.

Table 1: Spending of municipal infrastructure grant per province

Province	Municipal infrastructure grant	
	Percentage spent	Amount R million
Eastern Cape	95%	3 063
Free State	90%	402
Gauteng	97%	446
KwaZulu-Natal	98%	3 413
Limpopo	85%	2 740
Mpumalanga	93%	1 817
Northern Cape	93%	365
North West	89%	1 224
Western Cape	97%	488
Total	93%	13 958

Figure 1 shows how much of the MIG allocations municipalities had spent and whether the planned targets for the infrastructure projects audited, had been achieved in 2015-16 and 2014-15. We audited 652 projects funded by the MIG in 2015-16. The projects in the red category are those where the targets were not achieved, the municipality had not assessed the achievement, or we could not audit the assessment as supporting documentation was not provided.

Figure 1: Municipal infrastructure grant: spending and achievement of planned targets



In 2015-16, 93% of the **available grant was spent** – an improvement from the 87% in 2014-15. In total, 105 municipalities underspent on the MIG, of which 53 underspent by more than 10%. This is an improvement from the 123 municipalities that had underspent in 2014-15.

At 94% of these municipalities, the grant money was **used for its intended purpose**. Where the grant money was not used for its intended purpose, it was reported in the audit report and/or management report as non-compliance with DoRA. Five of these municipalities (which did not spend the grant money for its intended purpose) were in the Free State and four in the Eastern Cape. Examples of this practice are Mafube and Masilonyana in the Free State that used the grants for operating expenditure.

We continued to audit the multi-year projects selected in 2014-15. We also selected other projects, mostly those that deliver water and sanitation infrastructure. Although there has been an overall improvement in the **achievement of the targets set for these projects** (as shown in figure 1), the slow delivery of projects affects the ability of municipalities to improve access to basic services for poor communities. A grant amount of R6 099 million was provided for 226 projects at 92 municipalities where the targets were not achieved or performance had not been evaluated, of which R5 511 million (90%) had been spent.

Table 2 shows our **key findings** from the audit of these projects – the table includes the number and percentage of municipalities and projects affected in each province.

Table 2: Findings on projects funded by the municipal infrastructure grant

Findings		Total	Eastern Cape	Free State	Gauteng	KwaZulu-Natal	Limpopo	Mpumalanga	Northern Cape	North West	Western Cape
Planned targets not achieved / Performance on project not evaluated	Projects	226 (35%)	42 (35%)	13 (33%)	1 (5%)	25 (15%)	45 (48%)	20 (41%)	33 (63%)	38 (63%)	9 (16%)
	Municipalities	92 (40%)	17 (43%)	6 (38%)	1 (14%)	12 (20%)	9 (35%)	11 (61%)	15 (71%)	17 (85%)	4 (17%)
Incorrect performance reporting	Projects	72 (11%)	17 (14%)	4 (10%)	1 (5%)	5 (3%)	5 (5%)	2 (4%)	14 (27%)	21 (35%)	3 (5%)
	Municipalities	35 (15%)	8 (20%)	2 (13%)	1 (14%)	4 (7%)	2 (8%)	2 (11%)	5 (24%)	10 (50%)	1 (4%)
SCM findings on project	Projects	192 (29%)	36 (30%)	14 (35%)	2 (10%)	16 (10%)	49 (52%)	21 (43%)	19 (37%)	31 (52%)	4 (7%)
	Municipalities	65 (28%)	12 (30%)	5 (31%)	2 (29%)	7 (12%)	7 (27%)	10 (56%)	8 (38%)	12 (60%)	2 (8%)
Misstatements identified	Projects	84 (13%)	22 (18%)	3 (8%)		6 (4%)	32 (34%)	3 (6%)	11 (21%)	7 (12%)	
	Municipalities	21 (9%)	6 (15%)	2 (13%)		2 (3%)	2 (8%)	2 (11%)	4 (19%)	3 (15%)	

The following are examples of weaknesses that we observed in the infrastructure projects funded by the MIG:

- Highmast phase 2 commenced in April 2016 in Tubatse (Limpopo) to improve the provision of basic services (lighting) in the rural areas of the municipality. The project was planned to be completed by 31 July 2016 with a target of 70 highmast lights. At year-end, only 40 highmast lights had been completed at a cost of R8,3 million financed through the MIG. Because the municipality appointed the contractor late, the targeted completion date was not met. The project is significantly behind schedule and many rural areas in the municipality remain without lighting.
- The Garies bulk water infrastructure project commenced during 2016 in Kamiesberg (Northern Cape) to eradicate the use of sceptic tanks and ventilated pit latrines within the small towns that surround Garies. The project was financed through a R14,1 million MIG and the first phase, originally planned to be completed in December 2015, was completed in May 2016. The project was split into three phases, but due to challenges experienced during the first phase, the planned completion date of the entire project could possibly be delayed. Inadequate project planning and budgeting by the municipality caused these delays as changes had to be made to the original plan: the municipality had planned to make use of the old infrastructure as part of the project by upgrading the current facilities, but the old reservoirs were located on private land and the owner wanted compensation that had not been budgeted for. The municipality then changed the specifications to include new reservoirs that would be located on municipal land.
- Irregular expenditure was incurred on the Hertzogville/Malebogo project (in Tokologo in the Free State) for the upgrading of the community stadium. Competitive bidding was not followed at all and a supplier was merely appointed with no letter of deviation.

Urban settlement development grant and public transport network grant

The **USDG** was introduced to assist metropolitan municipalities in improving access to basic services to households through the provision of bulk and reticulation infrastructure as well as urban land production to support broader urban development and integration. The **PTNG** aims at providing accelerated construction and improvement of non-motorised transport infrastructure.

In 2015-16, R10,55 billion to eight metros and R5,95 billion to 13 municipalities were allocated in terms of DoRA for the USDG and the PTNG, respectively.

The USDG allocated to seven metros (excluding Mangaung Metro for which the audit had not been completed by the cut-off date) amounted to R9,86 billion. Due to unspent funds rolled over from the previous financial year, the municipalities had R10,55 billion to spend on projects funded by the USDG.

The PTNG allocated to 11 municipalities (excluding Mangaung Metro and Rustenburg for which the audits had not been completed by the cut-off date) amounted to R5,37 billion. Although a DoRA allocation was made to Buffalo City Metro, the metro did not receive the allocation of R22 million, as the municipality did not have the capacity to implement the grant requirements. This, combined with the unspent funds rolled over from the previous financial year, meant that the municipalities had R5,36 billion to spend on projects funded by the PTNG in 2015-16.

Figures 2 and 3 show how much of the USDG and the PTNG municipalities had spent and whether the planned targets for the projects tested had been achieved.

Figure 2: Urban settlement development grant: spending and achievement of planned targets

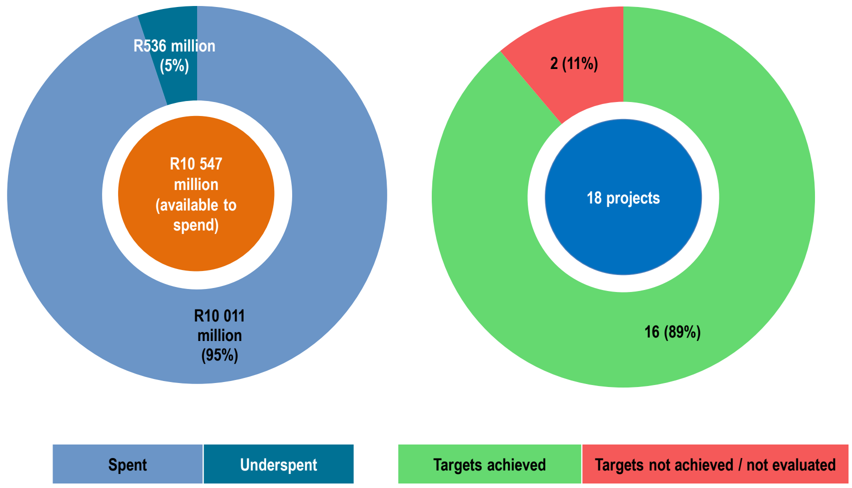
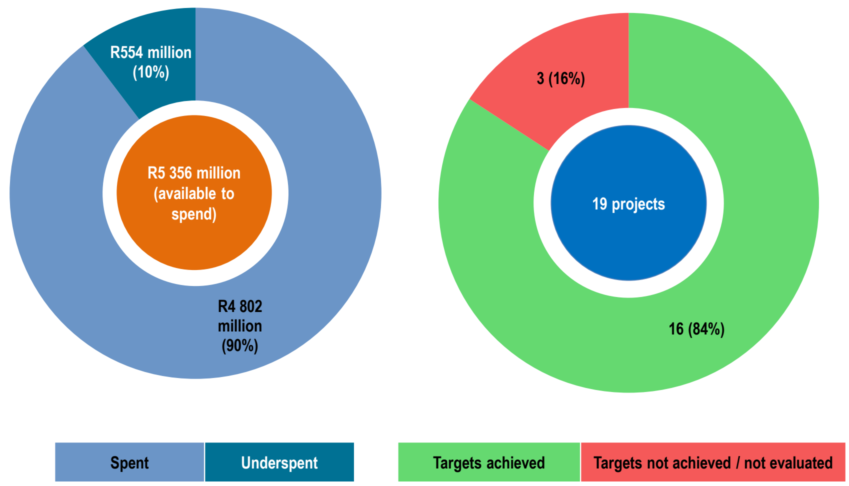


Figure 3: Public transport network grant: spending and achievement of planned targets



The **targets for the majority of the projects** had been achieved, goods and services were received for the money spent, and performance was evaluated on projects funded by the USDG and the PTNG. Ekurhuleni Metro was the only municipality that **underspent** the USDG by more than 10%, mainly due to delays in finalising designs, cash-flow problems by service providers, and disputes with constructors and service providers. The City of Cape Town Metro, Mbombela, Msunduzi and Nelson Mandela Bay Metro underspent the PTNG by more than 10%, mainly due to delays in procurement processes and designs, which resulted in work on some projects starting late. Ekurhuleni Metro alone was responsible for R291 million (54%) of the total underspending of R536 million relating to the USDG.

Targets were not achieved or evaluated at Ekurhuleni Metro and the City of Tshwane Metro on two projects that were funded by the USDG and three projects that were funded by the PTNG. We also raised SCM findings on one project funded by the USDG at the City of Johannesburg Metro.

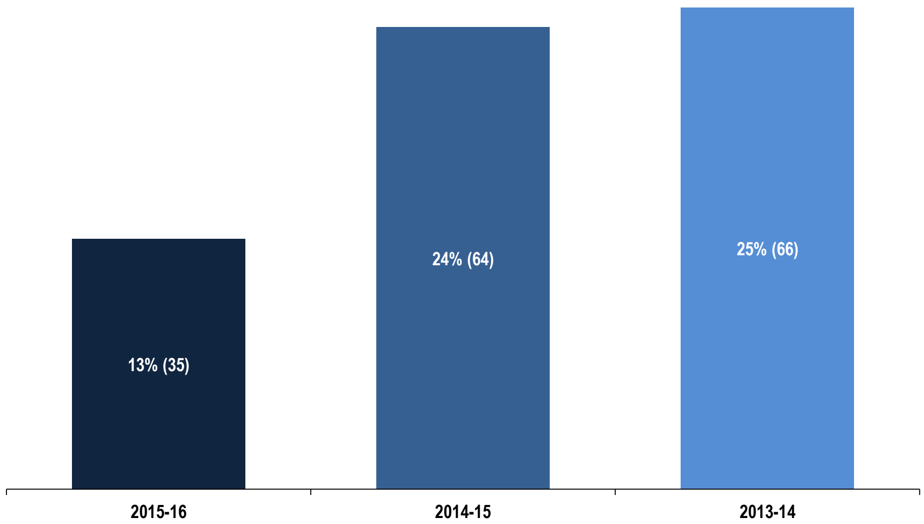
The following are examples of weaknesses that we observed in the infrastructure projects funded by the USDG and the PTNG:

- Targets were not achieved on the project funded by the USDG to upgrade gravel to tar in the Ekangala ward in the City of Tshwane Metro, due to the late appointment of a panel of consultants. The BRT line 2C project funded by the PTNG was deferred to 2016-17 due to a policy decision on lane acquisition, which could result in the revision of the designs.
- At an overall level, a large number of variation orders were issued on projects funded by the PTNG. In addition, a number of accidents and incidents occurred at the integrated rapid public transport network locations, some of which related to construction, pointing to safety risks. Some quality issues were also identified during site visits, such as the deterioration of bus lanes due to a lack of maintenance.

Non-compliance with the Division of Revenue Act

Figure 4 shows the number of municipalities that received a conditional grant via a DoRA allocation where we **reported material findings on compliance** with the act.

Figure 4: Non-compliance with the Division of Revenue Act in managing conditional grants



As indicated in figure 4, only 13% of the municipalities failed materially to comply with DoRA – an improvement from the 24% in the previous year. The most notable improvements were in North West (26%), Mpumalanga (19%) and the Eastern Cape (16%) due to improved controls at the municipalities as well as oversight by some external stakeholders.

The common compliance findings below indicate that not all municipalities properly managed the funds provided through grants and the funded programmes:

- The performance of the programmes funded by allocations was not evaluated – 27 municipalities (2014-15: 45).
- Allocations were used for purposes other than those stipulated in DoRA or in the gazetted framework – 13 municipalities (2014-15: 25).

Conditional grants are allocated to drive specific government objectives. It is important that projects and programmes funded by grants are closely managed to ensure that they not only meet the set targets, but also deliver the intended outcomes.

4.5 mSCOA readiness of municipalities – an emerging risk

The **mSCOA** project is part of the National Treasury's ongoing budget and reporting reforms aimed at improving financial reporting. With effect from 1 July 2017, all municipalities will have to capture all their financial transactions against a predefined classification framework, which will result in uniformity of line items in terms of revenue, expenditure, assets and liabilities. This will thus have an impact on the 2017-18 financial statements and audits of all local government auditees. Piloting takes place in close cooperation with the National Treasury's mSCOA project team and provincial treasuries.

The objectives of the project are as follows:

- Enable the alignment of budget information captured in the course of the implementation of the budget.
- Improve data quality and credibility.
- Achieve a greater level of standardisation.
- Develop uniform data sets critical for 'whole-of-government' reporting.
- Standardise and align the local government accountability cycle by the regulation of not only the budget and in-year reporting formats but also the annual report and annual financial statement formats.
- Create the opportunity to standardise key business processes with the consequential introduction of further consistency in the management of municipal finances.
- Improve transparency, accountability and governance through the uniform recording of transactions at posting account level detail.
- Enable deeper data analysis and sector comparisons to improve financial performance.
- Standardise the account classification to facilitate mobility in financial skills within local government and between local government and other spheres as well as the private sector and to enhance the ability of local government to attract and retain skilled personnel.

Figure 1 indicates our overall assessment of the state of readiness of municipalities to implement mSCOA, while figure 2 shows a provincial overview of mSCOA readiness.

Figure 1: Readiness for mSCOA

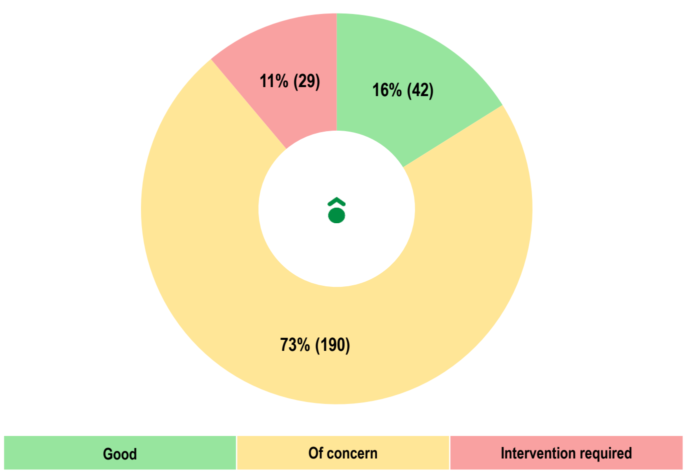
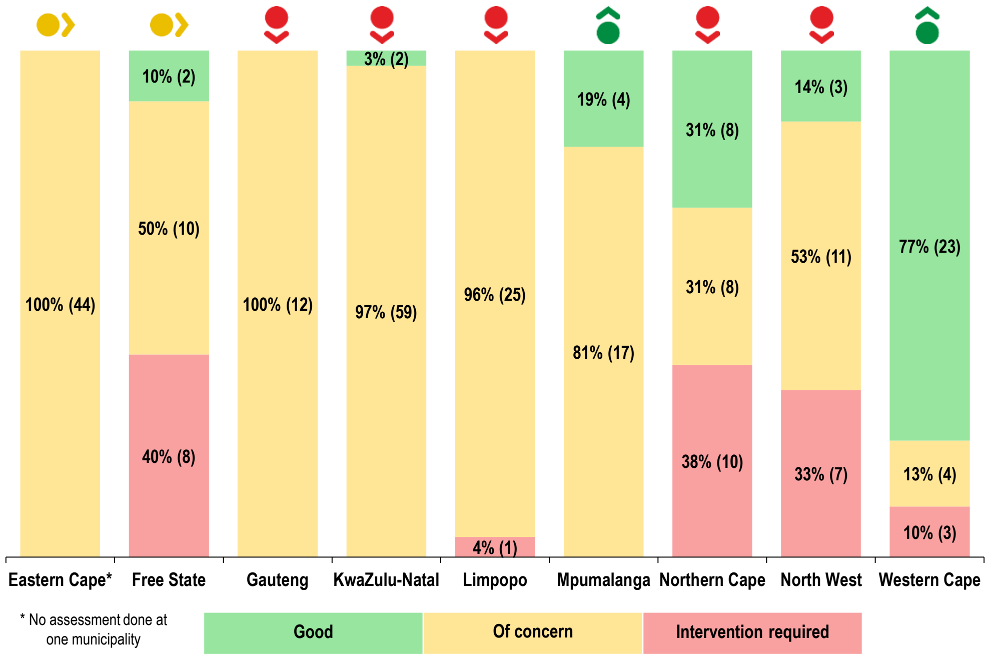


Figure 2: Provincial overview of mSCOA readiness



Municipalities generally made slow progress in ensuring that they would be ready to implement mSCOA by the due date. As indicated in figure 1, the readiness of 73% of the municipalities was still concerning, while that of 11% still required intervention, which represent the majority of municipalities. Regressions were noted in Gauteng, KwaZulu-Natal, Limpopo, North West and the Northern Cape due to some municipalities, which were previously on track with their mSCOA implementation, falling behind in 2015-16. Furthermore, Mpumalanga and the Western Cape showed a significant improvement in ensuring readiness to implement mSCOA by 1 July 2017. The Free State, the Northern Cape and North West were among the provinces that required intervention at more than a third of their municipalities, as they did not pay attention to the previous year's assessment results – which could mean that they will not be able to meet the implementation date.

Some of the **root causes** that may result in municipalities **not meeting the implementation due date** are the following:

- Municipalities experienced capacity and skills constraints that made it difficult to plan and manage the change to mSCOA requirements.
- Municipalities did not have the money to commence with the implementation of mSCOA and to use the internal audit unit to support them from a project-assurance perspective.
- Municipalities were waiting for the outcomes of the pilot municipalities that were implementing mSCOA to ensure that they address the lessons learned from these pilots.
- Municipalities experienced challenges with regard to data-cleansing, data-migration and data-mapping processes within the current systems.
- Municipalities had to keep up to date with the different versions of mSCOA that were released, which created some uncertainty. However, the National Treasury indicated in MFMA Circular No. 80 that mSCOA version 6 would be released and locked down for the 2017-18 financial year for transacting and auditing.

The following **actions** should be taken **to address the root causes**:

- All municipalities should follow the guidance provided by the National Treasury and issued through MFMA SCOA circulars.
- Ongoing training is of the utmost importance to capacitate staff in the successful implementation of mSCOA. The National Treasury, in partnership with the Institute of Municipal Finance Officers (IMFO), developed accredited training to provide an introduction and theoretical information on mSCOA, including testing of candidates. Municipalities should liaise with their provincial treasury to arrange for non-accredited training, geared at converting their existing trial balance to the mSCOA chart.
- Municipalities should share their experiences and lessons learned with the implementation of mSCOA to ensure that efficiencies are built into the process.
- Municipalities should continue to prepare for the implementation of mSCOA or keep the momentum going if they are already busy with implementation to ensure that all implementation challenges are resolved by 1 July 2017.

Conclusion

Sustainable improvements in financial management can be achieved if the leadership clearly defines the targets to be achieved in terms of audit outcomes, project delivery and financial health by using, among other, audit action plans, the new integrated development plan, service delivery and budget implementation plan, annual budget and project plans (**PLAN**).

The basic disciplines of proper record keeping and standard daily and monthly controls built on a foundation of effective and efficient leadership and stability in key positions will enable a robust financial management system (**DO**).

Regular, credible in-year reporting monitored by, and acted upon, senior management, the municipal manager, the mayor as well as reports and recommendations on financial management and compliance from the internal audit unit and the audit committee will enable corrective action to be taken if targets are not achieved or if transgressions or poor performance is identified (**CHECK**).

Consistently investigating indicators or allegations of transgressions and poor performance and applying consequence management will ensure that a culture of accountability prevails (**ACT**).

5 Status of performance management

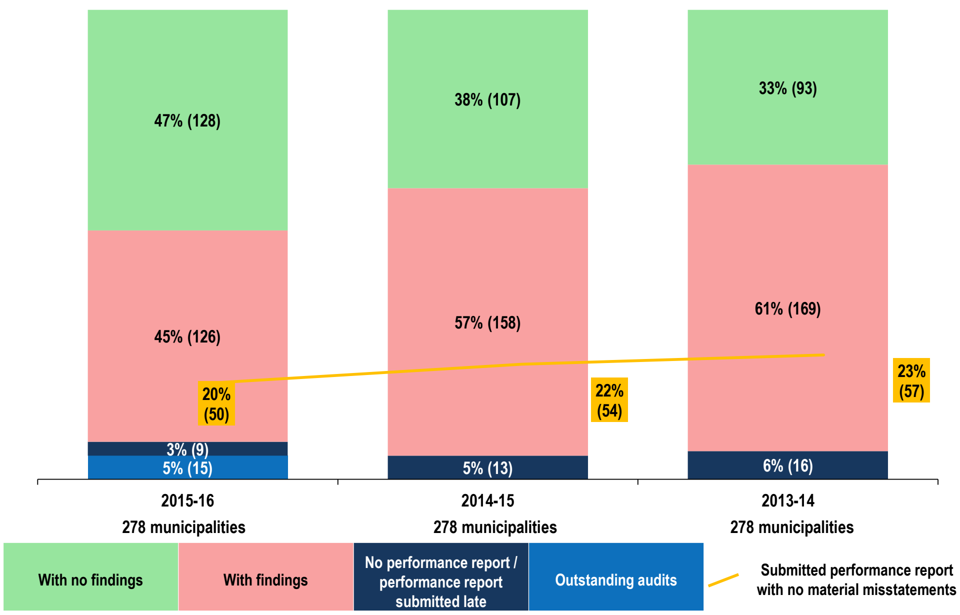
5. Status of performance management

The result of poor internal controls on performance management is reflected and demonstrated in this section.

5.1 Performance reports

Figure 1 provides an overview of audit outcomes on the performance reports, the performance reports submitted with no material misstatements (orange line), and the municipalities that did not submit performance reports or submitted them late over a period of three years.

Figure 1: Findings on performance reports and the quality and timeliness of submission for auditing



As depicted in figure 1, there had been a significant increase in the number of municipalities with **no material findings** on the quality of their performance reports since 2014-15. The main improvements during 2015-16 occurred in the Free State and Gauteng, while Mpumalanga slightly regressed.

Overall, 94 municipalities (36%) had **no material findings in the current and previous year**, which means that the controls and processes required to produce credible performance reports were in place to sustain the quality of performance reports. There had been a slight improvement in the **submission of performance reports** since 2014-15 when 5% of municipalities had either not prepared performance reports or not submitted them on time for the audit. The improvement was more noticeable in the Northern Cape over the two-year period.
The province still remained the highest contributor in this regard, with 23% of their municipalities not preparing performance reports due to performance management systems not being in place and a lack of skills and competencies at senior management level to implement systems and to produce credible performance reports. Some municipalities also focused more on the reporting of financial statements than on the reporting of performance information.

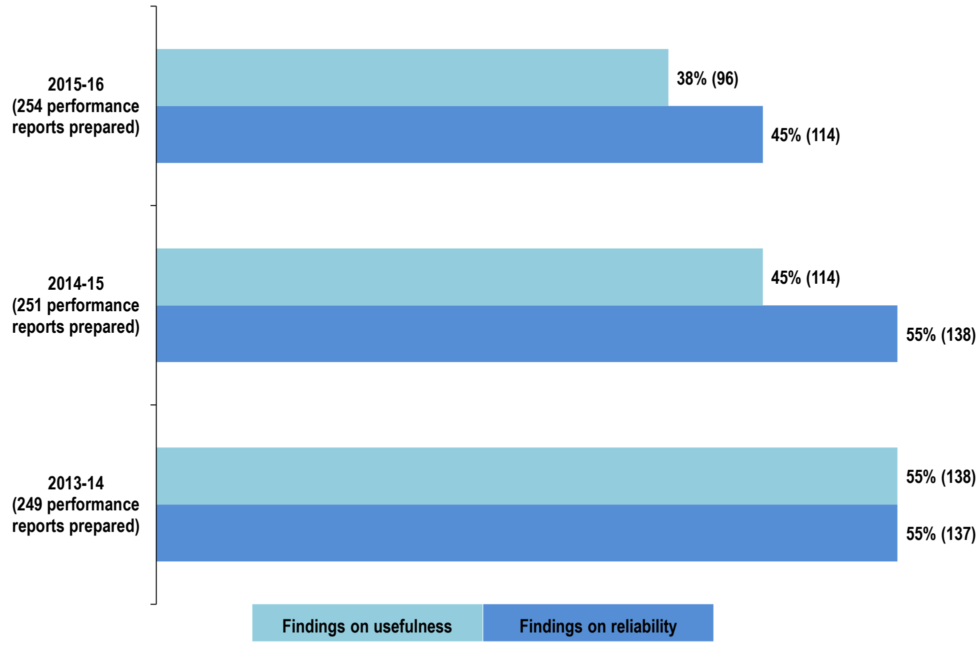
Examples of municipalities that did not prepare performance reports or did not submit them on time included the following:

- Eastern Cape (two): Tsolwana did not prepare a report this year, while Ikwezi failed to prepare a report in the current and previous year.
- Northern Cape (six): Hantam did not prepare a report this year, while Khai-Ma, Mier, Richtersveld, Thembelihle and Ubuntu failed to prepare a report in the current and previous year.
- Western Cape (one): Oudtshoorn failed to prepare a report in the current and previous year.

Figure 1 also shows a slight reduction since the previous year in the number of municipalities that submitted **performance reports that contained no material misstatements**. In total, 78 municipalities (31%) had no material findings on the quality of their performance reports in their 2015-16 audit report only because they **corrected all the misstatements** we had identified during the audit.

Figure 2 reflects the findings on the **usefulness and reliability of performance reports** over the three-year period for municipalities that had prepared and timeously submitted performance reports.

Figure 2: Findings on the performance reports prepared



As can be seen in figure 2, there had been an improvement in the **usefulness** of the information in the performance reports since 2014-15. The number of municipalities with findings on usefulness decreased by 7% from 114 to 96.

The most common findings on usefulness in 2015-16 were that municipalities reported on indicators that were not well defined (22%) or verifiable (19%); reported information was not consistent with the objectives, measures and/or targets (24%); and targets were not measurable (16%) or specific enough (15%) to ensure that the required performance could be measured and reported in a useful manner.

The usefulness of the reported information continued to improve, as municipalities corrected their performance indicators and targets as part of the annual planning and budget processes based on our recommendations and their increased understanding of the application of the requirements for performance planning.

Figure 2 also shows that there was an improvement in the **reliability** of performance reports in 2015-16. The processes and controls required to produce reliable information on performance had shown some improvement over the period.

Quality financial statements are an important accountability mechanism, as they enable oversight structures to assess the financial performance and position of a municipality. In the public sector, however, the focus of oversight is also on whether the municipality used its money and resources to deliver on its service delivery objectives and mandate. Performance reports that do not include useful information or that are unreliable hamper the ability of oversight structures to assess the performance of the municipality and call them to account. It also weakens decision-making at different levels, including the decisions made by the management of municipalities.

Performance planning, management and reporting are improving slightly every year, but overall the progress is too slow. This could affect the ability of communities to hold municipalities accountable and makes it difficult for provincial and national government to track progress towards the service delivery goals in the MTSF and the National Development Plan.

Municipal legislation defines a need for **community involvement in the development and review of municipalities' integrated development plans**. An integrated development plan is a five-year plan that municipalities must compile to determine their development needs. It guides and informs all planning, budgeting, management and decision-making in a municipality. In accordance with legislation, municipalities should have a new integrated development plan in place within the prescribed time frame. In the past two years, 25 municipalities (10%) either did not consult with the local community in reviews of these plans or did not grant the local community the prescribed period to comment on the reviews. We call on municipalities to ensure that there is public participation in the development of integrated development plans, to take into account the needs of local residents and enhance local government's transparency and accountability towards them.

5.2 Provision of water and sanitation

The **provision of water and sanitation** to all citizens is a right enshrined in our country's constitution and a key government priority. This has received even more attention with the adoption of the sustainable development goals whereby all citizens should have access to water and sanitation by 2030. Historically, the country has had backlogs in providing access to water and sanitation, but the situation has significantly improved since 1994. According to the *General household survey, 2015* published by Statistics South Africa, 89% of households had off-site or on-site access to pipe or tap water in their dwellings, and 80% to sanitation facilities. Inequalities continue to persist, however, with residents in the Eastern Cape, KwaZulu-Natal and Limpopo most at a disadvantage.

The main role players in addressing the remaining backlog are the Department of Water and Sanitation (DWS) that is the custodian of dams and rivers as well as bulk infrastructure, the water boards that purify and distribute water, and the municipalities as the water service authorities.

There are 152 municipalities that are water service authorities. They are responsible for the distribution of water as well as for infrastructure development and maintenance, mostly funded by the MIG managed by the DCoG and grants from the DWS.

We tabled a stand-alone **performance audit report** in November 2016 on water infrastructure, which reported on the planning, management and implementation of 14 water infrastructure projects across six provinces. It was the result of a detailed audit of these projects, which highlighted weaknesses in areas of leadership and oversight, funding, project management, and intergovernmental coordination.

The reporting in this section focuses specifically on the responsibilities of municipalities with regard to the provision of water and sanitation. Different projects than those in our performance audit were included in our 2015-16 audits.

We audited the following at 151 municipalities that were responsible for the provision of water and/or sanitation services:

- Performance planning for, and reporting on, the provision of water and services
- The management of water and sanitation infrastructure projects
- The maintenance of water infrastructure and the extent of water losses

Performance planning and reporting

To ensure the proper implementation of government priorities for water and sanitation, each municipality responsible for the provisioning thereof must **plan, manage, monitor and report on their water and sanitation indicators and targets**.

In accordance with the Municipal Planning and Performance Management Regulations, municipalities should at least report on the percentage of households with access to a basic level of water and/or sanitation.

Our findings in this regard are the following:

- A total of 23 (15%) of the municipalities **did not include indicators and targets** for the provision of water and/or sanitation services in their integrated development plans or service delivery and budget implementation plans, and also did not report on it in their annual reports. These municipalities included 13 from the Northern Cape, which represented 62% of the water service providers in the province. The municipalities in the Northern Cape also did not report on a quarterly basis to the National Treasury on the progress they were making in addressing the water backlogs. The main reasons for these shortcomings were that six municipalities in the province did not submit their performance reports. Some municipalities did also not understand the legislation that guides the performance report in relation to how information should be collated, the method of collating, and how the information should be presented and disclosed.
- The information reported by 17 (11%) of the municipalities on the provision of the service **was not useful**, as it was not always consistent with what was planned; indicators were not well defined or verifiable; and/or targets were not specific, measurable or time bound.
- Eight municipalities **did not report** on the achievement of all the targets and indicators in their plans.
- The reported achievement of targets for the provision of water and/or sanitation was **not reliable** at 22 (15%) of the municipalities.
- Of the 129 municipalities that reported in a reliable manner on the provisioning of water and/or sanitation services, 119 (92%) **achieved their planned targets**.

Most municipalities responsible for water and sanitation are planning to provide the services, are reporting in a useful and reliable manner, and achieve their targets.

Water and sanitation infrastructure projects

The DWS made the eradication of basic water backlogs a national priority. The reason for the backlog is inadequate and aging infrastructure. The DCoG and the DWS made money available to fund infrastructure-related projects to address this backlog.

For audit purposes, we selected key basic water backlog projects in all nine provinces. We found that most grant funding for infrastructure projects was **used for its intended purpose**, with the exception of six municipalities.

The following are examples where grant funding was not used for its intended purpose:

- Thaba Chweu (Mpumalanga): The total amount of R16 million in funding received for water infrastructure projects was instead used for road projects.
- Zululand District (KwaZulu-Natal): Only 21% of the intended funding for water infrastructure was utilised.
- Alfred Nzo District (Eastern Cape): A total of R46 917 407 (50%) of the R93 289 899 in funding received for sanitation infrastructure projects was instead used for water projects, resulting in an underspending on sanitation.

The **grant funding** was fully utilised at 118 (78%) of the municipalities. In total, 19% underspent grants by more than 10%, of which six municipalities did not utilise their grant funding at all.

An example of such a municipality is Mafube in the Free State – the funding was used to finance operating expenditure, which resulted in the intended project being significantly delayed.

Table 1 shows our key findings from the audit of water infrastructure projects (at 148 municipalities), while table 2 shows our key findings on sanitation infrastructure projects (at 150 municipalities). The tables show the number and percentage of municipalities in a province with findings as well as further relevant information.

Table 1: Key findings on water infrastructure projects

Province	*Water infrastructure projects*					
	Total municipalities audited	Municipalities where projects exceeded planned completion date		Municipalities where projects had significant findings on SCM		Municipalities where projects did not address the cause of the backlog reported
		Number of municipalities	Average number of days exceeded	Number of municipalities	Number of projects	
Eastern Cape	15	9 (60%)	147	7 (47%)	17	4 (27%)
Free State	16	3 (19%)	189	4 (25%)	7	5 (31%)
Gauteng	10	1 (10%)	378	1 (10%)	1	
KwaZulu-Natal	15	2 (13%)	81	3 (20%)	5	2 (13%)
Limpopo	9	3 (33%)	187	1 (11%)	17	4 (44%)
Mpumalanga	18	12 (67%)	127	8 (44%)	14	2 (11%)
Northern Cape	21	4 (19%)	62	3 (14%)	5	4 (19%)
North West	19	6 (32%)	77	5 (26%)	9	8 (42%)
Western Cape	25	1 (4%)	118			1 (4%)
Total	**148**	**41 (28%)**	**130**	**32 (22%)**	**75**	**30 (20%)**

Table 2: Key findings on sanitation infrastructure projects

Province	*Sanitation infrastructure projects*					
	Total municipalities audited	Municipalities where projects exceeded planned completion date		Municipalities where projects had significant findings on SCM		Municipalities where projects did not address the cause of the backlog reported
		Number of municipalities	Average number of days exceeded	Number of municipalities	Number of projects	
Eastern Cape	14	8 (57%)	146	5 (36%)	9	5 (36%)
Free State	16	4 (25%)	428	4 (25%)	5	3 (19%)
Gauteng	10	1 (10%)	179	1 (10%)	1	
KwaZulu-Natal	16			2 (13%)	4	1 (6%)
Limpopo	9	2 (22%)	289	1 (11%)	12	4 (44%)
Mpumalanga	18	9 (50%)	157	5 (28%)	7	4 (22%)
Northern Cape	21			3 (14%)	2	2 (10%)
North West	19	6 (32%)	95	7 (37%)	11	7 (37%)
Western Cape	27	4 (15%)	155			1 (4%)
Total	**150**	**37 (25%)**	**169**	**28 (19%)**	**51**	**27 (18%)**

Below are some examples of the infrastructure projects where we had found weaknesses.

Projects exceeded planned completion date and did not address backlogs

- Alfred Nzo District (Eastern Cape) – Ntabankulu wastewater treatment works (R39,6 million)

  The project was 17 months behind the original completion date. An extension of 194 days was recorded as having been granted, but no evidence to this effect could be provided. This moved the completion date to 3 January 2016. The construction of the multimillion rand project commenced without the availability of a water source, which meant that the project did not address the root cause of the sanitation backlog at the municipality. It further implies that this project would not be operational on completion, possibly resulting in fruitless and wasteful expenditure and the non-delivery of the promised services.

Projects over budget or with significant findings on supply chain management

- Bushbuckridge (Mpumalanga)

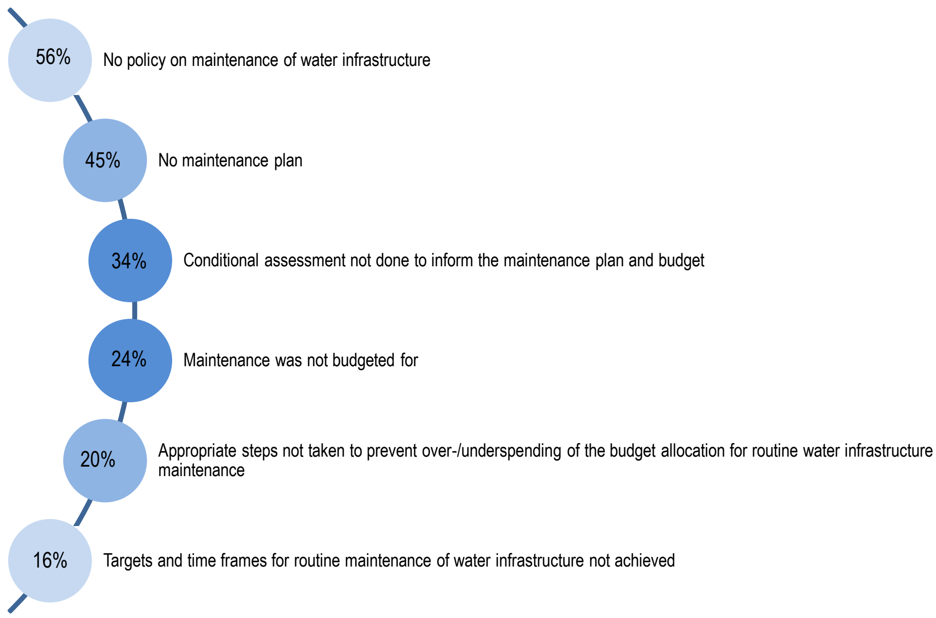
  Two contractors were unfairly awarded a tender for the provision of water supply infrastructure and borehole maintenance (turnkey projects), as they did not have the experience to do the project: they were consultants who would then have to appoint suppliers to do the work on their behalf. This largely contributed to the high irregular expenditure of R569 504 824 incurred by the municipality.

Section 4.2.1 provides further details on the most common SCM findings.

Maintenance of water infrastructure and extent of water losses

Maintenance is necessary to allow water infrastructure to be used over its full lifespan and to prevent water losses and poor quality of water. Figure 1 shows our key findings on the maintenance of water infrastructure at the 148 municipalities where we audited this.

Figure 1: Findings on maintenance of water infrastructure



Over half of the municipalities did not have basic policies and plans to ensure that maintenance took place. Even more concerning is that just over a third did not assess the condition of their infrastructure to determine when and where maintenance was required. Maintaining water infrastructure comes at a cost and the lack of budgeting for this at 24% of the municipalities is another indication that the maintenance of water infrastructure is being neglected. The municipalities in the Free State, the Northern Cape and North West had the most findings on infrastructure maintenance.

The following are examples of the result of poor maintenance:

- Kamiesberg (Northern Cape) – Garies bulk water infrastructure project

  The municipality did not have an approved policy that addressed the routine maintenance of water infrastructure, nor did they plan for the maintenance of water infrastructure by setting specific time frames and targets in this regard. The project began in 2016 to eradicate the use of sceptic tanks and ventilated pit latrines within the small towns around Garies. The servicing of septic tanks became increasingly demanding, particularly during the peak holiday season when the current sceptic tank system had to be emptied more frequently. This affected progress with no completion in sight.

- Mafube (Free State) – Qalabotjha wastewater treatment plant

  An amount of R35 845 709 had originally been budgeted for this project in 2012-13. The aim of the project was to alleviate the dire sanitation situation in Qalabotjha and Villiers and to assist in the eradication of 1 261 bucket toilets. This project has been delayed significantly, with the estimated cost escalating to R65 million. The contractor did poor quality work, as observed during our site inspection (e.g. steel structures and the steel ring enforcement were exposed and showed signs of corrosion). The municipality did also not perform proper feasibility studies and costing for the project. The following photos illustrate the absence of maintenance on the project.

- Ngwathe (Free State) – Phiritona sport complex

  The condition of the complex facility had not been maintained, as was evident during our site inspection. The complex had been completed more than a year ago at an approximate cost of R3,3 million, but had not been brought into use yet.

- Mahikeng (North West) – wastewater treatment plant

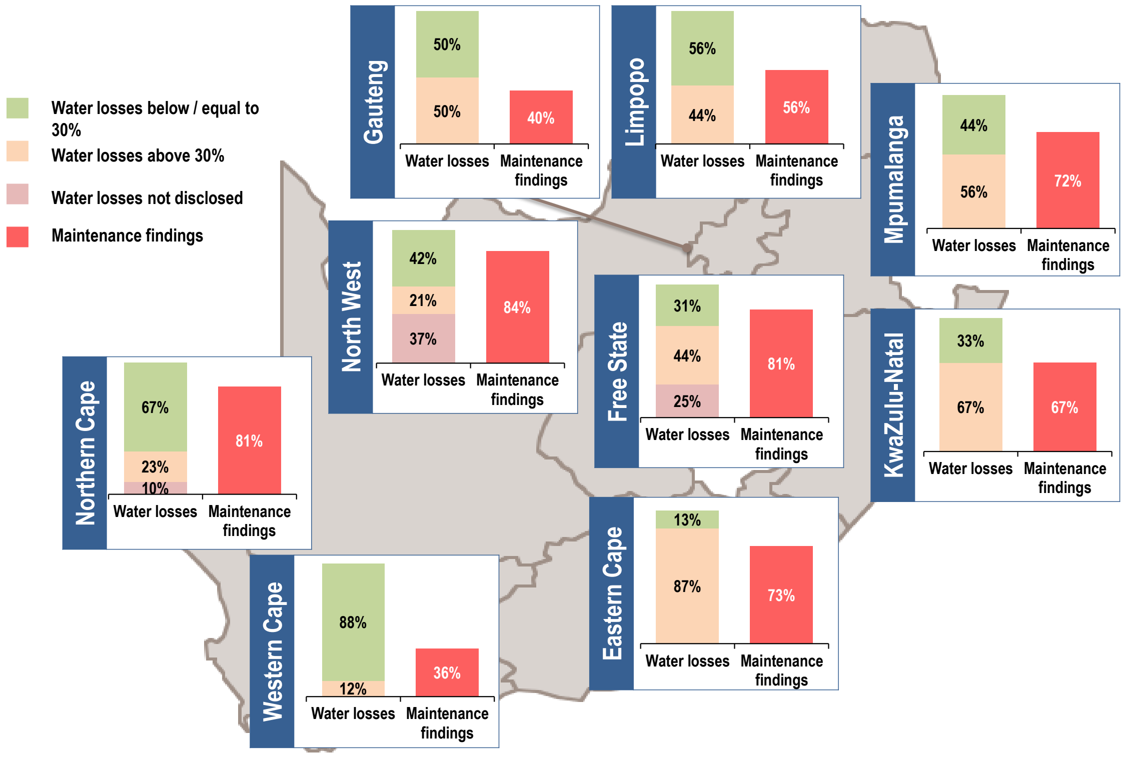
  Pumps and other equipment were out of order (in some instances for more than a year), while no cleaning or maintenance was evident. This resulted in wastewater overflowing and raw sewerage leaking directly into the river.

Water losses should be known, monitored and disclosed to enable municipalities to control and manage their losses and ultimately limit the loss of revenue and poor service delivery. The National Treasury introduced a target to limit water losses to below 30% in 2014.

Only 74 municipalities (50%) could keep their water losses below 30% in 2015-16. In total, 13 (9%) did not disclose their water losses in their financial statements as required. The water losses of the remaining 61 municipalities (41%) were on average 52% and ranged from 30,6% to 94%.

Figure 2 shows the occurrence of water losses and the percentage of municipalities that had maintenance weaknesses as listed in figure 1.

Figure 2: Water losses and the percentage of municipalities with weaknesses



The provision of sustainable water and sanitation services is at the core of service delivery to communities. Although funding is available to address the backlogs and the maintenance of infrastructure, the management thereof needs immediate attention at the municipalities authorised to provide these services.

5.3 Road infrastructure

The MTSF states that there will be a focus on ensuring that municipalities provide and properly maintain an adequate core set of basic services, including water, sanitation, electricity, municipal roads, refuse removal and traffic lights. According to the MTSF, government has expanded access to basic services over the past 20 years but backlogs remain and the quality of services is uneven.

According to a survey conducted in 2016 by the South African Institute of Race Relations, the country has approximately 535 000 kilometres of urban and non-urban roads that are managed by the different spheres of government. Local government therefore also has a role to play in managing the road network.

We again focused on **road infrastructure** during 2015-16 due to its importance for growth and development. Our audits focused on the planning, budgeting and delivery of road maintenance. We finalised the audits of 217 road authorities nationwide.

Municipalities made progress in addressing some of the challenges relating to the planning and budgeting of road maintenance, such as:

- performing condition assessments of infrastructure
- budgeting for routine maintenance of road infrastructure
- compiling an approved road maintenance plan or priority list for renewal and routine maintenance.

However, all nine provinces had municipalities where we again raised the same findings as in previous years, pointing to a **lack of consequence management** where corrective action had not been implemented. Figure 1 indicates the number of municipalities with findings on road infrastructure in the current and prior year, while figure 2 gives a provincial overview.

Figure 1: Progress at municipalities affecting the delivery of road infrastructure

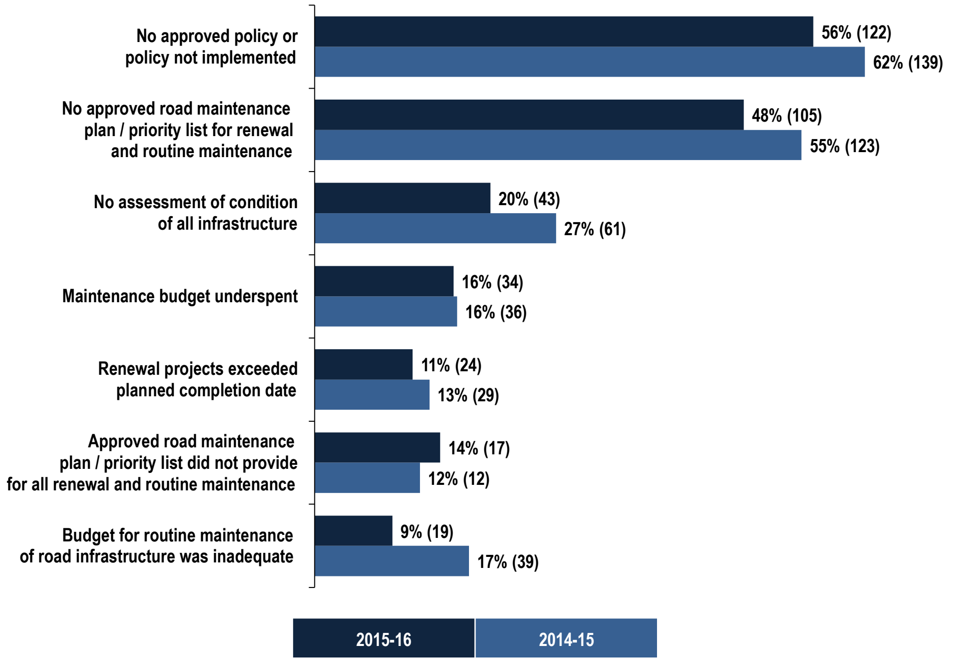
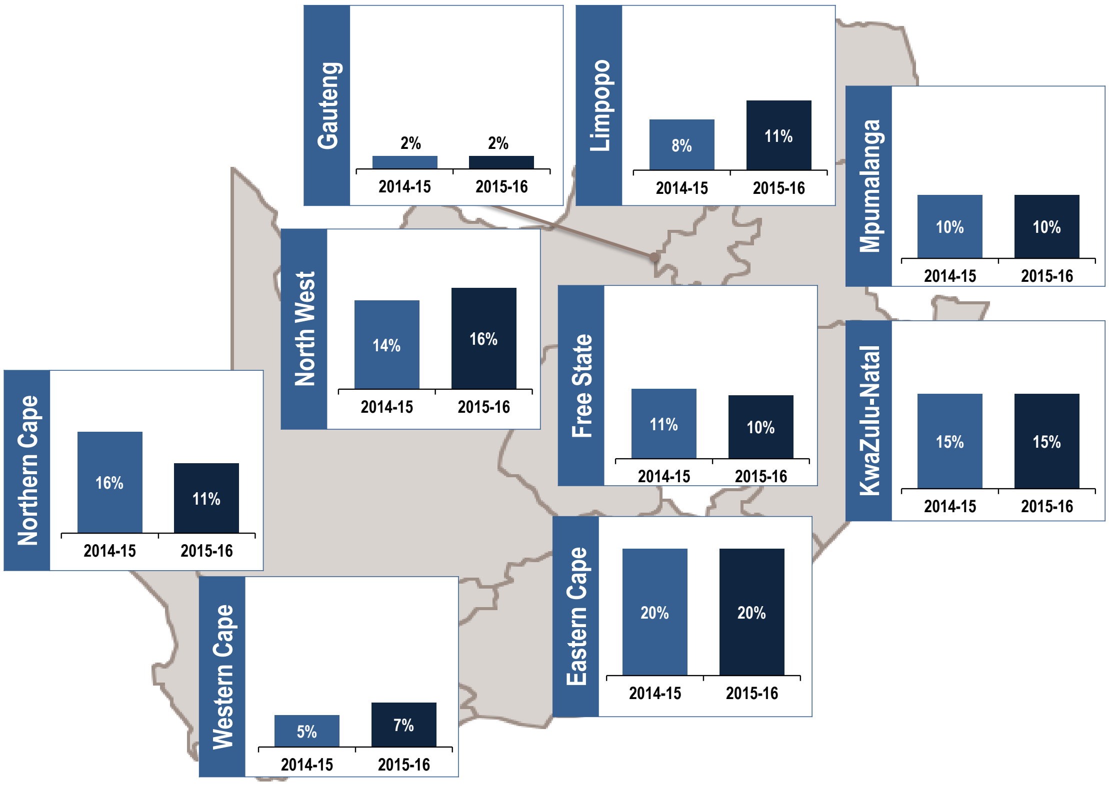


Figure 2: Provincial overview of findings affecting the delivery of road infrastructure



Policies are important to ensure proper planning and decision-making so that the desired outcomes are achieved for the management of road infrastructure. However, the main problem at 56% of the municipalities was that they had no approved policy or that the policy had not been implemented.

In addition, 48% of the municipalities did not have an approved road maintenance plan or priority list to inform the renewal and routine maintenance of road infrastructure. Furthermore, at 14% of those municipalities that had an approved maintenance plan or priority list, it did not provide for all renewal and routine maintenance.

Although there had been an improvement in conducting condition assessments, 20% of the municipalities still did not assess the condition of all road infrastructure to inform the road maintenance plan or priority list. This road maintenance plan or priority list is important to provide for all renewal and routine maintenance, as well as the allocation of adequate funds for maintenance activities.

The goal of maintenance is to **preserve the asset**. Unlike major road works, maintenance must be done regularly. Transport Note No. TRN-4 issued by the World Bank states that road maintenance comprises 'activities to keep pavement, shoulders, slopes, drainage facilities and all other structures and property within the road margins as near as possible to their as-constructed or renewed condition'.

At 16% of the municipalities, the **maintenance budget was underspent**. In addition, the budget for routine maintenance of road infrastructure was inadequate at 9% of the municipalities. According to the mentioned transport note, where road improvements and infrastructure are not maintained adequately, it may lead to further deterioration and result in high direct and indirect costs. This will affect the current backlogs, which will have an impact on service delivery. A lack of maintenance can also cause damage to vehicles and affect the safety of road users.

Furthermore, at 11% of the municipalities, the renewal and routine maintenance projects had exceeded their **planned completion dates** by between 2 and 529 days. This could result in an increase in project costs and a delay in the delivery of the project.

As also stated in the mentioned transport note, road improvements bring immediate and sometimes dramatic benefits to road users through improved access to hospitals, schools and markets; improved comfort, speed and safety; and lower vehicle operating costs. For these benefits to be sustained, however, road improvements must be followed by a well-planned programme of maintenance.

Conclusion

Sustainable improvements in performance management and service delivery can be achieved if the leadership clearly defines the targets to be achieved by using, among other, the new integrated development plan, service delivery and budget implementation plan, annual budget as well as maintenance and project plans (**PLAN**).

The basic disciplines of proper record keeping and standard daily and monthly controls built on a foundation of effective and efficient leadership and stability in key positions will enable a robust performance management system (**DO**).

Regular, credible in-year reporting monitored by, and acted upon, senior management, the municipal manager, the mayor as well as reports and recommendations on performance management from the internal audit unit and the audit committee will enable corrective action to be taken if targets are not achieved or if transgressions or poor performance is identified (**CHECK**).

Consistently investigating indicators or allegations of transgressions and poor performance and applying consequence management will ensure that a culture of accountability prevails (**ACT**).

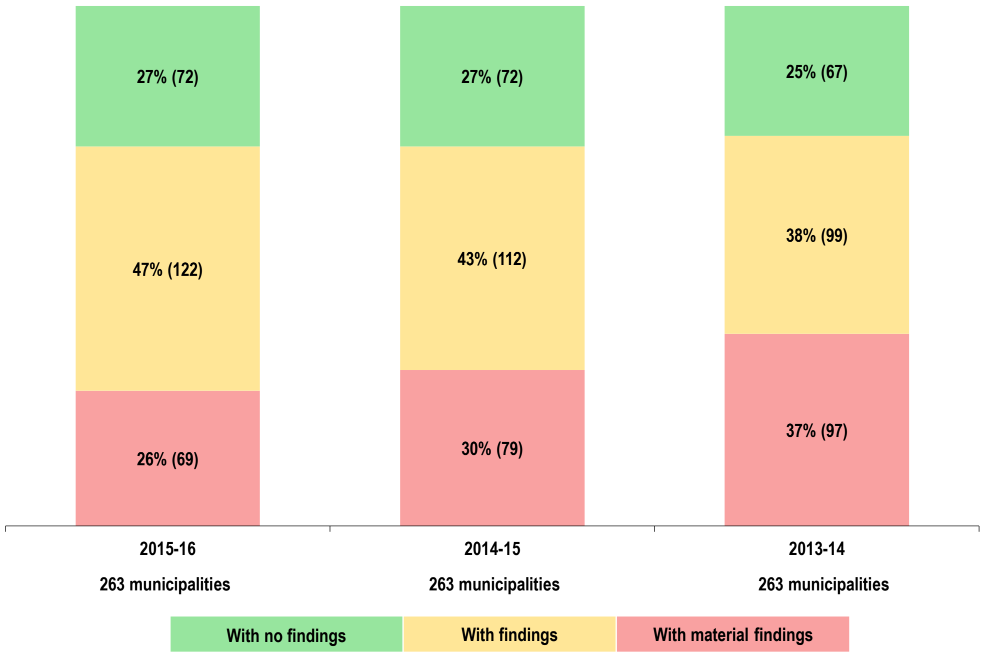
These improvements in performance management will enable better audit results, but more importantly contribute to a better life for all citizens **(IMPACT**).

6 Human resource management and the use of consultants

6.1 Human resource management

Figure 1 shows the status of HR management controls over the past three years.

Figure 1: Status of human resource management controls



At an overall level, the number of municipalities with HR management controls assessed as good was the same as in 2014-15 and those requiring intervention was slightly fewer. The improvements at 13 municipalities were offset by regressions at another 13, of which the majority were in KwaZulu-Natal (eight). These regressions can be attributed to vacant key positions not being filled.

One of the biggest challenges for local government, especially rural municipalities, is to attract and retain qualified and competent persons in all areas of administration. The remainder of this section provides more detail on these challenges.

Vacancies and stability

In the past two years, the average overall vacancy rate at year-end showed no movement – it was 20% in both 2015-16 and 2014-15. There was a slight regression in the **senior management vacancy rate** – from 19% in 2014-15 to 23% in the current year. This is consistent with our overall observation that the instability and uncertainties in 2015-16 caused by the elections and re-demarcation of municipal boundaries affected the vacancy rates and filling of positions at senior management level.

As part of our audits, we considered the vacancies and resourcing of finance units, as inadequate capacity in these units negatively affects the management, controls and quality of financial reporting. The **average vacancy rate in finance units** at year-end remained the same as in 2014-15 at 17%. In our assessment (based on vacancies and the skills of finance staff), the capacity of the finance units of 115 municipalities (44%) was either concerning or required intervention.

We also considered **vacancies in key positions** at year-end and **stability** in those positions. These key positions include municipal managers, CFOs, heads of SCM units and senior managers responsible for strategic planning and for monitoring and evaluation.

Figures 2, 4 and 6 provide a three-year overview of the number of municipalities where the positions of municipal manager, CFO and head of the SCM unit were vacant at year-end as well as the period that the positions had been vacant. They further show the average number of months the current incumbents had been in their positions.

Figure 2: Municipal managers – vacancy and stability

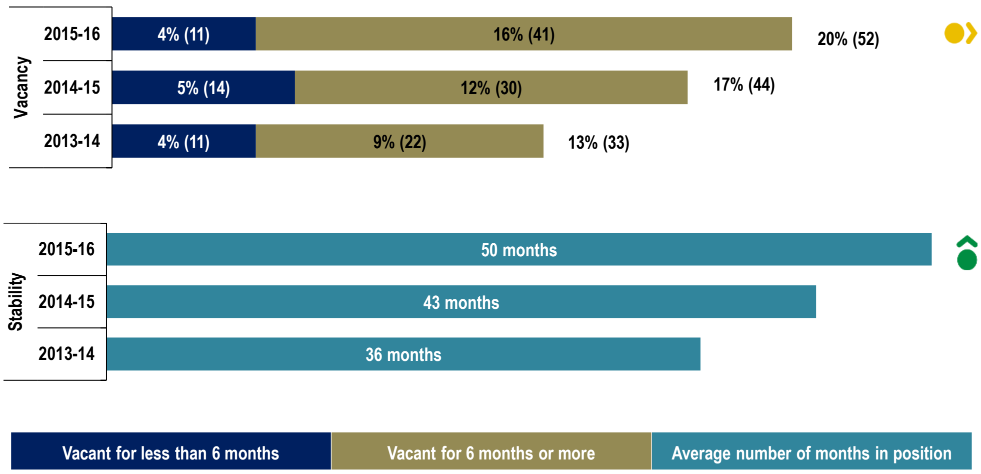
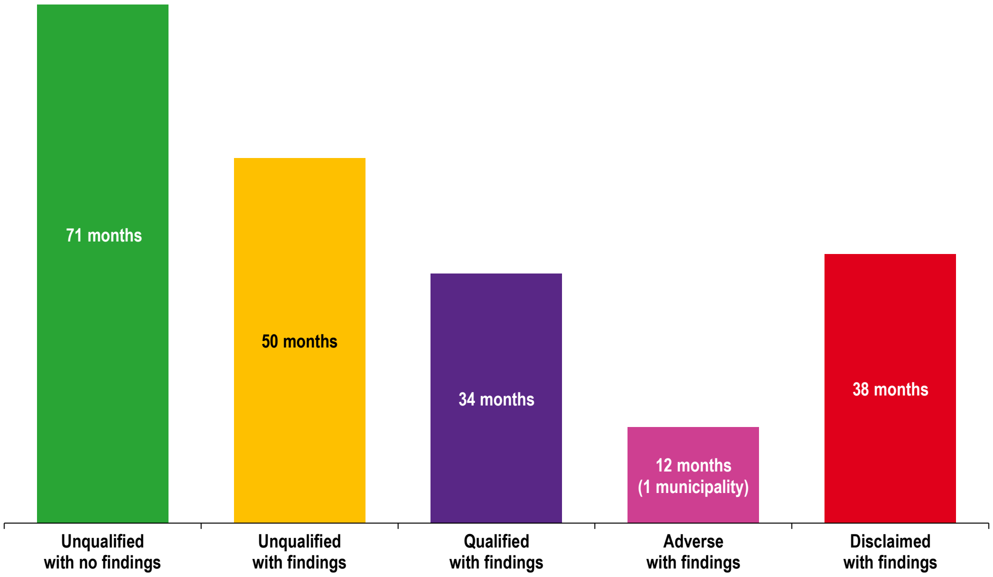


Figure 2 shows that the **municipal manager** vacancy rate had slightly increased from the previous year. Municipalities in North West (seven), the Western Cape (six) and the Northern Cape (seven) were the main contributors to the increased vacancies, which were mainly caused by contracts that came to an end and the re-demarcation of municipalities.

The average length of time that municipal managers had been in their positions was more than four years in 2015-16, which was an improvement from the previous year. By 2015-16, municipal managers at 100 municipalities (47%) had been in the position for four years or longer – a significant improvement compared to the 70 (32%) in 2014-15.

Figure 3 shows that those municipalities with increased stability at municipal manager level also achieved better audit outcomes.

Figure 3: Municipal managers – average number of months in position (per audit outcome)



The employment contracts of the municipal managers come to an end in 2016-17 and it is unlikely that the continuous improvement in stability will be maintained. It is expected that many contracts will not be renewed – especially where the political leadership has changed after the elections.

Figure 4: Chief financial officers – vacancy and stability

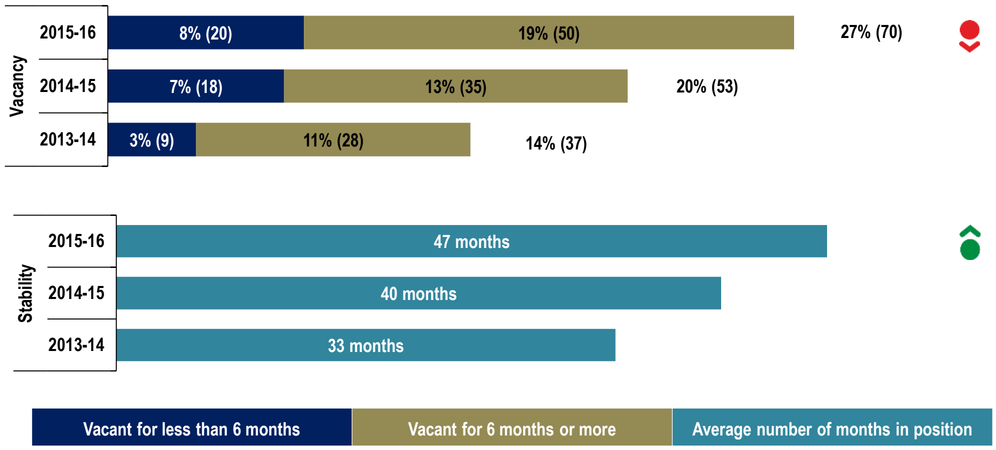
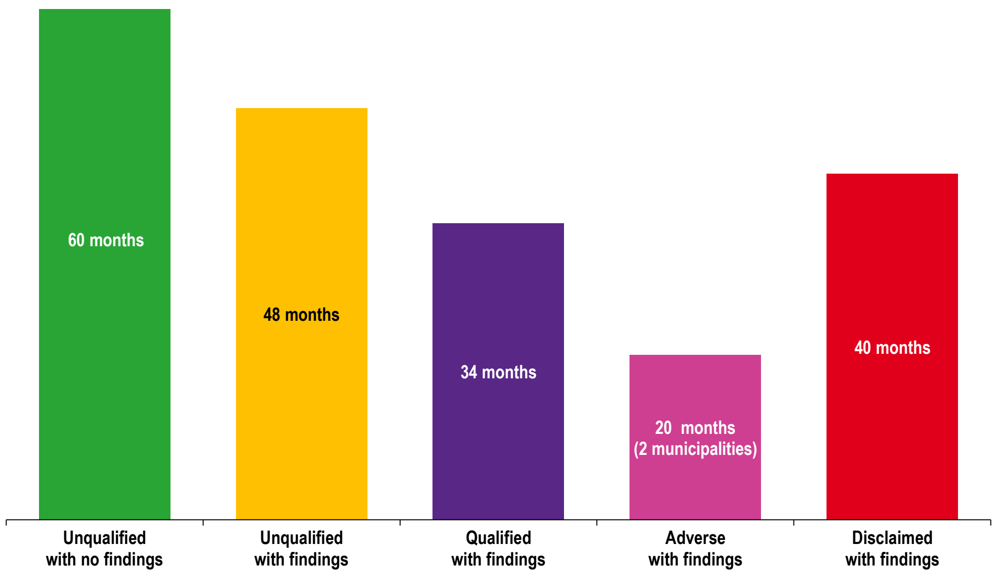


Figure 4 shows that the **CFO** vacancy rate at municipalities had increased from the previous year. Municipalities in Mpumalanga (four), North West (four) and Gauteng (two) were the main contributors to the regression. The regression can in part be attributed to financial constraints at municipalities, resignations due to the re-demarcation of municipalities, inadequate succession planning, and challenges in attracting skilled individuals by rural municipalities.

The average number of months that CFOs had been in their positions had improved from the previous year. By 2015-16, CFOs of 110 municipalities (57%) had been in the position for three years or longer. This is a significant improvement compared to the 84 (40%) in the previous year.

Figure 5 shows that those municipalities with stability in their CFO positions produced better financial statements or audit outcomes (based on the outcomes).

Figure 5: Chief financial officers – average number of months in position (per audit outcome)



Although the employment contracts of most of the CFOs also come to an end in 2016-17, changes in the political leadership should not affect the renewal of the contracts as this is not a political post. However, we foresee that the stability in these positions could be affected at some municipalities.

Figure 6: Heads of supply chain management units – vacancy and stability

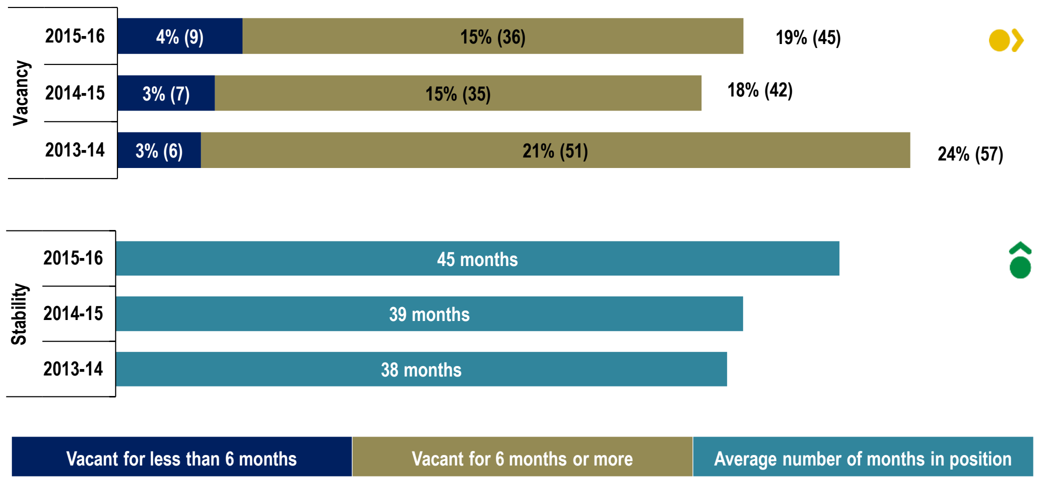


Figure 6 shows that the vacancy rate for **heads of SCM units** at municipalities had slightly regressed since the previous year. In 2015-16, 23 municipalities did not have a dedicated position for this role, with the work being performed mostly by the CFO.

The average number of months that the heads of SCM units had been in their positions had improved since the previous year. By 2015-16, heads of SCM units at 94 municipalities (48%) had been in the position for three years or longer – an improvement compared to the 80 (40%) in 2014-15.

Senior managers responsible for **strategic planning and/or monitoring and evaluation** are crucial for effective strategic planning and performance monitoring as well as credible and reliable performance reports.

Although not all municipalities had a specific position for strategic planning or to perform the monitoring and evaluation function, 211 municipalities (80%) had a senior manager responsible for strategic planning and 196 (75%) for monitoring and evaluation. It is concerning that not all municipalities had allocated these very important functions to senior managers to oversee. The vacancies at year-end in these positions were 14% (30) for senior managers responsible for strategic planning and 14% (27) for those responsible for monitoring and evaluation. This is a slight regression from the 12% (26) and 12% (22) at the end of 2014-15, respectively.

Competencies and skills

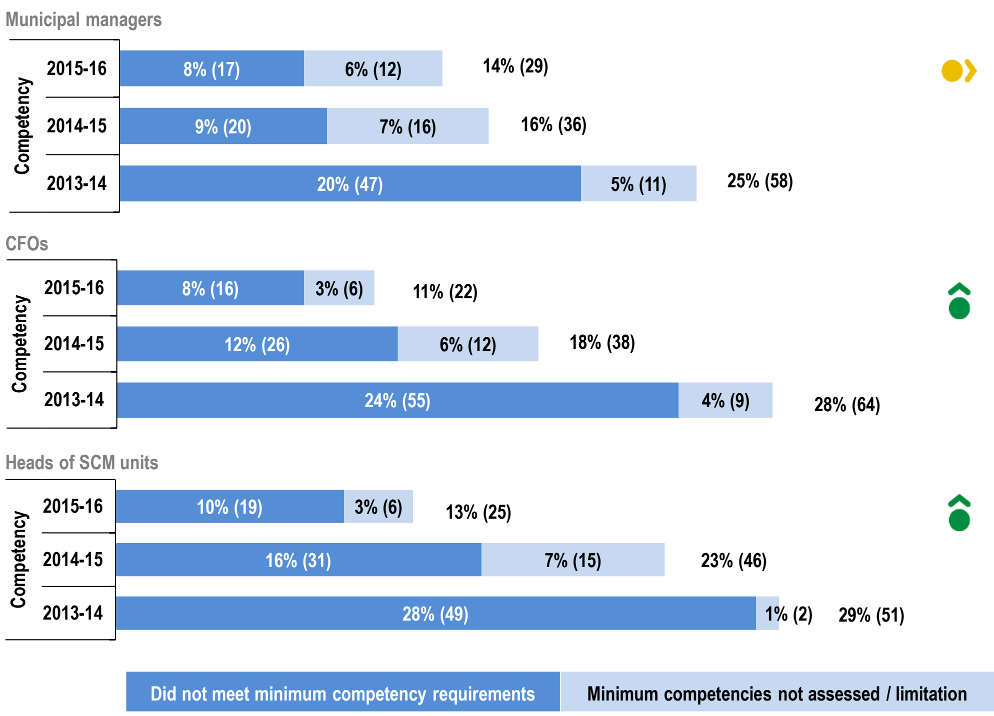
The **minimum competency levels** for accounting officers, CFOs, senior managers, SCM officials and other finance officials are prescribed by the Municipal Regulations on Minimum Competency Levels issued by the National Treasury on 15 June 2007. These regulations define the minimum competency levels, taking into account the size and scope of municipalities, and cover proficiency in competency areas, higher education qualifications and work-related experience.

The regulations provided for a phasing-in period for staff currently in those positions to obtain the minimum competency levels through academic studies and experience and by addressing any gaps in competencies through training and development. The phasing-in period ended on 1 January 2013 and, as per the regulations, municipal managers, CFOs, heads of SCM units, senior managers, SCM staff and other finance officials who failed to meet the minimum competency levels could not continue to fill the positions, which had an impact on the continued employment of these officials. After a number of extensions, the National Treasury granted municipalities a further extension on 3 February 2017, giving municipalities an additional 18 months.

The information on the competencies of key officials that follows is based on municipalities' own assessment of the achievement of the competency requirements by their key officials.

Figure 7 provides a three-year overview of the number of municipalities where key officials had failed to meet the prescribed minimum competency requirements at year-end. It also shows the number of municipalities where the officials' competencies were not assessed by the municipality as required by legislation, or where we could not obtain evidence of a competency assessment.

Figure 7: Achievement of competency requirements by key officials



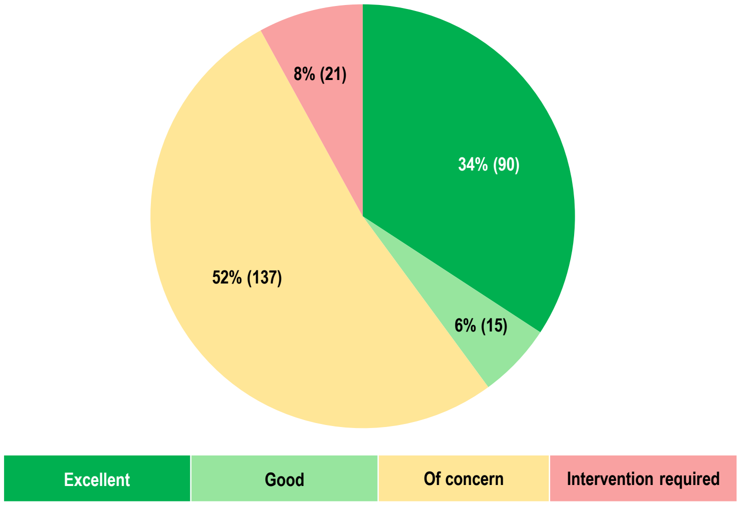
As can be seen in figure 7, there had been an improvement in the number of key officials with the required competency since the previous year, although only slightly so for municipal managers. Only a few officials in these positions were still not at the required level or had not been assessed. The reason for the overall improvement was mainly the appointment of officials with the required minimum competency (in adherence to the legislation) and incumbents obtaining the competencies to avoid their employment being terminated or not having their contracts renewed if they did not meet the minimum competencies.

Considering the reliance municipalities still place on auditors to identify and help with the correction of misstatements (as discussed in section 4.1) and on consultants to assist with financial reporting (as discussed in section 6.2), the question comes up whether **financial management skills** at municipalities still remain a challenge.

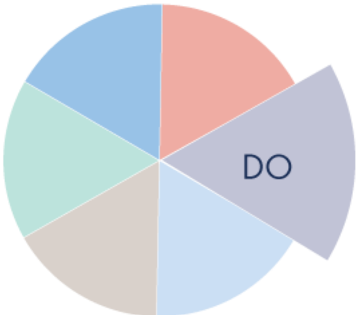
To answer this question, we considered the following criteria: our assessment of the capacity of the finance units, whether the CFO positions were filled, and municipalities' assessment of whether their CFO and financial officials had obtained the required minimum competencies.

Figure 8 shows the outcome of our assessment.

Figure 8: Financial management capacity



In our assessment, the financial management skills of 158 municipalities (60%) were either concerning or required intervention. The provinces with the highest percentage of municipalities with problems relating to their financial management skills were North West (82%), Mpumalanga (76%) and the Free State (70%).



Good HR management practices are a foundation for strong internal controls, as vacancies and inadequate skills affect the establishment, execution and monitoring of control activities.

A Annexure 1 lists all auditees and the status of their HR management controls.

6.2 Effective use of consultants

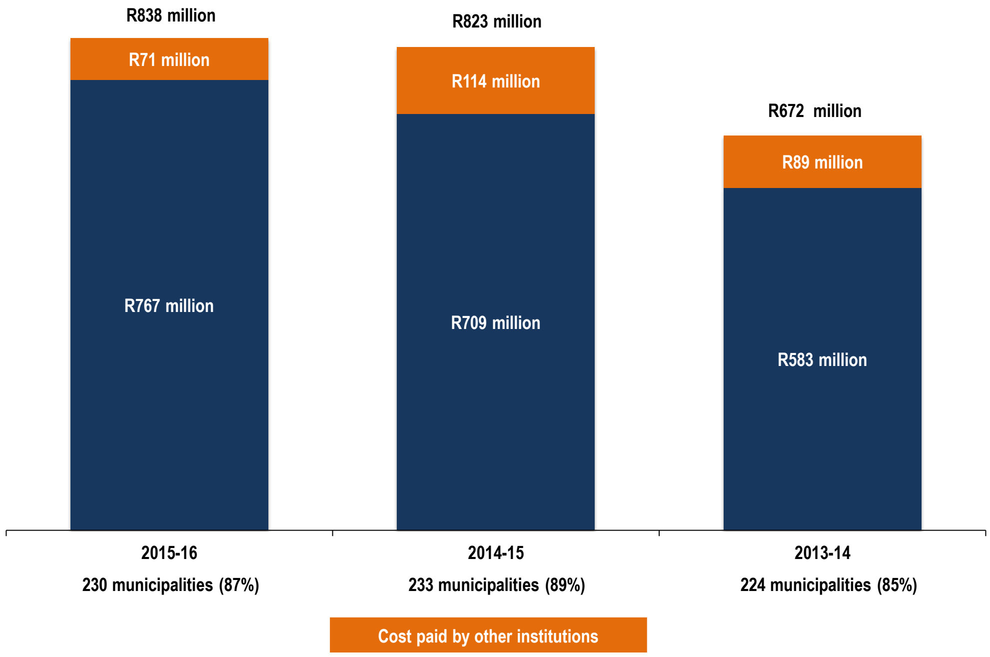
In 2015-16, local government spent an estimated R3 500 million on consultancy services. The amount was spent in the following areas:

- Financial reporting services – R838 million (including R71 million paid by the provincial treasuries and provincial Cogtas on behalf of municipalities)
- Preparation of performance information – R33 million
- IT services – R590 million
- Other services – R2 038 million

Financial reporting services

Figure 1 shows the number of municipalities that used consultants for financial reporting services and the cost thereof over three years.

Figure 1: Consultants used for financial reporting

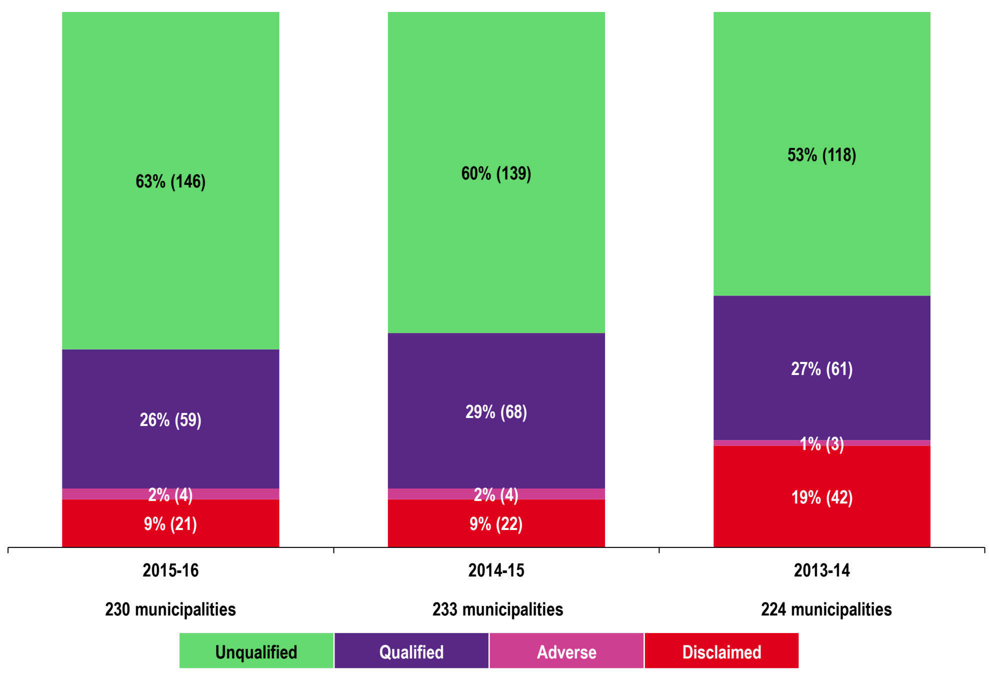


The **number of municipalities assisted by consultants** had slightly decreased from the previous year and the **consultants' costs** had increased by only 2%. The use of consultants' services was most common in Limpopo (96% of the municipalities), the Northern Cape (92% of the municipalities) and North West (91% of the municipalities).

The most common **reason why consultants were appointed** was a lack of skills (60%), a combination of a lack of skills and vacancies (34%), and vacancies only (5%). Of the 230 municipalities assisted in 2015-16, 220 (96%) had also used consultants in 2014-15. A total of 202 municipalities (88%) had used consultants for the past three years.

The audit outcomes of municipalities assisted by consultants since 2013-14 are shown in figure 2.

Figure 2: Audit outcomes of municipalities assisted by consultants – financial reporting



The **audit opinions on the financial statements** of the municipalities assisted by consultants had slightly improved since the previous year. The audit opinions of 162 assisted municipalities (70%) had remained unchanged since the previous year, with 38 (17%) improving and 30 (13%) regressing. Of the 25 municipalities that received an adverse or disclaimed audit opinion in 2015-16, all of them had also used consultants in 2014-15 and 88% had done so since 2013-14.

The audit opinion on the financial statements cannot always be attributed to consultants, as they might not have done work in the specific areas that led to the poor audit opinion. However, we found that at 130 municipalities (57%) (2014-15: 146 [63%]), the financial statements submitted for auditing included **material misstatements** in the areas in which consultants did work, which meant that the misstatements were identified and corrected by the audit process and not by the consultants. This remains a concern regarding the effective use of these consultants.

Our audits also included gathering information on the **reasons why financial reporting consultants were ineffective** at some municipalities. We identified the following reasons:

- Auditee ineffectiveness – 42 municipalities (18%) (2014-15: 46 [20%])
- Poor project management – 34 municipalities (15%) (2014-15: 27 [12%])
- Lack of records and documents – 25 municipalities (11%) (2014-15: 30 [13%])
- Poor delivery by consultants – 15 municipalities (7%) (2014-15: 24 [10%])
- Consultants appointed too late – 14 municipalities (6%) (2014-15: 19 [8%])

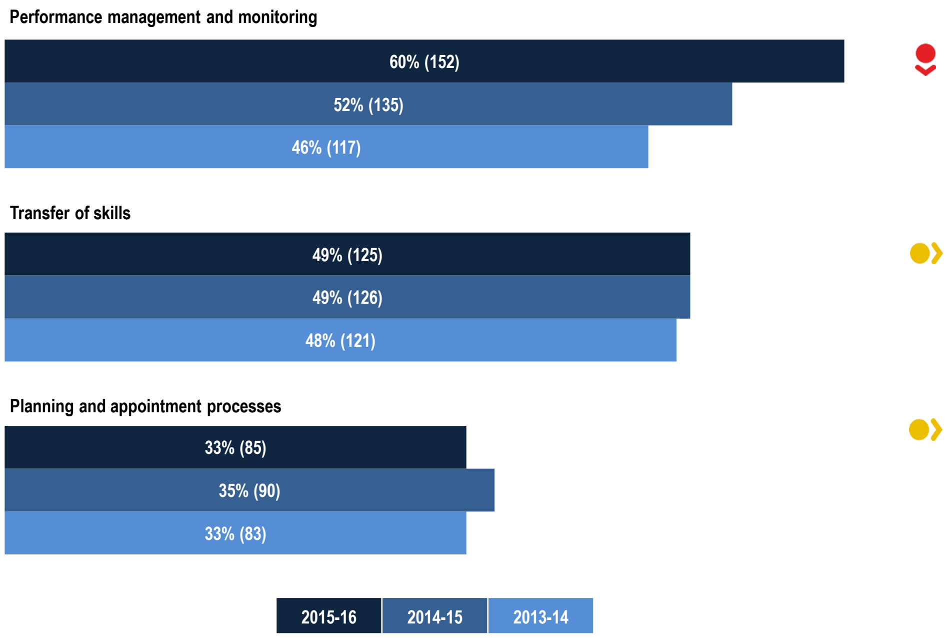
The discussion on the management of consultants provides further insight into the reasons for the ineffective use of consultants.

Management of consultants

We identified weaknesses in the management of consultants at 178 (70%) of the municipalities that used consultancy services (not limited to financial reporting services) – a regression from the 166 municipalities (64%) in the previous year.

Figure 3 shows the number of municipalities that had findings in the different focus areas of the audit on consultants since 2013-14.

Figure 3: Findings arising from the audit on the use of consultants



There had been little movement from the previous year in any of the focus areas, except the municipalities with findings on performance management and monitoring processes that had regressed since the previous year.

The following were our key findings on **performance management and monitoring:**

- The measures to monitor contract performance and delivery were not defined and/or implemented – 82 municipalities (32%) (2014-15: 86 [33%]).
- No evaluation was performed to determine whether the consultancy services rendered met the initial project objectives, needs and deliverables – 36 municipalities (14%) (2014-15: 41 [16%]).
- The measures to monitor delivery on the consultancy project were inadequate, as they failed to detect underperformance by consultants – 33 municipalities (13%) (2014-15: 41 [16%]).
- The contract of the consultant did not stipulate the terms and conditions for the termination of the contract in the case of non- or underperformance – 28 municipalities (11%) (2014-15: 28 [11%]).

The following were our key findings on the **transfer of skills:**

- The transfer of skills was a requirement of the contract but no evidence could be provided that skills had been transferred or that training had taken place – 101 municipalities (40%) (2014-15: 99 [38%]).
- The measures to monitor the transfer of skills in accordance with the contract were not implemented – 80 municipalities (31%) (2014-15: 78 [30%]).
- The requirements for the transfer of skills were not included in the terms of reference – 65 municipalities (26%) (2014-15: 66 [26%]).
- The employees to be trained were not identified or available to attend the training programme – 64 municipalities (25%) (2014-15: 65 [25%]).
- Conditions or clauses relating to the transfer of skills were not included in the contract – 63 municipalities (25%) (2014-15: 81 [31%]).

The following were our key findings on **planning and appointment processes:**

- Consultants were appointed without conducting a needs assessment – 65 municipalities (26%) (2014-15: 59 [23%]).
- Consultants were appointed without any terms of reference – 34 municipalities (13%) (2014-15: 30 [12%]).
- The terms of reference were inadequate – 19 municipalities (7%) (2014-15: 23 [9%]).

Mayors, councils as well as national and provincial role players should pay attention to the management of consultants to ensure that this expensive resource is procured economically and used effectively and efficiently. Having clear targets for consultants to achieve (**PLAN**), allowing them adequate time to perform the required functions for which they were appointed (**DO**), monitoring the achievement of the targets (**CHECK**), and addressing any lack of performance timeously (**ACT**) will have the desired result.

7 Information technology controls

7. Information technology controls

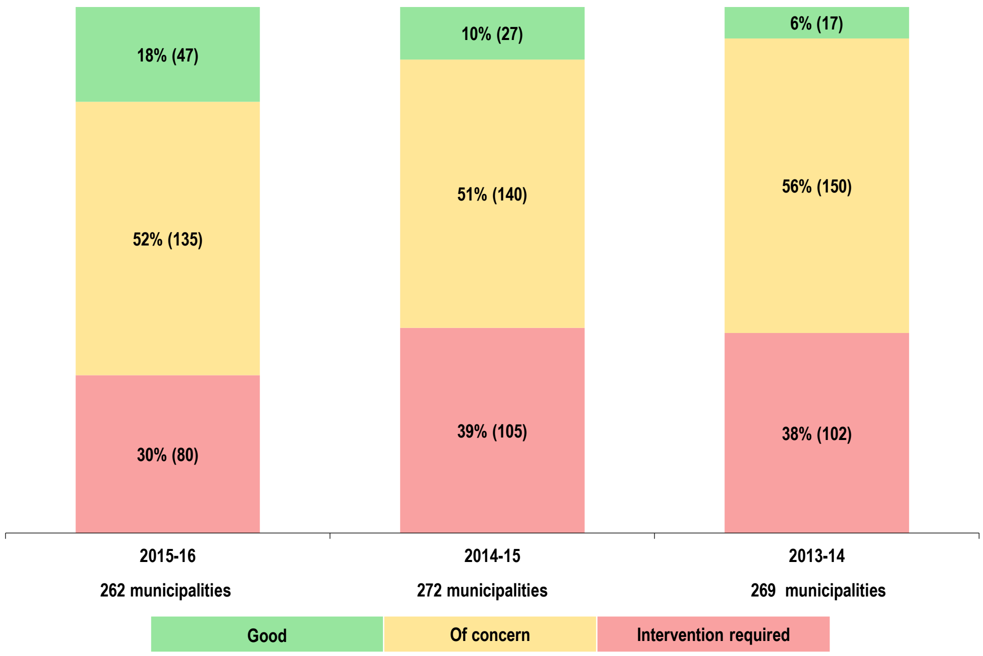
An inherent part of the control environment in municipalities is the status of their IT controls. IT controls ensure the **confidentiality, integrity and availability** of state information, enable **service delivery** and promote **security** in local government. It is thus essential for good IT governance, effective IT management and a secure IT infrastructure to be in place.

Effective IT governance underpins the overall well-being of a municipality's IT function and ensures that the municipality's IT control environment functions well and enables service delivery.

Overview of the status of information technology focus areas

Figure 1 shows the status of IT controls since 2013-14.

Figure 1: Status of information technology controls



We assessed IT controls at 262 municipalities and found that the number of municipalities that had good IT controls in place increased significantly from 10% in 2014-15 to 18% in 2015-16. The improvements were generally due to the capacitating of, and increase in support to, municipalities by coordinating departments. We had assessed 272 municipalities in 2014-15.

Our audits included an **assessment of the IT controls** in the areas of **security management, user access management** and **IT service continuity**. Figure 2 outlines the status of the controls in the areas we audited and indicates, per focus area, whether the IT controls were good, concerning or required intervention.

Figure 2: Information technology focus areas

There had been an improvement over the two years in all focus areas, with a significant decrease in the number of municipalities where intervention was required, indicating that municipalities were moving in the right direction.

Table 1 indicates the **progress made** since the previous year in addressing areas of concern at municipalities. The improvements were generally due to the following:

- **Coordinating departments** were playing a pivotal role in capacitating and supporting municipalities.
- More municipalities were employing CIOs or IT managers with **adequate qualifications and experience**.
- Municipalities **implemented some of the recommendations** made by internal and external auditors.

Table 1: Progress made in improving information technology controls

Province	Security management	User access management	IT continuity
Eastern Cape	↑	↑	↑
Free State	↑	↑	↑
Gauteng	↑	↓	↑
KwaZulu-Natal	↑	↑	↑
Limpopo	↑	↓	→
Mpumalanga	↑	↓	↑
Northern Cape	↑	↓	↑
North West	→	↑	↑
Western Cape	↑	↑	↑

The most common findings were the following:

- Most of the metros remained concerning or required intervention, while the City of Johannesburg Metro and Ekurhuleni Metro regressed from the previous year. This was due to some metros still experiencing challenges to fill vacancies in key positions, such as those of the CIO and specific positions within the IT section. Furthermore, some metros were still experiencing weaknesses in internal control. This included not establishing an IT governance framework, isolated security vulnerabilities, IT steering committees being inactive, action plans not being implemented and monitored, and disaster recovery plans not being tested to ensure the recovery of data in the event of a disaster.
- Although municipalities were moving in the right direction and there had been an improvement over the two years in all areas, a number of municipalities still had not adequately defined and implemented basic IT controls in the security management, user access management and IT service continuity areas. The regression in user account management in Limpopo, Mpumalanga and the Northern Cape was mainly due to inadequate management oversight to ensure that prior year commitments had been implemented. Policies and procedures were not designed or implemented, as also reported in the previous year. Some municipalities experienced security breaches as security controls were compromised, resulting in fraudulent activities. Some municipalities were still highly dependent on IT service providers and in many instances their performance was not monitored to ensure the agreed-upon level of quality was delivered. System administrator activities and user access rights were not always reviewed and the segregation of duties was not in all instances maintained. Furthermore, the management of backups remained a challenge, as most of the municipalities did not test their backups to ensure that they could be restored when required.

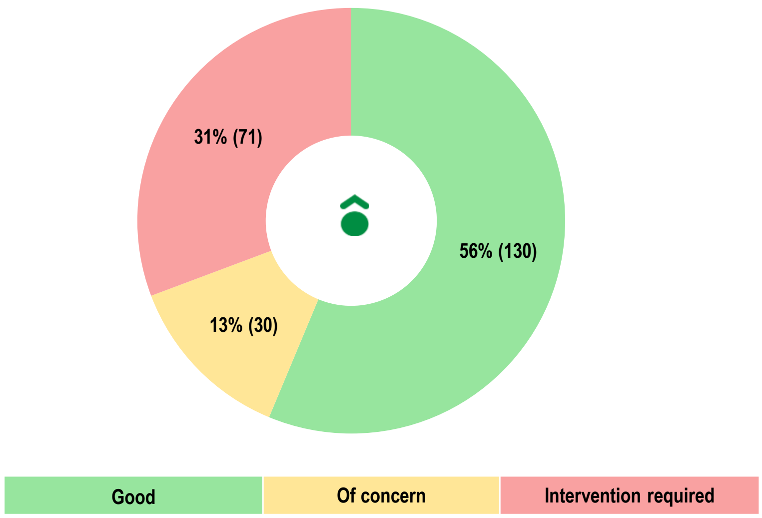
The challenges experienced with regard to adequate security management, user access management and IT service continuity were made worse by the following factors:

- Municipalities experienced budget constraints, which limited the development of IT policies and procedures. In other instances, already developed IT policies and procedures were still awaiting approval from management and the council.
- Service level agreements with vendors did not include the management or development of IT policies and procedures.
- District municipalities did not provide adequate guidance and support to the local municipalities under their jurisdiction.
- Staff did not fulfil their responsibilities in terms of ensuring compliance with the controls established to secure and regulate municipalities' IT environments. Moreover, they were not held accountable for failing to address previously raised findings.

Evaluation of qualifications and experience of chief information officers or information technology managers

Figure 3 indicates that, for most of the municipalities, the **qualifications and experience of CIOs or IT managers** in local government had improved from the previous year and were adequate, which meant that they had relevant information and communication technology qualifications and six or more years of relevant experience.

Figure 3: Qualifications and experience – chief information officers or information technology managers



Overall, 56% of municipalities employed CIOs or IT managers with the necessary qualifications and experience to implement the IT governance structures and controls and to ensure an improvement in IT controls. Where municipalities employed CIOs or IT managers with adequate qualifications and experience, it had a positive impact on the improvements over the two years.

The municipalities where intervention was required in many instances had **failed to fill the position**. However, some municipalities still **did not have an approved position** for this function on the organisational structure. In such instances, municipalities made use of consultants to ensure that IT roles and responsibilities were fulfilled; however, the performance of consultants was not monitored closely. Furthermore, it was a concern that although these positions had been filled at some municipalities, the CIO or IT manager did not have the appropriate qualification and/or years' experience required for the position. The above may have contributed to the areas of concern and where intervention was required with regard to IT controls.

Information technology support provided by coordinating departments

Coordinating departments play a pivotal role in **capacitating and supporting municipalities**, especially in respect of the implementation of mSCOA. The roles of each coordinating department are interlinked, but with a clear indication of the support to be provided.

Table 2 indicates whether these coordinating departments provided support to municipalities.

Table 2: Support provided to municipalities by coordinating departments

Province	Provincial Cogta	Provincial treasury	Office of the premier
Eastern Cape	No	Yes	No
Free State	Yes	Yes	Yes
Gauteng	No	No	No
KwaZulu-Natal	Yes	Yes	No
Limpopo	Yes	No	Yes
Mpumalanga	Yes	Yes	Yes
Northern Cape	Yes	No	Yes
North West	Yes	No	Yes
Western Cape	Yes	Yes	Yes

The **DCoG** established an information and communication technology think tank made up of officials from the National Treasury, departments of cooperative governance, the State Information Technology Agency, the Department of Public Service and Administration and our office (as an observer), as previously reported. However, the structure did not function during the latter part of 2015-16. Provincial Cogtas supported their municipalities in at least seven of the nine provinces as indicated in table 2, but in some provinces they did not have adequate capacity to effectively support all municipalities.

The **offices of the premier** continued to invite municipalities to attend **meetings of the provincial government IT officers** and are rolling out processes that will provide assistance to municipalities that are struggling with the implementation of IT controls.

The **National Treasury** issued guidance through MFMA SCOA circulars and rolled out accredited training initiatives on mSCOA implementation. Provincial treasuries are responsible for providing budgetary assistance to municipalities and for facilitating arrangements for non-accredited mSCOA training sessions.

We recommend that the coordinating departments that have not supported municipalities as indicated in table 2, take the following actions:

- Provincial Cogtas should strengthen their capacity to effectively support the municipalities in all provinces.
- All coordinating departments should share their supporting strategies across provinces so that they can leverage on each other's success.

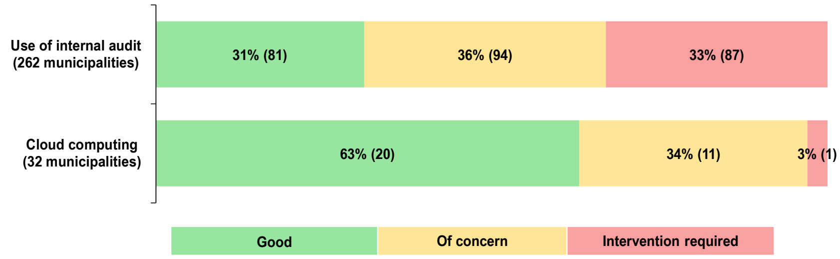
Information technology health within local government

Municipalities should (i) perform their operations in a secure IT environment, (ii) operate effective financial systems to enable the presentation of credible information on a timely basis for internal and external use, and (iii) enable their internal audit functions to provide the level of assurance required by those charged with governance.

We therefore assessed IT health within local government at municipalities by focusing on the IT audit skills within internal audit units as well as cloud computing.

Figure 4 indicates the results of these assessments.

Figure 4: Information technology health within local government

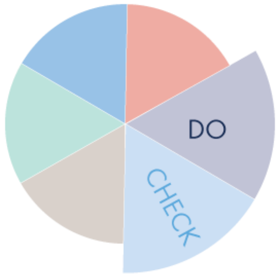


We assessed the **internal audit units** of municipalities and found that 31% of these municipalities had an internal audit function that performed IT audits, while 36% of them were assessed as concerning as they had the capacity to perform IT audits, but were not yet performing this function. Most municipalities therefore had sufficient capacity in their internal audit function to evaluate their internal controls in the IT environment, perform risk management, and evaluate governance processes to provide the assurance required by management.

Cloud computing and storage solutions are an emerging technology that provides municipalities with various capabilities to store and process their data in third-party data centres that may be located far from the municipality or even outside the country. We found during our assessment that most municipalities were not yet utilising cloud computing, with only 32 indicating that they were making use of these services. From these few municipalities, we further found that 63% of them had adequate internal controls to manage this environment, while the remaining municipalities were concerning or required intervention. The latter is of concern, as the following are some of the business risks associated with cloud computing:

- Sharing resources increases the risk of private information leaking to others in the cloud.
- The unavailability of data and services may have an impact on the business of the municipality.
- Security may be breached with shared access control, while the risk of unprotected data may increase.
- Cloud providers may become the owners of the data, as this could be included as a clause in the agreements between cloud providers and municipalities.

We also assessed the readiness of municipalities to use the **central supplier database** and to start inviting bids through the **eTender portal**. Refer to section 4.2.1 on the readiness for SCM reforms for more detail on the results of the assessment.



As the majority of financial management controls are automated and monitoring takes place mostly on reports generated by the IT systems, good IT controls and skills are fundamental to enabling robust financial management systems (**DO**) and in-year monitoring (**CHECK**).

NOTES

8 Support to local government

8. Support to local government

The DCoG has been allocated critical roles and responsibilities in terms of outcome 9 of the MTSF, which seeks to bring about a responsive, accountable, effective and efficient developmental local government system. The DCoG, its provincial counterparts and the Municipal Infrastructure Support Agent (Misa), which is a government component of the DCoG, are to play a pivotal role in creating an enabling environment for local government to flourish, and to provide a context for oversight and support to municipalities.

We assessed these departments to determine whether they have implemented or put processes in place to ensure that the relevant monitoring and support initiatives as envisaged per the revised chapter 9 of the MTSF can – or will – be achieved.

The revised chapter 9 of the MTSF constitutes the strategy and contains the proposed initiatives to be implemented by the DCoG with respect to support to local government, and forms the basis of the sector audit procedures that we performed. We discuss the progress towards the implementation of the sub-outcomes of the revised MTSF initiatives (pertaining to the support to local government) in the rest of this section.

Progress towards the implementation of the revised Medium-Term Strategic Framework initiatives pertaining to support to local government

Sub-outcome 1: Members of society have sustainable and reliable access to basic services

According to the revised chapter 9 of the MTSF, the core focus and purpose of sub-outcome 1 is to ensure that 'members of society have sustainable and reliable access to basic services'. Access to services is constrained by a number of factors, not least the absence of sound asset management in the local government sphere. The high replacement cost of municipal assets makes it necessary to emphasise the critical importance of effective asset management and care in local government.

Programme management office

A programme management office comprising sector departments (Water and Sanitation, Energy, Environmental Affairs, and Transport) as well as the National Treasury, the Department of Planning, Monitoring and Evaluation (DPME), the DCoG and Misa is to be established to **oversee and coordinate** various matters relating to service delivery, such as new infrastructure projects and maintenance interventions. The DCoG indicated that a programme management office had been established and that the roles and responsibilities of each sector department had been clearly defined; however, evidence to corroborate the establishment and proposed functioning of the programme management office was not provided.

Municipal asset management

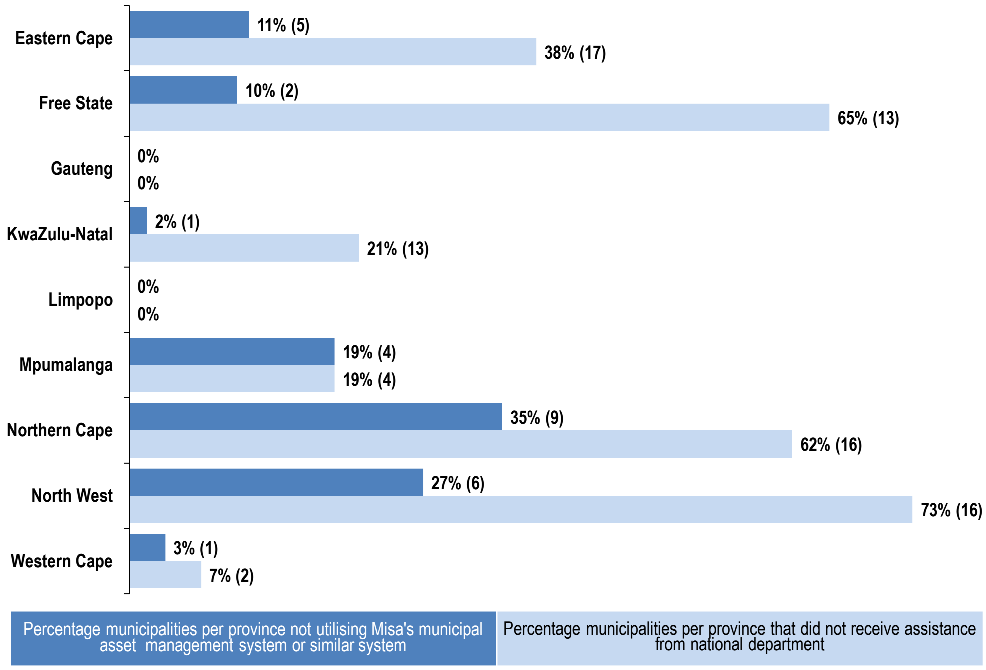
Municipalities are to be encouraged to increase their expenditure on maintenance and asset management over the life cycle of the asset. The following indicator was included in the 2015-16 annual performance plan of **Misa**: *Number of municipalities supported to develop, review and implement operations and maintenance plans, including spending of minimum 7% of the budget for operational expenditure*. Although Misa indicated in their performance report that this indicator had been achieved and that the targeted 21 municipalities received this support, we were unable to verify the actual achievement reported with regard to the operations and maintenance plans. Additionally, Misa was unable to reliably measure the operational expenditure spending given that the indicator and target had not been well defined upfront. Sections 5.2 and 5.3 detail the limited spending on maintenance during the 2015-16 financial year, including the fact that 50% of municipalities did not have maintenance plans, highlighting the need to enhance and expedite support initiatives in this area.

Support by national Department of Cooperative Governance

Municipalities are to be supported by the DCoG to establish municipal asset management systems. To this effect, the Municipal Infrastructure Performance Management Information System was developed under the control of Misa for implementation by municipalities in 2015-16. Implementation was largely successful, as only 28 municipalities had not implemented Misa's municipal asset management system or a similar system for purposes of asset management. However, support is still clearly required to ensure that these systems are effectively utilised to improve asset management in local government.

Figure 1 depicts the percentage and number of municipalities per province that did not utilise this or a similar system for **asset management**. It also depicts the percentage and number of municipalities per province that did not receive assistance from the DCoG with regard to Misa's Municipal Infrastructure Performance Management Information System or another similar system that serves the same purpose.

Figure 1: Percentage of municipalities per province not utilising municipal asset management systems and that did not receive related assistance from the national department



Delivery of basic services

Municipalities are to be supported by national and provincial cooperative governance departments, provincial treasuries and the National Treasury to improve their ability to deliver services. A total of 45 municipalities (17%) did not receive any support from the cooperative governance departments or any of the treasuries. The highest number of municipalities that did not receive the necessary support was in the Free State (nine municipalities – 45%), the Northern Cape (10 municipalities – 38%) and KwaZulu-Natal (12 municipalities – 20%). The lack of support could adversely affect the ability of these municipalities to improve service delivery.

Sub-outcome 2: Strengthened intergovernmental arrangements for a functional system of cooperative governance for local government

Strengthening the capability of provincial Cogtas will provide a solid institutional platform for the provision of effective context-specific institutional development and capacity-building support to municipalities as well as improved monitoring and oversight to ensure that high standards of public service and good governance are maintained at local government level.

The DCoG put processes in place to undertake the **organisational evaluation** of provincial Cogtas. The effectiveness of provincial departments is evaluated to improve their functioning in terms of monitoring, supporting and empowering municipalities to fulfil their mandate. The process is, however, still ongoing and as a result actions to facilitate envisioned improvement had not yet commenced.

Sub-outcome 3: Democratic, well-governed and effective municipal institutions capable of carrying out their development mandate as per the constitution

Municipalities should have fundamental institutional and management processes and practices in place to deliver quality services and to be responsive to the needs of communities. The following are two key outputs for this sub-outcome:

- Putting people first (ward committees to engage in participatory ward-level planning to produce ward-level service delivery plans and municipalities to have responsive and viable community complaints systems)
- Good governance (strengthened accountability and functional executive structures; as well as key risk areas associated with corruption and/or weak governance identified and responded to, including political interference, non-compliance with tender rules and reducing the high levels of unauthorised, irregular as well as fruitless and wasteful expenditure)

Key output 1: Putting people first

The DCoG reported in its 2015-16 performance report that the target relating to monitoring the functionality of ward committees in line with the implementation of the ward operational plans had been achieved; however, we were unable to obtain sufficient appropriate evidence to support the reported achievement. The department reported that a national analysis was conducted on the current ward committee functionality to inform the next generation after the 2016 local government elections.

Customised indicators were developed to measure public participation for inclusion in the annual performance plans of all provincial Cogtas. While these departments in Gauteng, Limpopo, Mpumalanga, the Eastern Cape and the Western Cape validly reported their achievement of these indicators, table 1 sets out our findings in the remaining provinces.

Table 1: Provinces that did not achieve the relevant customised indicators relating to public participation (putting people first)

Finding	Province			
The target relating to the following matters was not achieved	Free State	KwaZulu-Natal	Northern Cape	North West
Number of ward committees supported on implementation of ward operational plans	Not achieved	Indicated as achieved; however, we were unable to obtain sufficient appropriate audit evidence to support the achievement reported	Indicated as achieved; however, we were unable to obtain sufficient appropriate audit evidence to support the achievement reported	Target not included in performance plan
Number of municipalities supported on development of ward-level database with community concerns and remedial actions produced	Reliably reported as achieved	Reliably reported as achieved	Indicated as achieved; however, we were unable to obtain sufficient appropriate audit evidence to support the achievement reported	Target not included in performance plan
Report on the number of community report-back meetings convened by councillors in each ward	Reliably reported as achieved	Indicated as achieved; however, we were unable to obtain sufficient appropriate audit evidence to support the achievement reported	Indicated as achieved; however, we were unable to obtain sufficient appropriate audit evidence to support the achievement reported	Target not included in performance plan

Sub-outcome 3 lists as one of its key outputs that ward committees should engage in participatory ward-level planning to improve ward-level service delivery. Furthermore, municipalities should have responsive and viable community complaints systems. These elements should then be addressed through a comprehensive ward-level improvement plan. Table 2 lists the number of municipalities (excluding district municipalities) per province where we identified findings relating to this key output.

Table 2: Number of municipalities per province with findings relating to ward committees

Province	No ward-level improvement plans submitted for auditing	Ward committees not established for each ward	Ward-level improvement plans developed but did not address basic concerns	Ward-level improvement plans not developed
Eastern Cape	5	1	3	6
Free State	1	-	2	3
Gauteng	-	1	-	-
KwaZulu-Natal	1	-	-	2
Limpopo	-	-	-	1
Mpumalanga	1	-	-	7
Northern Cape	1	2	-	10
North West	5	2	-	8
Western Cape	1	1	-	5
Total	15	7	5	42

Key output 2: Good governance

We were unable to obtain information from the DCoG to determine whether appropriate actions had been taken to ensure that the targets as set out in the revised MTSF relating to the curbing of unauthorised, irregular as well as fruitless and wasteful expenditure, monitoring and reporting on the functioning of executive structures, and undertaking management performance assessments, would be achieved over the MTSF period.

We assessed that the DCoG and/or the National Treasury did not have a significant impact in respect of support in investigating and curbing unauthorised, irregular as well fruitless and wasteful expenditure at 37% of the municipalities. Limited impact was also reported at 33% of the municipalities where support was provided towards ensuring that the municipalities had and applied clear tender rules, monitored adherence thereto and enforced compliance. This was predominantly noted in the Eastern Cape and KwaZulu-Natal.

Sections 4.2.1 to 4.2.3 further detail the distribution and value of unauthorised, irregular as well as fruitless and wasteful expenditure.

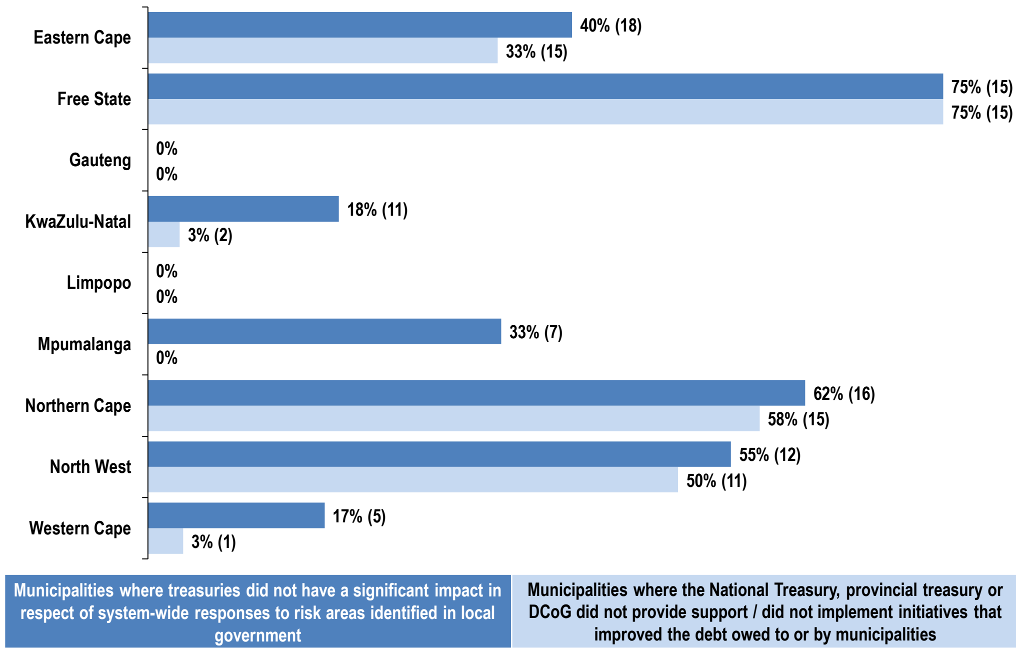
Sub-outcome 4: Sound financial and administration management

The fundamental aim of this sub-outcome is to attain a robust and sound financial management regime at local government level. Municipalities in Gauteng and Limpopo reported a high level of support with regard to sound financial and administration management – best practices in these provinces should be shared with the remainder of the sector to implement where appropriate.

We assessed that there was a lack of support in the following critical processes at a municipal level in the remainder of the provinces, as detailed in figure 2:

- Provide support to municipalities relating to the identification and addressing of transversal financial risk areas in local government.
- Provide support to municipalities regarding the resolution of concerns surrounding long-outstanding debt owed to and by municipalities.

Figure 2: Percentage of municipalities per province that reported a lack of support with regard to improving financial management



Municipalities are supported by provincial and national government (including treasuries and cooperative governance departments) through a number of different programmes, direct support to targeted municipalities, the provision of funding for consultants, and the municipal audit support programme of the South African Local Government Association (Salga). By improving the monitoring and reporting by municipalities, risk areas in local government finances will be identified. This will make it possible for appropriate system-wide responses to be investigated and developed and the issue of debt owed to and by municipalities to be addressed by the DCoG to find viable solutions to the problems of low collection, debt older than 90 days, and municipalities not paying creditors within 30 days. This will eliminate the weaknesses in the system that compromise the ability of municipalities to fulfil their service delivery obligations and developmental mandate.

Implementation of the back-to-basics programme

The DCoG continued its B2B programme during the year under review. This programme came into existence in 2014 and adopts the B2B approach as an urgent action plan to strengthen local government by getting the basics right. B2B is based on the following five pillars, which are aligned to the MTSF sub-outcomes:

- Putting people and their concerns first
- Supporting the delivery of municipal services of the right quality and standards
- Promoting good governance
- Ensuring sound financial management and accounting
- Building institutional capacity and administrative capability

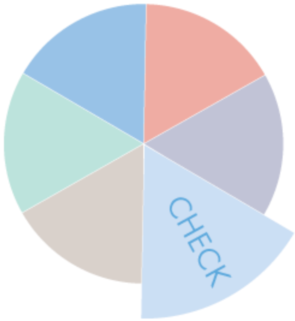
Municipalities were initially classified into three categories to aim the focus of the programme: those that are functioning well and getting the basics right (111 municipalities); those that are fairly functional with average performance and the potential to do well (86 municipalities); and those that are dysfunctional and require intervention (81 municipalities). The DCoG indicated that no significant changes were made to the B2B categorisation of municipalities during 2015-16. This was as a result of certain challenges that municipalities still faced, including weaknesses in the delivery of basic services, weak citizen engagement, incomplete and inaccurate data being provided by municipalities, uneven participation in provincial task teams, and a lack of central coordination and standardisation of the work of provincial task teams, which led to problems with the quality of information and B2B action plans.

The DCoG developed a 10-point plan of B2B priority actions during the third quarter of 2015-16 to guide ongoing activities and the next phase of the B2B programme.

During the year under review, 222 municipalities (84%) reported on a monthly basis on the B2B programme. The highest number of municipalities not reporting on the B2B programme was in the Eastern Cape (14 municipalities). The DCoG is currently still using the manual system used in the previous year for monthly reporting on B2B and for populating dashboard reports. The DCoG did not have processes in place to ensure that the monthly B2B reporting was accurate, as the department did not have capacity to verify all monthly responses received from municipalities. The department indicated that going forward, municipal managers would be required to sign off on the monthly reports submitted to ensure a higher level of control and accountability. Although it would initially have been completed by April 2016, the dashboard was not yet available for public viewing although it was being used for internal monitoring purposes. The DCoG plans on automating this process in the near future.

The B2B programme is the DCoG's key initiative and encompasses the proposed actions for support to local government to improve its functioning. It is therefore critical for municipalities to provide their B2B feedback for the programme to succeed. We thus included an audit procedure at MFMA level to determine the participation of municipalities in the programme.

Support plans had to be drafted to address the key challenges by municipalities that were classified as 'potential to do well' and 'dysfunctional'. B2B support plans were not drafted by 42 municipalities (which included 14 municipalities in the Northern Cape), while support plans were not adequate at only 23 municipalities (which included 16 municipalities in the Free State). These 16 municipalities also formed part of the 29 municipalities where the B2B support plans had not been implemented or monitored.



Conclusion

The departments of cooperative governance's oversight of, and support to, local government are not at the desired level, as evident from the matters highlighted in this section, particularly the fact that the categorisation of municipalities as part of the B2B programme remained unchanged in 2015-16. This indicates that, from the departments of cooperative governance's perspective, there had not been any material improvement in the functioning of local government during the 2015-16 financial year. While we acknowledge that leadership instability at the DCoG, who is primarily responsible for coordinating cohesive oversight and support initiatives to municipalities, has had a negative impact on the activities of the departments of cooperative governance, a concerted effort will have to be made to ensure the achievement of support interventions proposed in the MTSF by 2019.

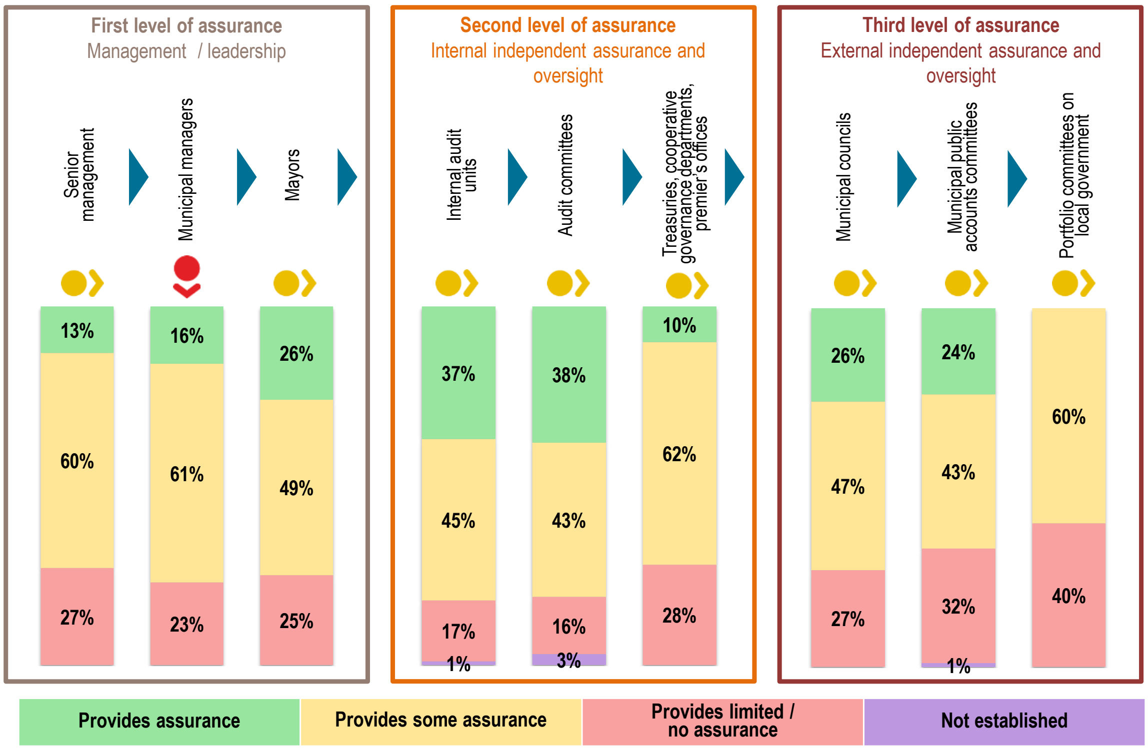
NOTES

9 Assurance providers

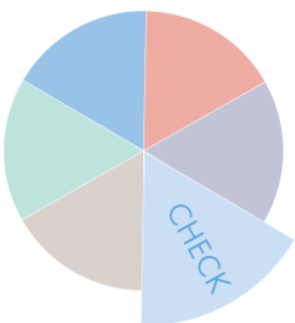
9. Assurance providers

Figure 1 shows our assessment in 2015-16 of the **assurance** provided by the management/leadership of municipalities and those that provide independent assurance and oversight. The arrows show the movement in assurance levels since 2014-15. We determined the movements, taking into account either increases in ‘provides assurance’ or reductions in ‘provides limited/no assurance’.

Figure 1: Assurance provided by key role players



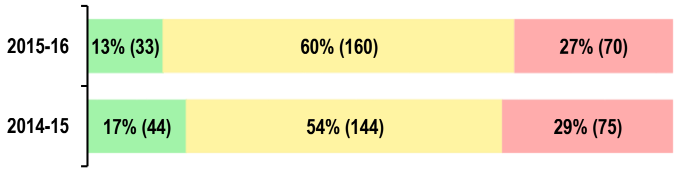
The assurance provided by these key role players had remained unchanged since 2014-15, except for the regression in the assurance provided by municipal managers.



Low levels of assurance show that there is a breakdown in a crucial element of the improvement cycle, being the monitoring to ensure that internal controls are adhered to, risks are managed and outcomes are achieved.

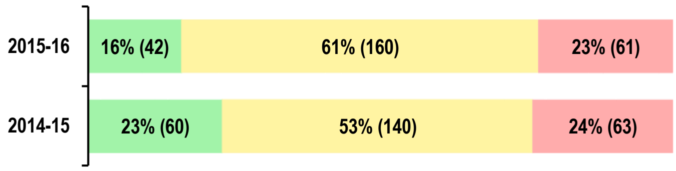
We provide an overview of the level of assurance provided by the different role players in the rest of this section. Refer to section 13.1 for further detail on the role of each role player providing assurance and the assessment thereof. We also reflect on the status of commitments made and key initiatives that will be undertaken by the offices of the premier, treasuries and departments of cooperative governance to address the audit outcomes. We further detail the commitments made (whether honoured or not) and the impact thereof by the DPME and Salga.

Senior management



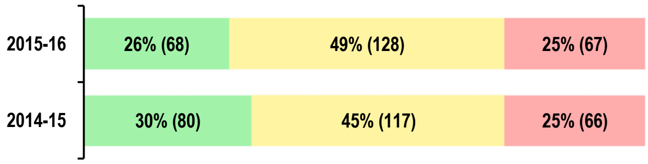
Senior management at 87% of the municipalities did not provide the required level of assurance in 2015-16 – a slight regression compared to the 83% in the previous year. The number of municipalities where senior management is providing limited or no assurance decreased slightly.

Municipal managers



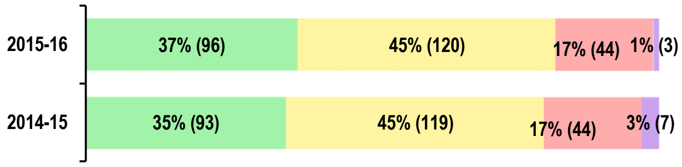
The assurance provided by municipal managers had regressed since the previous year, and municipal managers at 84% of the municipalities (2014-15: 77%) still did not provide the required level of assurance by 2015-16. We noted a regression in the assurance provided by municipal managers at municipalities in the Free State, Gauteng, KwaZulu-Natal and Limpopo. This was due to inadequate monitoring and evaluation of action plans as well as ineffective oversight of financial reporting to ensure credible financial reports.

Mayors



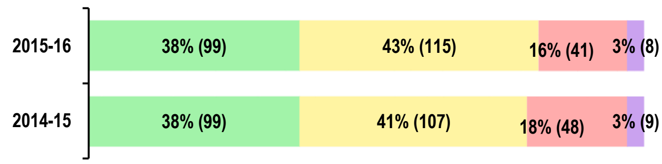
The mayors that provided the required level of assurance slightly regressed in 2015-16 and mayors did not yet provide the required level of assurance at 74% of the municipalities – a slight regression compared to the 70% in the previous year. This slight regression is evidenced by the overall status of leadership controls (as detailed in section 2.2). At some municipalities, the mayor did not provide adequate oversight of the implementation of action plans to address prior year findings, while not all of the commitments made by mayors to improve audit outcomes were honoured.

Internal audit units



At some municipalities, well-resourced and effective internal audit units have helped to improve internal controls and have had a positive impact on audit outcomes. We assessed that in 2015-16, 44% of the internal audit units had a positive impact on the audit outcomes (2014-15: 50%). The main reason for the lack of positive impact was management's failure to address internal audit findings.

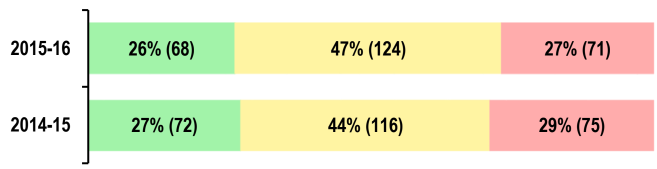
Audit committees



At 38% of the municipalities, audit committees provided full assurance, which remained unchanged compared to 2014-15.

The audit committees of 58% of the municipalities had a positive impact on the audit outcomes (2014-15: 59%). The number of audit committees that interacted with the mayors and/or councils had increased to 232 (91%) from 226 (90%) in 2014-15.

Municipal councils



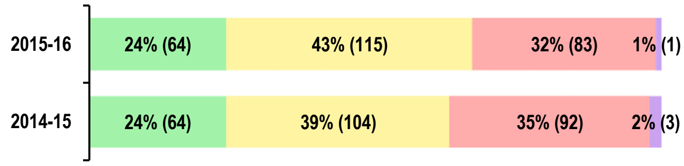
The council can provide extensive assurance through its monitoring and oversight role. Although councils are becoming more aware of the important role they have in this regard, most were not functioning at the required level, with only 26% of the municipal councils providing the required level of assurance by 2015-16. This is a slight regression compared to the 27% in 2014-15.

We participated in the national councillor induction programme that took place from September to October 2016 across all provinces. The programme concentrated on the following modules, among others:

- Legislative and policy framework
- Understanding sound financial management and governance
- Municipal planning and strategy
- Municipal finance management
- Municipal performance and accountability
- Role players and stakeholders
- The skilled municipal councillor
- The ethical municipal councillor
- Municipal procedures and protocols

As part of the handover process, all our audit business units engaged the new councillors (where MPAC chairpersons were in attendance) on the MFMA audit outcomes. There was a general appreciation of the handover report, which provided a glimpse of the issues that the new leadership would need to monitor towards attaining improved audit outcomes in the following year.

Municipal public accounts committees and the Association of Public Accounts Committees



At 24% of the municipalities, MPACs provided full assurance, which is unchanged from the previous year. Only one municipality had failed to establish an MPAC, compared to three in 2014-15.

The following are some of the challenges that affected the work of MPACs:

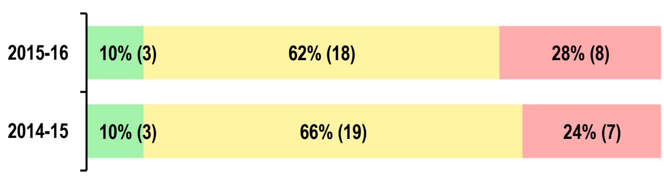
- Lack of capacity and awareness of MPAC roles and responsibilities, mainly because most MPAC members were new councillors largely due to the high turnover of MPAC members.
- Problems relating to effective administrative support – most of the committees still depended on support provided by the offices of the speaker or the municipal manager.
- Delayed submission of reports and information from the administration in some cases.

The new MPACs will require further support in capacity building and guidance to ensure improved oversight and assurance provision at local government level.

During our interaction with the Association of Public Accounts Committees (APAC) on the 2015-16 MFMA audit outcomes, the following initiatives were put forward:

- All provincial public accounts committee chairpersons must conduct joint hearings with MPACs to share best practices.
- The APAC leadership will conduct capacity building of MPACs and engage relevant institutions such as the DCoG and Salga to support the initiative.
- APAC to engage the minister responsible for cooperative governance to initiate a bill that will provide a clear legal provision for the existence of MPACs.
- APAC to engage the provincial speakers' forums to provide support in championing oversight through MPACs.
- APAC to coordinate provincial indabas to discuss the current MFMA audit outcomes and develop solutions. In preparation for the indabas, the following should be considered:
  - Provincial speakers, MECs responsible for cooperative governance and for finance, public accounts committees and MPACs should be in attendance.
  - An APAC exco planning workshop should be organised to craft a common approach.
  - Our support to provide insights on transversal issues should be prioritised.

Treasuries, offices of the premier and departments of cooperative governance (coordinating/monitoring departments)



Only 10% of the coordinating/monitoring departments provided the required level of assurance in 2015-16, while 28% provided limited or no assurance in the year under review.

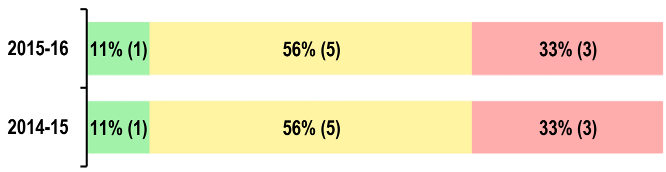
Our country's constitution stipulates that national and provincial government must support and strengthen the capacity of municipalities to manage their own affairs, to exercise their powers, and to perform their duties. The MFMA further requires national and provincial government to assist municipalities in building capacity to support efficient, effective and transparent financial management. Both the MFMA and the Municipal Systems Act (MSA) define the responsibilities for monitoring financial and performance management.

The departments with specific coordinating and monitoring responsibilities are the National Treasury, the provincial treasuries, the offices of the premier and the departments of cooperative governance. We assessed the impact of these departments on the controls of municipalities based on interactions with them, commitments given and honoured by them, and the impact of their actions and initiatives. We also looked at the role of the DPME and Salga, although we did not assess them as assurance providers.

There had been a slight regression in the assurance provided since 2014-15. The assurance provided by both the provincial treasury and the premier's office regressed in North West. In Limpopo, the assurance provided by the premier's office improved.

The MTSF emphasises the involvement and collaboration by various role players in national and provincial government in addition to the municipalities. These include the DCoG, the National Treasury as well as provincial Cogtas, provincial treasuries and offices of the premier. Our assessment of these assurance providers based on the work done to support local government, as well as commentary on their role in implementing the MTSF outcomes, is detailed below and in section 8.

Offices of the premier



The level of assurance provided by the offices of the premier had remained unchanged from the previous year, with only the premier's office in the Western Cape providing the required level of assurance. The premier in the Western Cape continued to use the premier's coordinating forum to coordinate and monitor provincial oversight as well as interactions with MECs on a monthly basis to monitor progress towards clean administration. The premier improved the oversight of the implementation of the municipal governance review and outlook process, which is coordinated by the provincial treasury and the provincial Cogta.

The premier's office in Limpopo had improved the level of assurance from the previous year to provide some assurance in 2015-16. The level of assurance provided by the premier's office in North West had regressed from providing some assurance in the previous year, as they played no role in improving the audit outcomes. The provincial treasury and the provincial Cogta had to implement some of the initiatives planned by the premier. The level of assurance provided by the rest of the offices of the premier had not improved from 2014-15, due to the slow response to our messages and the commitments made in the previous year not always being honoured.

Table 1 lists the commitments previously made and the status thereof, while table 2 lists the key initiatives agreed on in response to the 2015-16 audit outcomes.

Table 1: Status of previous year's commitments

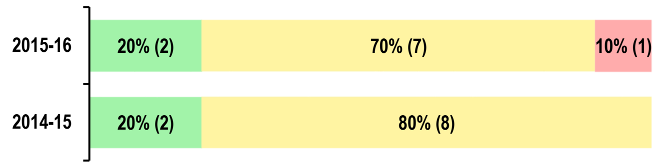
Offices of the premier										
Outline of commitments		Province								
Number	Previous year's commitments	EC	FS	GP	KZN	LP	MP	NC	NW	WC
1	Eliminate disclaimed opinions.									
2	Ensure a sound control environment - provincial executive leadership's recommitment to B2B programme.									
3	Address the competency shortcomings of municipal managers and CFOs.									
4	Implement consequences for poor performance and transgressions against all employees.									
5	Improve key controls over record management.									
6	Exercise oversight of the implementation of service delivery war rooms across departments and municipalities by tracking and monitoring instances of service delivery protests and government rapid response.									
7	Promote a culture of accountability at municipalities.									
8	Address the lack of consequence management and lack of action taken against transgressors through the newly established consequence management committee under the leadership of the MEC responsible for finance.									
9	In line with the prior year commitments, the premier continued to use the premier's coordinating forum to coordinate and monitor provincial oversight as well as interactions with MECs on a monthly basis to determine the progress towards clean administration.									

Completed	In progress	Not implemented

Table 2: Key initiatives agreed on in response to the 2015-16 audit outcomes

Offices of the premier										
Outline of key initiatives		Province								
Number	Key initiatives	EC	FS	GP	KZN	LP	MP	NC	NW	WC
1	Detect and prevent irregular expenditure as an executive priority.									
2	Focus on local economic development during outreach programme.									
3	Implement consequence management in the absence of improved audit outcomes for 2016-17.									
4	Exercise oversight of the implementation of service delivery war rooms across departments and municipalities by tracking and monitoring instances of service delivery protests and government rapid response.									
5	Strengthen coordinating role by strengthening the institutional arrangements through the intergovernmental framework.									
6	Seek visible actions to address poor outcomes.									
7	Focus on strategic interventions (including the acceleration of provision of water and education in the 2017-18 Medium-Term Expenditure Framework period, finalisation of comprehensive integrated development plan / budget review by municipalities, improvement of infrastructure planning and programme management, development of capacity in the provincial and municipal administration towards a creation of a developmental state, and revitalisation of operation clean audit programme).									
8	Prioritise accountability and service delivery at municipalities through Troika's commitments.									
9	Assist municipalities through provincial Cogta and provincial treasury.									
10	Apply a concentrated and focused approach regarding financial management issues (move the financial management unit from provincial Cogta to provincial treasury).									

Provincial treasuries and the National Treasury



The assurance provided by the treasuries regressed over the past year due to the limited or no assurance provided by the provincial treasury in North West.

The provincial treasury in the Western Cape and the National Treasury continued to provide the required level of assurance in 2015-16. The National Treasury demonstrated a proactive and consistent approach in using our reports on audit outcomes as one of its indicators to respond to, among others, identified control weaknesses.

We assessed the remaining provincial treasuries as providing some assurance. At some of the provinces, officials from the provincial treasuries were involved during the audit process and attended audit steering committee meetings; however, their involvement was not sufficient to drive positive outcomes. We noted improvements at some municipalities, but others still submitted financial statements with material misstatements.

Table 3 lists the commitments previously made and the status thereof, while table 4 lists the key initiatives agreed on.

Table 3: Status of previous year's commitments

National Treasury and provincial treasuries											
Outline of commitments		Province									National Treasury
Number	Previous year's commitments	EC	FS	GP	KZN	LP	MP	NC	NW	WC	
1	Capacitate the municipal finance unit within provincial treasury.										
2	Establish an audit intervention forum chaired by the MEC responsible for finance to discuss transversal audit matters, to intervene where required, to facilitate conclusion of unresolved outstanding matters, and to provide the necessary political leadership during the audit process.										
3	Intensify the implementation of the municipal finance hands-on support programme with specific emphasis on assisting municipalities in budgeting.										
4	Enhance local government support initiatives through CFO forums.										
5	Provincial Cogta and provincial treasury to assist district municipalities to improve basic disciplines through a joint support plan and the implementation of the B2B programme in the districts.										
6	Improve the availability of quality supporting documentation to support the financial statements and management information.										
7	Assess the financial sustainability of municipalities and, where necessary, assist in developing and monitoring a financial recovery plan.										
8	Develop action plans to address the root causes of findings contained in management and audit reports.										
9	Office of the MEC at the provincial treasury to appoint a liaison person to warn the MEC when units providing support to the municipalities are defaulting from the agreed programmes.										
10	Create capacity and an understanding of issues that the new councillors should be driving.										

National Treasury and provincial treasuries											
Outline of commitments		Province									National Treasury
Number	Previous year's commitments	EC	FS	GP	KZN	LP	MP	NC	NW	WC	
11	Formulate a shared service model at district level to enable the sharing of expertise and best practices.										
12	Municipalities to compile draft annual financial statements by June 2016 to be reviewed by the treasury; this will reduce material misstatements in the financial statements submitted for auditing on 31 August 2016.										
13	Implement a creditors' payment initiative to ensure that all service providers are paid within 30 days.										
14	Sustain the implementation of the municipal governance review and outlook process to ensure that control measures are institutionalised to sustain clean administration.										
15	Remain committed to sustaining and refining supervisory functions over financial management in local government.										
16	The centralisation of procurement by government is a current initiative flowing from the Office of the Chief Procurement Officer at the National Treasury. The development of the e-tendering platform by this office must be adequately tracked and monitored to ensure timely roll-out to local government and a positive impact in strengthening SCM controls, seeking to achieve better value for money in the government procurement system and mitigating financial mismanagement and errors.										

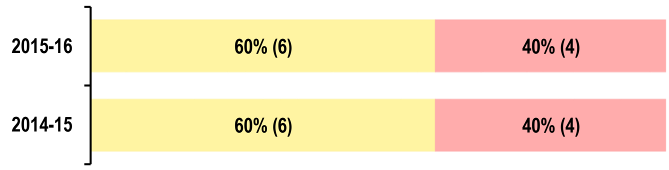
Completed **In progress** **Not implemented**

Table 4: Key initiatives agreed on in response to the 2015-16 audit outcomes

National Treasury and provincial treasuries											
Outline of key initiatives		Province									National Treasury
Number	Key initiatives	EC	FS	GP	KZN	LP	MP	NC	NW	WC	
1	Analyse the use of consultants where there is internal capacity to determine the value that the government is deriving from the use of consultants.										
2	Together with the departments of cooperative governance and Salga, continue with coordination efforts to ensure municipalities focus on the AGSA's recommendations.										
3	Focus on deviations granted by municipalities to ensure that effective controls are in place.										
4	Review credibility of budgets to reduce the level of unauthorised expenditure.										
5	Investigate capacity of internal audit units and audit committees.										
6	Focus on issues raised by the AGSA on financial health as well as unauthorised, irregular and fruitless and wasteful expenditure.										
7	Focus on municipalities that moved from disclaimed to unqualified opinions with findings to maintain sustainability of the audit outcome.										
8	Intensify implementation of the municipal finance hands-on support programme with specific emphasis on assisting municipalities with budgeting.										

National Treasury and provincial treasuries											
Outline of key initiatives		Province									National Treasury
Number	Key initiatives	EC	FS	GP	KZN	LP	MP	NC	NW	WC	
9	Continue to roll out mSCOA training to municipal officials.										
10	Closely monitor the use of consultants by municipalities to implement mSCOA.										
11	Standardise financial management systems to be implemented at all Limpopo municipalities by 2020 (mSCOA implementation).										
12	Improve availability of quality supporting documentation to support financial statements and management information.										
13	Develop action plans to address root causes of findings contained in management and audit reports.										
14	Together with the departments of cooperative governance, submitted an intervention report on unauthorised, irregular as well as fruitless and wasteful expenditure to exco, which included recommendations for investigation.										
15	Continue with the municipal governance review and outlook process.										
16	Together with the DCoG, commenced work in aligning the MFMA and MSA to provide better focus, clarify roles and responsibilities, reduce potential duplication of effort, and streamline implementation actions on financial management and governance arrangements in municipalities.										
17	Together with provincial treasuries, focus support over the medium term in assisting municipalities with the implementation of the various reforms based on gaps identified and strategic priorities as they relate to financial management and supplementary governance issues. The immediate initiatives relate to support and capacity building of newly elected councillors to better understand their role and responsibility on finance management relating to the duties of finance committees and MPACs, as well as councils' general oversight functions.										
18	Provided support both in technical and non-technical form, covering the following areas: mSCOA readiness, hosting of regional sessions to train and update municipal officials in producing credible and funded budgets, reforms in the accounting framework related to re-demarcated municipalities and other Standards of Generally Accepted Accounting Practice applications, review of audit action plans to assist and improve audit outcomes, process to address allegations of financial misconduct, treatment and process to address unauthorised, irregular as well as fruitless and wasteful expenditure, support for the minimum competencies and review of the regulations thereon, preparation of financial recovery plans, and updating and encouraging use of the central supplier database, transversal contracts and cost containment.										

National and provincial departments of cooperative governance



The assurance provided by the departments of cooperative governance had shown no improvement from the previous year, with no or limited assurance being provided by the DCoG and the provincial departments in the Free State, the Northern Cape and North West.

The DCoG was assessed as not having provided the required level of assurance as an oversight institution during 2015-16, based on their support initiatives not having been implemented to such a degree to bring about positive outcomes at all municipalities (also refer to section 8). Furthermore, we noted a number of instances in the department's annual performance plan where information was either not provided or not valid to support the actual achievements reported by the department. In our interactions with the new minister, only one commitment was received, namely to ensure that the department and its entities in the portfolio implement their respective action plans.

Table 5 lists the commitments previously made and the status thereof, while table 6 lists the key initiatives agreed on.

Table 5: Status of previous year's commitments

Provincial departments responsible for cooperative governance										
Outline of commitments		Province								
Number	Previous year's commitments	EC	FS	GP	KZN	LP	MP	NC	NW	WC
1	Induction of new councillors and oversight structures.									
2	Track, review and monitor progress on operation clean audit, provide and coordinate support (including the placement of technical advisors, audit steering and audit committee meetings - LP), and strengthen district monitoring committees.									
3	In respect of unauthorised, irregular and fruitless and wasteful expenditure, provide support to improve compliance and address irregular expenditure at those municipalities recording high amounts.									
4	Engage with municipalities that utilised consultants for the preparation of financial statements and performance reports to establish reasons for adverse findings despite such support, and introduce remedial measures to ensure value for money and mitigation.									
5	Provide specific support on performance management to address the regression in findings on predetermined objectives.									
6	MEC to convene several engagements with municipalities owing money to Eskom to sign repayment plan agreements and monitor the implementation thereof.									
7	Office of the CFO in the department will be taking a lead in capacity-building programmes for the municipalities.									
8	Establish a project management unit within the department to enable assistance at various municipalities without resources.									
9	Involvement with the provincial treasury in the municipal governance review and outlook process.									

Completed **In progress** **Not implemented**

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Table 6: Key initiatives agreed on in response to the 2015-16 audit outcomes

Provincial departments responsible for cooperative governance										
Outline of key initiatives		Province								
Number	Key initiatives	EC	FS	GP	KZN	LP	MP	NC	NW	WC
1	The detection and prevention of irregular expenditure will be a focus area of the Cogta roadshows with councils.									
2	Focus on intensifying monitoring at municipalities.									
3	Work with treasury on areas of joint responsibility.									
4	Continue to support capacitation of oversight structures.									
5	Track, review and monitor progress on operation clean audit and provide technical support (assist municipalities with their planning).									
6	Ensure that the B2B programme becomes a standing item for all key engagements at municipalities.									
7	Ensure that the audit committee's recommendations are implemented by municipalities.									
8	Train MPACs to manage unauthorised, irregular, and fruitless and wasteful expenditure.									
9	Set up meetings with municipalities that had obtained poor audit outcomes, during which the mayors of those municipalities have to present turnaround strategies.									
10	Strengthen the roles of district municipalities.									
11	Monitor municipalities and assess the progress made to address matters raised by the AGSA.									
12	Together with the provincial treasury, submitted an intervention report on unauthorised, irregular as well as fruitless and wasteful expenditure to exco, which included recommendations for investigation.									
13	Continue with the municipal governance review and outlook process.									

Department of Cooperative Governance's progress on implementing our prior year recommendations

We made a number of recommendations to the DCoG in the prior year for them to enhance their level of oversight and support. The following were noted with regard to the progress made:

- The department completed the reorganising of their functions within the organisational structure, which was approved in March 2016. A local government support and interventions branch was established with five chief directors to have a more hands-on approach to cooperative governance. We could not yet assess the effectiveness of this unit due to it being fairly new – the implementation of this recommendation was thus still in progress.
- The 2016-17 customised indicators include a new indicator requiring municipalities to report on the implementation of the B2B support plans. This indicator was added to enhance full cooperation by the entire sector in driving the impact of the B2B support plans. The implementation of this recommendation was in progress.
- The department made limited progress towards the implementation of the corporate governance of information and communication technology framework at municipal level. As was the case in the previous year, the lack of progress was due to capacity challenges. The implementation of this recommendation was thus still in progress.

- Misa displayed some improvement in the development of its indicators and targets by articulating the intended level of performance in providing support. However, reliable documents to support the actual achievement of these targets were not maintained. Misa should implement proper performance management systems and processes that will allow for complete, accurate and reliable performance reporting. The implementation of this recommendation was in progress.
- Misa continued to utilise consultants to provide technical infrastructure support to municipalities during 2015-16. No progress had been made with regard to Misa implementing proper tracking and monitoring systems and processes to enable them to regularly assess the performance of consultants and to measure the impact of the consultants' support. This recommendation had thus not been implemented.

Department of Planning, Monitoring and Evaluation

A primary aspect of the DPME's mandate is to measure and support improved management performance in municipalities. This mandate does not include monitoring and overseeing local government regarding audit-related matters and, accordingly, we do not assess them as an assurance provider.

Through its outcomes planning, monitoring and evaluation work, the DPME has developed the local government management improvement model. The model has been used from 2014-15 to measure and benchmark the performance of selected municipalities across key performance areas that are critical for improving service delivery and productivity.

Table 7 lists the key commitments that were undertaken in respect of this model during 2015-16 and the level of performance achieved, while table 8 lists the DPME's key initiatives to improve the effectiveness of this model.

Table 7: Prior year commitments for the local government management improvement model

Department of Planning, Monitoring and Evaluation		
Outline of commitments		
Number	Previous year's commitments	
1	Produce 25 local government management improvement model scorecards based on the model's assessments, performed by municipalities on a voluntary basis per year.	Completed
2	Submit an annual progress report on the local government management improvement model to the implementation forum for outcome 9.	Completed
3	Annually review and update the standards for the local government management improvement model for approval by the director-general by the end of September of each year.	Completed

Completed

Municipalities are enrolled on a voluntary basis after consultation with, and nomination by, the provincial Cogtas. Municipalities in distress and municipalities under administration are not targeted as part of these assessments to avoid duplication with programmes imitated by other role players in this environment, including the DCoG and Salga.

The effectiveness of the tool is highly dependent on the commitment from municipal management to utilise the results of the model as critical management information to develop and monitor improved action plans in the areas where performance gaps are identified.

Table 8: Key initiatives for the implementation of the local government management improvement model

Department of Planning, Monitoring and Evaluation		
Outline of key initiatives		
Number	Key initiatives	
1	Increase the targeted score sheets from 25 to 30 per year from the 2017-18 Public Finance Management Act cycle.	
2	Replace the current Excel assessments with a live web-based platform, which will allow for real-time monitoring by the DPME team of the activities of both municipal management as well as the provincial cooperative governance support teams on the system during assessments.	
3	Provide training to ensure that provincial departments are knowledgeable of the resources required to effectively implement the initiative.	
4	Select municipalities in conjunction with provinces, and clearly outline the requirements from municipalities prior to their participation in the assessment.	
5	Track activities of identified provincial champions and coordinators, to strengthen reporting on the level of commitment and interaction of the provincial cooperative governance support teams in respect of the assessment of the local government management improvement model.	

Completed	In progress	New

South African Local Government Association

Salga's mandate does not include monitoring and overseeing local government regarding audit-related matters and, accordingly, we do not assess them as an assurance provider. However, Salga has launched initiatives aimed at supporting local government to improve audit outcomes.

Salga introduced its municipal audit support programme on 31 July 2014. The programme aims to support all municipalities with poor audit outcomes so that they may improve their audit outcomes, but with a specific focus on municipalities with disclaimed or adverse opinions, or whose audits had not been finalised by the legislated deadline. These are classified as 'red zone' municipalities. Thirty-nine municipalities were classified as 'red zone' municipalities in 2015-16, based on their audit outcomes in 2014-15.

In terms of the municipal audit support programme, Salga aims to influence the improvement of the audit outcomes of municipalities while maintaining a strategic balance between a focus on audit outcomes and service delivery / institutional viability by concentrating on the root causes and main risks of poor audit outcomes identified by us. They base their support on a multidisciplinary approach focusing on four pillars, namely institutional capacity, financial management, leadership, and governance. These pillars are aligned to the B2B initiative of the DCoG.

Table 9 lists the key initiatives that were undertaken as part of the municipal audit support programme during 2015-16 and the status thereof, while table 10 lists Salga's other continuing initiatives and the status thereof as well as new initiatives and commitments.

Table 9: Status of previous year's commitments

South African Local Government Association		
Outline of commitments		
Number	Previous year's commitments	
1	Hold workshops in seven provinces with provincial treasuries, provincial Cogtas and offices of the premier to strengthen collaboration in the support of municipalities. This has led to a stronger working relationship between Salga and these departments, which also translated into more effective and efficient support to identified municipalities in these provinces.	
2	Develop support plans for 39 municipalities in the red zone and share such plans with provincial treasuries and provincial Cogtas to ensure collaboration of the support effort.	
3	Provide hands-on support to 43 municipalities to improve audit outcomes. Improved audit outcomes were noted at eight of these municipalities.	
4	Initiate an online support portal and finalise the proof of concept. Salga presented the online portal concept at various forums with municipalities and the feedback has been very positive in terms of the need for the portal. Salga is thus gathering evidence that the online support portal is feasible for implementation across local government.	

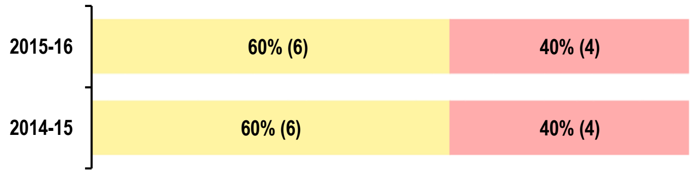
Completed	In progress

Table 10: Key initiatives agreed on in response to the 2015-16 audit outcomes

South African Local Government Association		
Outline of key initiatives		
Number	Key initiatives	
1	Support municipalities comprehensively in IT governance.	
2	Hold workshops on revenue and debt management as well as capacity development of councillor oversight in the provinces.	
3	Focus on those municipalities that are perennially attaining disclaimed audit opinions with the emphasis for 2016-17 to be on asset management.	
4	Work closely with the Office of the Chief Procurement Officer to assist in communication and education around procurement reforms.	
5	Provide record management training to municipalities to address a key root cause of disclaimed audit outcomes.	
6	Assess the implications of new reforms at local government, such as new accounting standards or legislation. In addition, communicate in a timely fashion to municipalities the impact of proposed new regulations or standards and how to ensure readiness.	
7	Develop processes that municipalities should follow when they encounter underfunding and unfunded mandates, and assist with alternative funding proposals. Coordinate this with treasuries to eliminate a duplication of effort.	
8	Continue with workshops, similar to the ones conducted in 2015-16, in all nine provinces during 2016-17 to further strengthen collaboration in the effort to support local government.	
9	Operationalise the first phase of the online support portal throughout local government.	

In progress	New

Portfolio committees on local government and the National Council of Provinces



In 2015-16, only 60% of the portfolio committees provided some assurance. This remained at the same level as in 2014-15, with the portfolio committees on local government in the Free State, Limpopo, the Northern Cape and North West providing limited or no assurance.

National Council of Provinces

The National Council of Provinces (NCoP) is one of the two houses of Parliament. The NCoP is constitutionally mandated to ensure that provincial interests are taken into account in the national sphere of government. This is done through participation in the national legislative process and by providing a national forum for the consideration of issues affecting provinces.

The NCoP also plays a unique role in the promotion of the principles of cooperative governance and intergovernmental relations. It ensures that the three spheres of government work together in performing their unique functions in terms of our country's constitution and that, in doing so, there is no encroaching on each other's area of competence.

Committee of chairpersons of the National Council of Provinces

During the year under review, no roadshow was held with the collective leadership of the NCoP, but the auditor-general constantly interacted with the house's chairperson responsible for the committee. During the tabling of the previous MFMA general report, the house chairperson made the following commitments:

- Select committees on finance and local government to intensify oversight on issues raised in the 2014-15 general report.
- Continuous engagement with Salga and the DCoG to ensure that all issues pertaining to the 2014-15 general report are followed up.
- Undertake various initiatives to fast-track capacity building of municipalities.
- Support the establishment and functioning of MPACs after the local government elections.

The following is a summary of the activities undertaken by the select committees in response to these commitments.

Select committee on local government

During the year under review, the committee held various oversight interventions aimed at municipalities that had challenges meeting their performance targets. As required by section 47 of the MFMA, the committee held hearings with the provincial Cogtas in Mpumalanga, the Northern Cape and KwaZulu-Natal as priority provinces identified by the committee for the year under review.

During these hearings, the committee raised the following key issues that required the attention of all the departments that appeared before them:

- Poor functioning of councils in holding departments accountable.
- Poor capacitation of MPACs.
- Ongoing service delivery protests owing to a lack of service delivery in some of the identified municipalities.
- Use of consultants without demonstrating a value-add.
- Lack of public meetings/forums in most municipalities leading to a disconnect between citizens and government in the local sphere.
- Slow progress in implementing the audit action plans.
- Late submission of financial statements for auditing.
- Poor recruitment and retention strategies leading to key staff leaving municipalities.

The committee further took part in oversight visits to municipalities to seek first-hand evidence of the service delivery and governance challenges faced by some of the municipalities. While the committee's oversight interventions focused on key issues in local government, they need to intensify their focus on how the DCoG has assisted municipalities.

Select committee on finance

The committee's mandate is to oversee the expenditure of government funds in the local government sphere, particularly the progress made in balancing expenditure and service delivery. During the year under review, the committee undertook various initiatives to enhance financial management in local government, including participating in the amendment of the following:

- Finance Intelligence Centre Bill
- Draft amendments to the Supply Chain Management Regulations
- Amendments to the 2017 fiscal framework and revenue

The committee also held a hearing with the City of Cape Town and the provincial treasury in the Western Cape on the city's integrated development plan, service delivery and budget implementation plan as well as local economic development. During this interaction, the committee raised the following key issues:

- Matters relating to water and property rates.
- Engagement by the provincial treasury with the city about debtors and creditors.
- The city's dependency on capital grants.
- The increased borrowing and increased spending of capital grants.
- Budget control challenges in Western Cape municipalities that needed intervention.
- The city's policy of withholding tenders by those who owe the city, while withholding payment to suppliers.
- The city's economic growth as it related to overall economic growth.

The committee provided adequate assurance in relation to its mandate, keeping in mind that part of its work was put on hold as the committee undertook a study tour to Mexico. Overall, this committee remains a good model of holding municipalities accountable for their expenditure.

Select committee on appropriations

The committee's mandate is the allocation and expenditure of government funds in the local government sphere. The committee executes its mandate through various initiatives, including undertaking oversight visits to provinces to check how municipalities are functioning. During the year under review, the committee undertook such oversight visits as well as participated in the processing of the following key money bills:

- Adjustment Appropriation Bill
- Division of Revenue Amendment Bill

The committee further held a hearing with the provincial Cogta in the Western Cape on municipal projects in Saldanha Bay. The following matters arose during the hearing:

- The performance of Saldanha Bay was reported as excellent and above 90%.
- Saldanha Bay and Cederberg were reported to have stood out in their commitment to spending in relation to other municipalities in the province.
- In Saldanha Bay, the overall expenditure for the second quarter under review accounted for 44% of the total municipal allocation, which was above the benchmark of 40%.
- The planned expenditure for the remainder of the financial year was at 88%.
- Presentation on the MIG projects scheduled for the site visit, including total project cost, MIG-registered amount, counter funding (municipal funding), number of beneficiaries, and current status of construction.
- The challenges faced by the municipality included the termination of the main contractor due to non-performance, delays in the appointment of the new contractor, securing funding from Transnet, and excessive underground water seepage that delayed the construction and necessitated the use of pumping equipment with a much larger capacity.
- Misa-assigned support in revenue management strategy where required.

For the year under review, the committee only focused on municipalities in the Western Cape owing to their good performance in the past. Overall, the committee provided adequate assurance for the year under review in line with the oversight activities planned for the year.

10 Recommendations

10. Recommendations

All role players in local government should continue to work together to strengthen the capacity, processes and controls of municipalities and municipal entities, which will enable credible financial and performance reporting, compliance with key legislation, sound financial management and service delivery. The recommendations that follow are consistent with our messages over the past years and are grouped according to the drivers of internal control, as well as linked to the plan+do+check+act cycle.

Leadership

1. In order to improve and sustain audit outcomes, municipalities require **effective leadership** (political and administrative) that is based on a culture of honesty, ethical business practices and good governance, protecting and enhancing the interests of the municipality.

   The following are some of the key aspects that should be considered:

   - Implement the required formal codes of conduct and regularly communicate their existence and continued applicability to officials.
   - Monitor key officials' performance regarding the maintenance of adequate systems of internal control that ensure credible monthly financial reporting, reliable reporting against predetermined objectives, and compliance with key legislation.
   - Establish clear lines of accountability.
   - Take corrective or disciplinary action against key officials for misconduct.
   - Honour commitments for interventions made to us in response to audit outcomes.

2. Policies and procedures should be applied fully to enable municipalities to implement **consequence management** for officials who fail to comply with the applicable legislation, while appropriate and timely action must be taken against transgressors. A less tolerant approach should be followed by all parties, including those charged with governance and oversight, which will result in accountability being enforced and consequences instituted against those who intentionally fail to comply with legislation.

3. Councils and municipal managers, with oversight from the provincial Cogtas, should ensure **stability in key senior management positions** (also after elections) – specifically those of municipal managers, CFOs and heads of SCM units. The ability to attract and retain competent officials remains a major challenge in local government but is key to consistent performance and a strong control environment.

4. Continue with the programmes (through the National Treasury) and intensify the support provided by the municipal leadership to ensure that key municipal officials reach the **minimum competency** levels as prescribed by the municipal regulations. An extension was granted on 3 February 2017, giving municipalities an additional 18 months (starting from the date of appointment or 3 February 2017 with regard to new employees and existing employees, respectively). Officials who had not reached the competency levels by the extended date should be appropriately dealt with in accordance with the regulations.

5. Councils and the management of municipalities responsible for the provision of **water and sanitation services** should focus on the following:

   - Develop customised indicators and targets for the provision of water and sanitation services that will ensure consistent application and monitoring between municipalities and provinces.
   - Properly plan and budget for the provision of water and sanitation in the integrated development plan, municipal budget, and service delivery and budget implementation plan by each municipality responsible for the provision of water and sanitation services.
   - Identify the basics in providing water, such as the establishment of infrastructure and facilities, to ensure the proper planning, budgeting and monitoring of these basics.
   - Establish monitoring processes that will enable the frequent and consistent monitoring of progress and enable proactive corrective action.
   - Develop and implement strict policies to ensure the consistent establishment and maintenance of infrastructure.
   - Develop and implement comprehensive infrastructure and maintenance plans that prioritise needs.
   - Manage water and sanitation infrastructure projects to ensure that they are delivered within the planned completion dates and that payments are made as planned and budgeted for.

6. Councils and the management of municipalities responsible for **road infrastructure** should focus on the following:

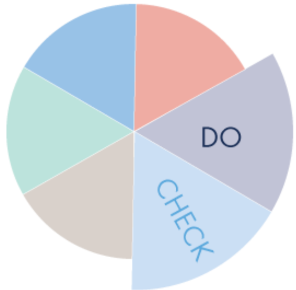
   - Develop and implement comprehensive policies to ensure proper planning and decision-making to achieve the desired outcomes for the management of road infrastructure. These policies should be approved and actioned.
   - Assess the condition of infrastructure. The results of this assessment should form the basis of the approved road maintenance plan or priority list to provide for all renewal and routine maintenance. Adequate funds can then be allocated to routine and scheduled maintenance instead of reactive maintenance.
   - Improve the management of road infrastructure; in addition, the maintenance of roads should receive the required attention. Funds should also be used and managed more effectively in this regard.
   - Ensure that projects are completed on time to avoid unnecessary delays, which could increase project costs.
   - Ensure that there is consequence management where corrective actions have not been implemented to address all issues identified.

7. Councils should insist on **credible in-year reporting** on financial and service delivery performance. Internal audit units can be of great assistance in checking the reliability of the information provided to the council.

8. Municipal managers and senior managers should pay attention to the management of **consultants**, ensuring value for money through considered planning and appointment processes, monitoring the performance of consultants, and insisting on the transfer of skills, where appropriate.

9. Cooperative governance departments and treasuries should provide support to municipalities in implementing and capacitating the **performance management and budgeting systems** to strengthen the planning, budgeting, monitoring and reporting of service delivery objectives. The development of customised indicators for basic services will contribute greatly towards a uniform and structured approach to planning and reporting on the provision of basic services. They should also continue with the implementation of, and improve the monitoring and accuracy of data for, the B2B programme as well as lead the coordination of, and enforce good practices by, the different role players in local government. The focus should be on implementing initiatives to achieve results in the different areas of service delivery at the end of the MTSF period. Further recommendations are also included in section 8.

Financial and performance management



1. **Proper and timely record keeping** ensures that complete, relevant and accurate information is accessible and available to support financial and performance reporting. Sound record keeping will also enable senior management to hold staff accountable for their actions. A lack of documentation affected all areas of the audit outcomes, including SCM. Senior managers should therefore ensure proper record keeping so that records supporting financial and performance information as well as compliance with key legislation can be made available when required for audit purposes. They should also implement policies, procedures and monitoring mechanisms to manage records and make staff members aware of their responsibilities in this regard.

2. Controls should be in place to ensure that **transactions** are processed in an accurate, complete and timely manner, which in turn will reduce errors and omissions in financial and performance reports.

   Some of the matters requiring attention from senior management include the following:

   - Daily capturing of financial transactions, supervisory reviews of captured information, and independent monthly reconciliations of key accounts.
   - Collecting performance information at intervals appropriate for monitoring, setting service delivery targets and milestones, and validating recorded information.
   - Confirming that legislative requirements and policies have been complied with before initiating transactions.

3. Municipal managers should ensure that municipalities have mechanisms to **identify applicable legislation** as well as changes to legislation, assess the requirements of legislation, and implement processes to ensure and monitor compliance with legislation. **Compliance checklists** should be implemented as a tool to supplement policies and procedures. These will enable officials, supervisors and monitoring units (e.g. internal audit units) to independently check whether all legislative requirements are met in the daily transactional, management as well as SCM processes.

4. **Regular reports** to management and governance structures on compliance with key legislation, specifically in the area of SCM, will further promote awareness of legislative requirements and ensure that management deals with compliance in a regular and structured manner.

5. The MTSF defines the implementation of **audit action plans** and the quarterly monitoring thereof by a coordinating structure in the province as key measures to support financial management and governance at municipalities. This is also echoed in the DCoG's B2B strategy, which tasks local government with addressing post-audit action plans; and the National Treasury, provincial treasuries and provincial Cogtas with assessing the capacity of municipalities to develop and implement such plans.

   The matters requiring attention by municipal managers and senior managers include the following:

   - Devise action plans to specifically address the external and internal audit findings.
   - Assign clear responsibility to specific staff members to carry out action plans and ensure that the responsibilities assigned are executed effectively and consistently through monitoring.

- Develop audit action plans early enough in the financial year to resolve matters by year-end.
- Ensure that audit action plans address all three areas of audit outcomes, namely qualifications, findings on performance reports and non-compliance with legislation.
- Focus the actions to be taken on the root causes of findings, thereby ensuring that sustainable solutions are found.

6. Urgent and focused attention should be given to preparing for the **implementation of mSCOA** to ensure that all implementation challenges are resolved by 1 July 2017. The guidance provided by the National Treasury through MFMA SCOA circulars should be followed and municipal staff should use the training opportunities provided.

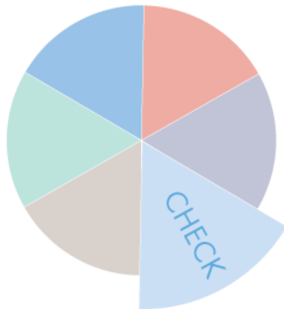
7. Municipal management should pay focused attention to improving the **IT control environment**. CIO and IT manager positions should be filled with appropriately qualified and experienced persons. The weaknesses in security management, user access management and IT continuity should also be addressed before the risks created by these weaknesses materialise. Continued efforts should be made towards implementing the IT governance framework. The provincial treasuries, premier's offices and provincial Cogtas should further improve the support provided to municipalities, especially with regard to system changes that could be required as a result of the implementation of mSCOA.

8. Reducing the cost of services provided is part of the solution for **improved municipal financial health**. We believe that more could be done with less if, among other cost-saving initiatives, a concerted effort is made to curtail the extent and costs of using external providers. The SCM process should be used effectively to procure goods and services from the best-qualified providers at the best price – and only if the need cannot be addressed internally or through other means (e.g. through the support provided by national and provincial government). The SCM reforms introduced by the National Treasury should be fully supported. The considerable financial resources and, therefore, strong negotiation power of local government as a collective, supported by national and provincial government, should also be considered and explored to reduce the cost of goods and services procured from the private sector.

9. The capacity and capability of local government **to plan, manage and report on service delivery** need urgent and increased attention from national and provincial government. **Project management** is required for infrastructure projects to succeed and municipalities should be guided and supported in a more focused manner in this regard.

10. Treasuries should intensify financial management and accounting **support to municipalities** and focus on sustainable solutions, such as training, guidance, standard operating procedures and knowledge-sharing forums.

Governance



1. Councils, municipal managers and senior managers should implement the recommendations of **internal audit units and audit committees** and use the opportunity to interact with these bodies to assist in improving governance and control.

2. The municipal manager supported by the mayor should focus on the following:

    - Ensure that there is an adequately resourced and functioning internal audit unit overseen by the audit committee that can identify internal control deficiencies and recommend corrective action effectively.
    - Ensure that the audit committee promotes accountability and service delivery through evaluating and monitoring responses to risks and providing oversight of the effectiveness of the internal control environment, including financial and performance reporting and compliance with legislation.
    - Implement appropriate risk management activities to ensure that regular risk assessments, including the consideration of IT risks and fraud prevention, are conducted and that a risk strategy to address the risks is developed and monitored.

3. Areas where these governance structures can jointly make significant contributions to the audit outcomes include the following:

    - Encourage senior management to submit regular financial and performance reports for audit committee review.
    - Assist with designing the audit action plan and monitor the implementation thereof.
    - Review financial statements and performance reports before submission for auditing to identify material misstatements.
    - Monitor the appropriateness and timeliness of actions taken by management in instances of known transgressions by officials.

Conclusion

In order for local government to position itself to achieve the goals as set out in the MTSF, it is vital that the leadership and management diligently execute their responsibilities to enable a professionalised local government that embraces the concepts of transparency and accountability. The enabling role of the accounting officer and the oversight functions of councils will play an important role in creating an environment where effective, efficient and economical service delivery and a clean audit are natural products of performing the correct actions. By implementing these simple practical steps, substantially improved financial management and performance reporting in local government can be brought about. This is a goal within reach and a key ingredient in building trust in the credibility and accountability of local government and its capacity to deliver services to citizens. All municipalities should keep striving to improve accountability, good governance and consequence management to attain or maintain clean administration.

In conclusion, we again draw your attention to the plan+do+check+act cycle that can be used when implementing our recommendations.

Figure 1: Plan+do+check+act cycle – committing to accountability

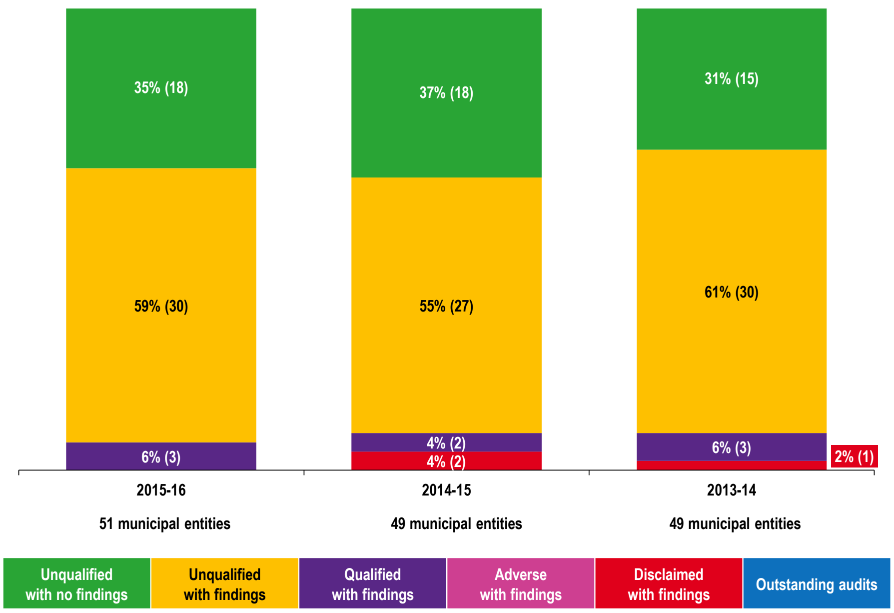
NOTES

11 Municipal entities

11. Municipal entities

Figure 1 depicts the audit outcomes of municipal entities over three years – four entities were excluded from our analysis in this report, due to their relatively small size or low level of activity.

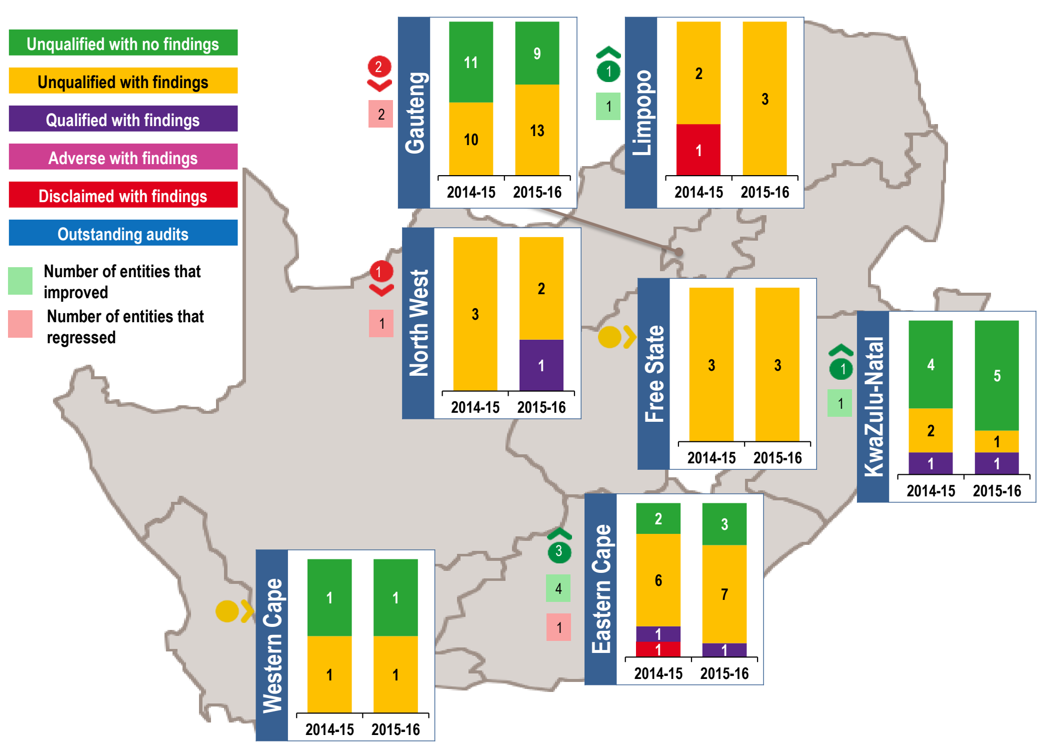
Figure 1: Slight improvement in audit outcomes of entities



As reflected in figure 1, there had been a **slight improvement overall in the audit outcomes** of entities since the previous year. The audit outcomes of 12% of the entities had improved, 8% had regressed and 76% remained unchanged (45% remaining as unqualified with findings).

Figure 2 compares the provincial audit outcomes of entities in 2014-15 and 2015-16.

Figure 2: Provincial audit outcomes of entities over two years



Audit of financial statements

The entities' financial statement submission rate had slightly regressed from 100% in 2014-15 to 98% in 2015-16, as one municipal entity submitted its financial statements late. The audit opinions on **financial statements** slightly improved from 8% that had either qualified or disclaimed opinions in 2014-15 to only 6% that were financially qualified in 2015-16. There was no improvement in the quality of the financial statements submitted for auditing – 53% of the entities submitted financial statements with **material misstatements** in both 2014-15 and 2015-16.

In 2015-16, the most common qualification areas were the financial statement items of expenditure, irregular expenditure, employee cost as well as payables, accruals and borrowings.

Compliance with key legislation

There had been a slight decrease in the number of entities with no findings on **compliance** over the two-year period – from 37% in 2014-15 to 35% in 2015-16.

The most common compliance findings in the current year and the progress made in addressing these since 2014-15 are as follows:

- Quality of financial statements submitted – 27 entities (53%) (2014-15: 26 [53%])
- Management of procurement and/or contracts – 19 entities (37%) (2014-15: 18 [37%])
- Prevention of irregular and fruitless and wasteful expenditure – 18 entities (35%) (2014-15: 22 [45%])
- Management of expenditure and payments – 12 entities (24%) (2014-15: 12 [24%])
- Consequence management – 11 entities (22%) (2014-15: 12 [24%])

The number of entities where we reported **SCM findings** had decreased from 69% in 2014-15 to 63% in the current year. The most common SCM areas in which entities had findings were uncompetitive or unfair procurement processes at 22 entities (2014-15: 27); inadequate contract management at seven entities (2014-15: seven); and awards to other state officials at 16 entities (2014-15: seven). Limitations in the planned scope of the audit of awards were experienced at only three entities (2014-15: four).

Irregular expenditure incurred

There had been a slight increase in **irregular expenditure** from R331 million in 2014-15 to R338 million in 2015-16. The main contributors (62%) to the increased irregular expenditure were Durban Marine Theme Park (R60 million), East Rand Water Care Company (R44 million), Maluti-A-Phofung Water (R42 million), Pikitup Johannesburg (R33 million), and Johannesburg Metropolitan Bus Services (R32 million).

Findings on performance reports

In total, 46 entities (90%) had prepared their 2015-16 **performance reports**. This is a slight regression from 2014-15 when 47 entities (96%) had done so. There had been a slight increase overall in the number of entities with no material findings on the quality of their performance reports from 69% in 2014-15 to 71% in 2015-16.

In total, 26 entities (51%) submitted performance reports that contained **no material misstatements** – a slight improvement from 2014-15.

Of the 46 submitted performance reports, the performance reports of two entities (2014-15: one) were not **reliable**, while those of five (2014-15: two) were not **useful** and those of three (2014-15: 10) were neither reliable nor useful, indicating that further attention is required from those in charge of oversight and governance in this regard.

Status of entities' financial health

There had been an improvement in the status of **financial health** of entities since the previous year – 29 entities (57%) had a good financial health status in 2015-16 compared to 25 entities (51%) in 2014-15.

Almost 12% of the entities had a **going concern uncertainty** in 2015-16. Although this is an improvement from the 20% in the previous year, it remains a cause for concern. The following financial health indicators had regressed since 2014-15:

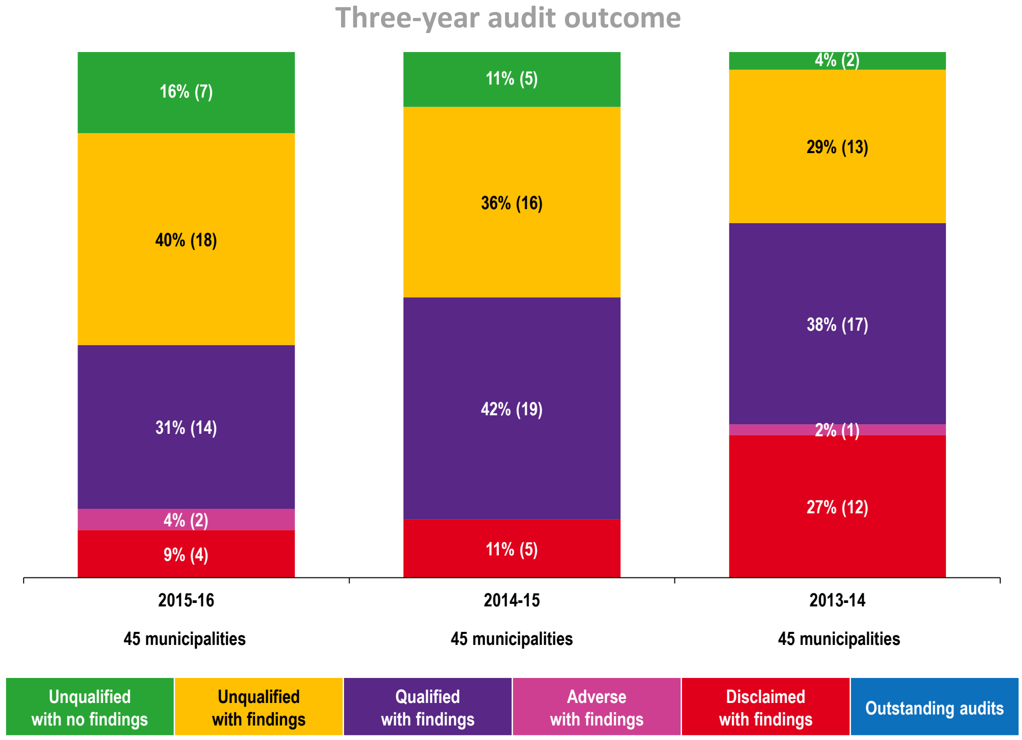
- Creditor-payment period of 90 days
- Creditors as a percentage of cash and cash equivalents more than 100%

The continued improvement in the audit outcomes of entities is encouraging, but the leadership of the entities and parent municipalities should pay attention to their compliance with legislation, SCM practices and financial health.

12 Provincial overviews

ACCOUNTABILITY = PLAN + DO + CHECK + ACT

12.1 Eastern Cape



The municipal leadership is accountable to the public for the equitable and efficient allocation of resources and for the planning, procurement and delivery of services in an effective, transparent and economical manner. In doing so, they contribute to improving the lives of the communities they represent. Good governance enhances accountability through the processes of decision-making and of then implementing those decisions. Such good governance includes the demonstration of effective leadership, robust and transparent financial and performance reporting, effective internal controls as well as strong oversight structures.

We are encouraged by the increased accountability and good governance shown by Engcobo, where we noted effective systems of budgeting and planning, efficient project and contract management, transparent and fair procurement processes, and appropriate reporting and record-management systems. This led to an improvement in the municipality's audit outcome from unqualified with findings on compliance matters to unqualified with no findings (also commonly referred to as a 'clean audit'). The municipality also better managed its infrastructure projects, as evidenced by the successful delivery of an electrification project. This project had a budgeted value of R8,5 million and was brought into use on time, at the required quality, and R1,6 million below budget. This project was supported by a proper business case, had a plan that was communicated to all role players allowing for proper coordination, had a clearly defined scope, followed all of the required SCM processes, was monitored regularly by the council, followed defined steps at completion, was appropriately reported on in the performance report, and was correctly recorded in the financial statements.

In contrast, the control environments of those municipalities that did not achieve clean audits remained at the same concerning levels as reported on in the previous year. Basic daily, weekly and monthly disciplines around financial and performance management were still not in place. Controls in the IT environment remained concerning and had improved only slightly from the previous year. These weak controls could expose municipalities in the province to the misappropriation of funds and lead to financial and performance reporting that is not credible. The slow response by accounting officers and senior managers to implement our recommendations relating to the poor status of record management, lack of a proactive risk-assessment process, as well as non-implementation of audit committee and internal audit recommendations, contributed to the poor control environments at most municipalities.

These poor control environments, ineffective and weak oversight structures and lack of leadership accountability resulted in findings on compliance with laws and regulations remaining at high levels (in particular, findings relating to the prevention and investigation of irregular expenditure as well as procurement and contract management). Consequences for poor performance and transgressions of legislation were not enforced. This created an emerging culture of discretion being applied to deviate from financial disciplines, internal controls and the laws and regulations governing the procurement of goods and services. This remained the biggest challenge facing local government in the province.

Irregular expenditure incurred during the year increased to R5,7 billion from R3,5 billion in the previous year. We observed this trend of increased irregular expenditure in all metros and municipal districts, other than in the Joe Gqabi district. The amount disclosed may furthermore not paint the full picture, as 19 municipalities were qualified as we could not confirm the completeness of the amount of irregular expenditure they had disclosed. Almost all (98%) of this irregular expenditure was caused by transgressions of SCM legislation.

We noted numerous examples of the inappropriate exercise of management's discretion to procure goods and services throughout the province. The accounting officers used their discretion in applying SCM regulation 36 to deviate from normal procurement processes to appoint targeted suppliers without ensuring that the requirements for valid deviations were met. One such example related to the upgrading of road infrastructure to the value of R222,5 million where the tender process was allowed to lapse, resulting in management deviating from the procurement processes in awarding the contract by going the deviation route.

At 27 municipalities, the accumulated prior year balance of irregular expenditure amounting to R7,7 billion was not investigated. Where investigations were done, they did not lead to disciplinary processes and/or the recovery of money.

The central focus of the MTSF is to ensure sustainable and reliable access to basic services. Weak control environments and a lack of accountability resulted in significant deficiencies relating to integrated and coordinated planning, project management as well as the economical use of resources in the delivery of municipal infrastructure.

The different spheres of government and other role players did not always conduct integrated and coordinated planning to determine the most appropriate options and to eliminate the duplication of effort and wastage. For example, the Ntabankulu water treatment project to the value of R39,6 million implemented by Alfred Nzo District had no water source and the flagship water supply project to the value of R23,1 million also implemented by the Alfred Nzo District could not function because it was not connected to electricity. These projects were not functioning at the time of our audit and will require additional resources and coordination to become fully functional in the near future.

Municipalities did also not always apply the principles of sound project management to their infrastructure projects, resulting in cost overruns, poor quality workmanship, and potential fruitless and wasteful expenditure. For example, the Lujazo bridge to the value of R5,1 million had to be abandoned when it was 25% complete due to inadequate planning, design defects and poor quality work, while the Jambeni access road to the value of R7,6 million was abandoned when it was 80% complete due to a lack of funding, inadequate supervision and poor quality workmanship. Both of these projects were implemented by Port St Johns.

Resources are used economically when goods and services are received at the right time, right place and right quality and at the lowest possible price. However, infrastructure projects were not always developed in the most economical way. An example in this regard related to phase 5 of the Fleet Street road project to the value of R27 million implemented by Buffalo City Metro, where a contractor had to be replaced due to inadequate supervision and poor quality workmanship. The initial contractor was paid R11,3 million for 18% of the work, whereas the replacement contractor was paid only R15,7 million for the remaining 82% of the work required.

The financial health of the municipalities in the province had deteriorated since the previous year due to inadequate processes to ensure sound financial management and worsening economic conditions. One district municipality and nine local municipalities had indicators that highlighted their inability to settle their liabilities as they fell due. Three of these local municipalities owed significant arrear amounts to Eskom, while one had also not paid over deductions from employees, including pension fund contributions. A further 21 municipalities, including two district municipalities that are water service providers, had concerning indicators that, if not acted upon and monitored closely, could result in an inability to maintain their current levels of service delivery. These indicators included the poor collection of receivables, excessive impairment of receivables, and insufficient cash on hand to settle liabilities timeously.

> There has been an improvement in the Eastern Cape audit outcomes. There's still significant work that needs to be done in respect of accounting systems, the control environment and record management.

We are encouraged by the net improvement of seven audit outcomes (16%) during 2015-16 and the overall improvement of 20 audit outcomes (44%) since 2013-14, as this supports the pursuit of sound financial and administrative management. This is significant because the financial statements of more than 50% of the municipalities in the province are now financially unqualified and goes a long way to achieving the target of 75% set out in the MTSF.

This net improvement is made up of 10 improved outcomes and three regressed outcomes. We are also encouraged by the improved outcomes at two of the 11 municipalities identified as requiring special intervention to unqualified with findings, as this shows that the actions taken are starting to have an impact. The improved outcomes can be attributed to better record keeping, the support provided by the provincial treasury and provincial Cogta, the leadership attending to audit recommendations, the implementation of the Municipal Regulations on Minimum Competency Levels, and the use of consultants.

Two of the regressions in the current year were at municipalities that had been amalgamated with other municipalities (Nxuba and Tsolwana) and were caused by the non-availability of personnel with institutional knowledge to deal with audit matters after the amalgamations.

Leadership stability, good internal controls, a leadership tone of intolerance towards control deviations, leadership commitment and recommendations that were acted upon were the common qualities of those municipalities that improved or achieved clean audit outcomes. The remaining municipalities in the province should strive to emulate this recipe for success.

Key role players did not provide the level of assurance over financial and performance reporting as well as compliance expected of them. Internal controls need to be improved if the expected levels of assurance that result in clean audit outcomes are to be achieved.

The vast majority (at least 80%) of municipal managers and CFOs had achieved both the minimum qualifications and minimum competencies prescribed by the Municipal Regulations on Minimum Competency Levels. However, this does not correlate with the continued use of consultants by 91% of municipalities and the poor quality of financial statements submitted by 69% of municipalities, and points to a lack of leadership and an absence of accountability rather than a shortage of skills and competencies.

The quality of the submitted financial statements had improved over the last three years; however, 69% of the municipalities still submitted financial statements that contained material misstatements. This can be attributed to a lack of in-year reporting and discipline relating to the reconciliation and recording of transactions on a daily, weekly and monthly basis. A total of 41 municipalities (91%) used consultants to prepare their financial statements, which cost local government in the province R147 million during the year under review. At least R39 million was paid to consultants by municipalities that had the internal capacity to prepare their financial statements themselves. Furthermore, 71% of the municipalities that used consultants still submitted financial statements that were of a poor quality, of which 46% received qualified, disclaimed or adverse opinions.

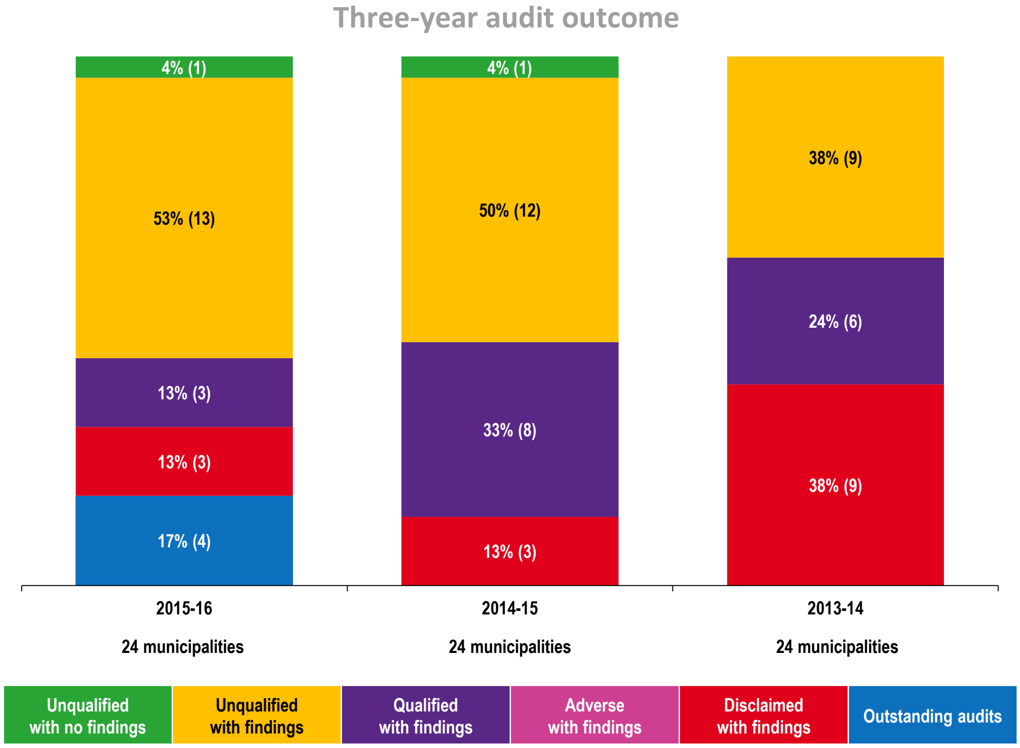
The quality of performance reports had improved marginally over the last three years due to improved record keeping relating to actual performance and the implementation of audit recommendations. However, 76% of the municipalities submitted reports that had usefulness findings and/or required material amendments. We reported findings on the usefulness of reported information at 38% of the municipalities, and reliability findings at 56% of the municipalities. The main cause of the usefulness findings was that those charged with governance did not adequately review planning documentation (integrated development plans and service delivery and budget implementation plans) for compliance with SMART principles (in other words, requiring performance criteria to be specific, measurable, achievable, relevant and time bound). The main reasons for the reliability findings were poor record-keeping practices and inadequate systems and processes to record information about actual performance.

In response to the previous general report, we obtained commitments relating to inducting new councillors, eliminating disclaimed audit outcomes, strengthening district monitoring committees, providing intensified and coordinated support to 16 municipalities, and capacitating the municipal finance unit within the provincial treasury. At the date of this report, only the commitment relating to the induction of councillors had been implemented. Although the remaining commitments were still in progress, they had a positive impact on the audit outcomes. Further improvements are expected once these commitments have been fully implemented and councils implement the following recommendations:

- Embark on leadership, governance and financial skilling programmes to enable effective oversight of the administration and to lead communities and municipalities to prosperity within the complex and challenging local government environment in which citizens demand quality services and value for money.
- Create an environment that brings predictability and stability at administration level and where the best talent and professionals are attracted, retained and allowed to flourish. Good HR management and career-development practices to maximise human potential should be developed, adopted and applied.
- Implement proper performance management systems that recognise and reward good performance and apply consequences for non-performance and transgressions. The leadership tone should promote accountability, professional ethics and transparency. The inappropriate use of discretion to deviate from internal controls, financial disciplines and legislative requirements should not be tolerated and should be dealt with swiftly.
- Enforce a culture of basic financial management disciplines, records review and adherence to good controls. This includes preparing reliable monthly and quarterly financial and performance reports that are supported by daily and monthly reconciliations to ensure that all transactions, balances and disclosures are accurately and completely recorded. IT systems should also be customised for better and accessible service delivery. Further, the councils should scrutinise all service delivery plans, regularly monitor in-year service delivery reports, and take action where actual performance is below expectation.
- Develop, adopt and apply policies and procedures that promote local content, local economic development and small businesses. An environment in which local suppliers, small businesses and cooperatives are allowed to flourish should be created by maximising local procurement opportunities, paying all suppliers within 30 days, and ensuring effective town planning and efficient network and internet systems. This will grow the local economy and increase the municipal revenue base which, in turn, will lead to improved financial health.
- Adopt appropriate measures to ensure that infrastructure projects are properly planned, effective and well coordinated. Discretion that leads to biased procurement processes should be eliminated and effective oversight exercised to ensure that projects are delivered on time, at the right quality and at the lowest possible price. The premier's office, provincial treasury and provincial Cogta should provide appropriate support to municipalities to ensure that they have the technical skills to undertake infrastructure projects.
- Ensure that all unauthorised, irregular as well as fruitless and wasteful expenditure is investigated properly and that those responsible for incurring it are held accountable. The premier's office, provincial treasury and provincial Cogta should provide support to the investigations process and also monitor that investigations are instituted and concluded.

The newly elected councils have assumed responsibility for ensuring responsive, accountable, effective and efficient local government as set out in the MTSF. It is their responsibility to act in a manner that will build public trust. This will be achieved by efficiently managing the limited municipal resources at their disposal and extending quality basic services to millions of households while upholding the laws and regulations governing the municipal environment and promoting anti-corruption initiatives, thus contributing to improving the lives of the communities they represent.

12.2 Free State



The steady improvement in audit outcomes in the previous two years, which included a notable reduction in the number of disclaimed opinions in 2014-15, could not be sustained by the cut-off date for the inclusion of results in this report. This stagnation, as evident from the figure above, is demonstrated by four improvements and three regressions. Fezile Dabi District improved from an unqualified opinion with findings to a clean audit, while Xhariep District, Kopanong and Moqhaka improved from qualified opinions to unqualified opinions with findings. We are encouraged by the accountability shown by management to strengthen the key control environment at these municipalities where year-on-year improvements have been realised since 2013-14.

These improvements were diminished by the regression of Thabo Mofutsanyana District from a clean audit to an unqualified opinion with findings, while Naledi and Masilonyana regressed from qualified opinions to disclaimed opinions. At the municipalities that regressed, the leadership failed to continuously strengthen the foundation of internal controls and the monitoring thereof. An example of such a failure was at Masilonyana where there was instability in the municipal manager and CFO positions over the last three years. Naledi, which was amalgamated into Mangaung Metro, regressed as documentation was not available during the audit process, as staff had already taken up other employment due to uncertainty regarding their job security.

The audit results of Mangaung Metro (consolidated financial statements) and Maluti-A-Phofung, Matjhabeng and Phumelela, which represented 56% of the province's municipal budget, were not finalised before the cut-off date for this report. As the internal control environment remained weak, these municipalities submitted financial statements late in an attempt to improve or sustain their previous year's audit outcomes. All four audits were subsequently finalised. The audit outcomes of Mangaung Metro and Phumelela were unchanged at unqualified with findings. Maluti-A-Phofung and Matjhabeng improved from a disclaimed opinion to a qualified opinion and an unqualified opinion with findings, respectively. These improvements were mainly as a result of the leadership's commitment to address the previous year's audit findings and the focused interventions of consultants.

During the three years, the province struggled to make significant progress towards a clean audit status due to weaknesses in the internal control environment, especially in the area of compliance with legislation.
Most municipalities were content to stagnate at an unqualified opinion with findings. Furthermore, in 2013-14 we conducted roadshows at six of the nine municipalities that had received an unqualified opinion with findings to encourage the leadership to address the internal control weaknesses and enforce accountability. Despite these

engagements and continuous quarterly interactions thereafter, only Thabo Mofutsanyana District was able to improve to a clean audit status even though this was not sustained. The stagnation in audit outcomes at unqualified opinions with findings was due to the leadership's minimal effort to address transgressions regarding compliance with legislation and transparent reporting of performance information even where they knew the transgressors. This created an environment where these actions were tolerated.

The weak internal control environment was also evidenced by the significant number of material adjustments to the financial statements required at 85% of the municipalities. Had these adjustments not been made, only Setsoto, Fezile Dabi District and Lejweleputswa District would have received financially unqualified audit opinions. The poor quality of financial statements was due to municipalities being complacent, as they relied on the audit process and consultants to identify shortcomings and produce credible financial statements despite their CFOs meeting the minimum competency requirements. This indicates a lack of monitoring and supervision, as CFOs did not review the financial statements and the relevant supporting information before submission. Inadequate skills and/or vacancies in finance sections also contributed to the poor implementation of internal controls over accurate and complete financial information. This created an over-reliance on consultants in the province for a number of years, with limited review of their work. This was demonstrated where a service provider incorrectly updated the billing system, resulting in incorrect billings to customers and postings to the general ledger without the errors being detected by the CFO. This breakdown in controls resulted in a loss of revenue and material adjustments to the financial statements.

There was a noticeable improvement in the reported performance information, as 10 municipalities had material findings in the year under review compared to 15 in the previous year. However, six of the 10 municipalities with no findings required material adjustments to their performance reports to avoid findings. Despite the improvement, inadequate record management due to a lack of transparency to measure the municipalities' performance still resulted in material findings. This hampered the communities' ability to hold municipalities accountable.

The leadership failed to confront non-compliance with legislation, as we still raised material compliance findings at 95% of the municipalities. Findings on the prevention of unauthorised, irregular and fruitless and wasteful expenditure and findings on compliance with SCM prescripts continued to be obstacles to clean audits, which resulted in irregular expenditure of R361 million for the year under review. Apart from the reported high occurrence of irregularities, Mafube (which received a disclaimed opinion) did not disclose any irregular expenditure in the financial statements for 2015-16, which is an indication that the total amount of irregular expenditure could be higher. The main area of non-compliance with SCM prescripts that resulted in irregular expenditure was procuring without competitive bidding or quotation processes. There was an increased tendency of municipalities avoiding competitive bidding processes by approving deviations on the basis of it being an emergency, whereas it was in fact due to poor planning. Municipalities also increased the use of contracts secured by other organs of state without meeting the requirements as stipulated in SCM regulation 32, while the financial benefit from these contracts could not always be demonstrated. The continuous disregard for procurement processes by the administrative and political leadership, coupled with limited consequences for these transgressions, is concerning as it creates an environment conducive to the misappropriation and abuse of state funds. Despite the known levels of transgressions, councils at 11 municipalities did not investigate unauthorised, irregular and/or fruitless and wasteful expenditure.

The overspending of budgets, occurrence of fruitless and wasteful expenditure and lack of transparent procurement processes to ensure that the best prices were obtained, placed further pressure on an already weak financial position of local government. This, together with the leadership's lack of accountability for sound financial management, and the diverted attention to the upcoming elections, had a negative impact on municipalities' financial sustainability. Excluding the districts, municipalities' financial health deteriorated from a net current liability position (where current liabilities exceed current assets) of R1,4 billion to R1,9 billion. These municipalities faced significant cash-flow constraints, as they did not maximise the revenue from service charges and rates or the collection of amounts outstanding from consumers. Given these cash-flow constraints, municipalities fell behind in their payments to Eskom (R1,2 billion) and water boards (R404 million) for their bulk purchases of electricity and water, which were outstanding at 30 June 2016. Furthermore, a number of municipalities deducted amounts from employees' salaries, such as pay as you earn, medical aid and pension fund contributions, but did not pay these amounts over to the relevant third parties, which could result in litigation.

Municipalities were also responsible for infrastructure assets with a net book value of R14,7 billion. Based on the National Treasury's budget circular, municipalities should budget for 8% of their infrastructure assets' net book value as maintenance. However, municipalities only spent 1% (which amounted to R184 million) on maintenance, resulting in a shortfall of R1 billion. This had a negative impact on service delivery in the province. Municipalities further incurred significant electricity and water distribution losses of at least R420 million due to theft, illegal connections, poor monitoring of indigents' consumption, and poorly maintained infrastructure.

Due to the continued drought and lack of maintenance, water-related infrastructure projects were a main focus area in the province. The delays in the finalisation of projects and poor project management were concerning. We further noted the following:

- Continued water losses were incurred.
- No approved policy that addressed routine maintenance of water infrastructure existed.
- There was no plan for the maintenance of water infrastructure, which set specific time frames and targets.
- Conditional assessments of water infrastructure were not done to inform the routine water infrastructure maintenance plan and budget.
- The maintenance of water infrastructure was not budgeted for.
- Targets for the provision of water services were not achieved.
- Indicators for the provision of water were not planned or reported.
- Delays in completing water projects were noted.

An example of a delayed project was where the consulting engineer initially indicated that a pipeline could be built from a hill directly downwards towards the river, but then realised that the slope was too steep and the pipeline had to be built around the hill. This resulted in variation orders and delays. There were further delays in the next phase due to inadequate contract management, poor performance by contractors and disputes between contractors and the consulting engineer, resulting in the community still not having access to running water. Importantly, the required procurement processes were not followed in the appointment of some of the contractors and the consulting engineer, which resulted in irregular expenditure.

A lack of accountability was evident in the province, as the assurance providers in local government did not take ownership of their annual commitments to implement basic key controls to ensure a sound control environment and implement consequences for poor performance and transgressions. The practical challenges facing local government require the political and administrative leadership to take ownership of the current state of affairs and to build a public service characterised by accountability and transparent financial and performance reporting. They can do this by focusing on the following:

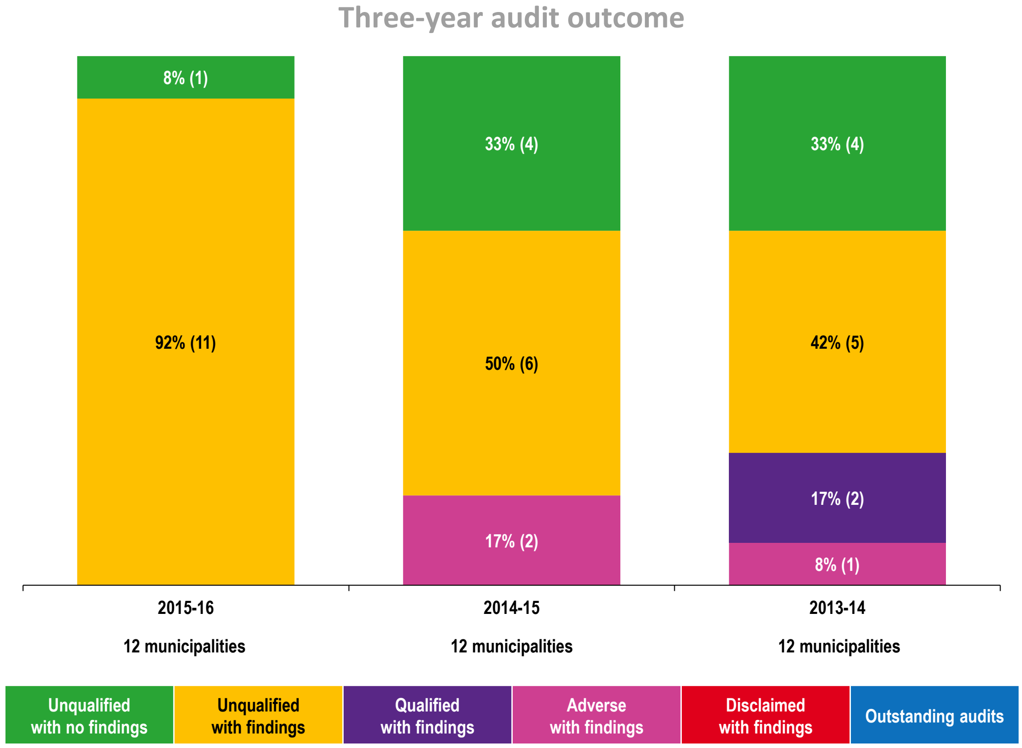
It is the responsibility of all key stakeholders to bring about accountability for improvements in all the disciplines to be realised. If care is taken in all these disciplines, there will be more funding available for service delivery.

- Strengthening key controls so that they become institutionalised, thus creating an environment conducive to sustainable positive audit outcomes.
- Setting a tone that informs the seriousness and urgency with which appropriate action plans and initiatives are implemented and monitored.
- Taking decisive steps and showing zero tolerance for deviations from SCM processes.
- Ensuring the effective, efficient and economical use of resources for service delivery.

The coordinating departments play a key role in ensuring that sound financial and performance management principles are implemented, thereby building trust and credibility, as well as institutionalising accountability in local government. In this respect, the provincial treasury and provincial Cogta need to continue their assistance and support to municipalities with a history of disclaimed opinions where audit outcomes subsequently improved to ensure the sustainability of these improvements. Furthermore, the coordinating departments should urgently intervene at Mafube, as it has received disclaimed audit opinions for more than a decade.

Effective monitoring and oversight by all assurance providers are essential to break the cycle of impunity and improve fundamental internal controls. The newly elected political leadership should ensure that municipal staff accept responsibility for their actions and should prompt for a responsive, accountable, effective and efficient local government as set out in the MTSF. Mechanisms to promote accountability typically include basic daily and monthly checks and balances on compliance and financial and performance information, managing the performance of staff, and implementing consequences for poor performance and transgressions. Accountability and transparency are considered the main pillars of good governance. Sustainable clean audits will only be achieved through a strong foundation of good governance.

12.3 Gauteng



The Gauteng local government audit outcomes regressed in 2015-16, with one municipality (8%) obtaining a clean audit outcome compared to four municipalities (33%) in both 2014-15 and 2013-14.

Three municipalities (Ekurhuleni Metro, Sedibeng District and Mogale City) regressed in 2015-16 from a clean audit to an unqualified opinion with findings. The regression at Ekurhuleni Metro and Mogale City was due to compliance with SCM prescripts not being monitored adequately, while the regression at Sedibeng District was as a result of a lack of adequate processes to ensure the usefulness and reliability of reported performance information.

Midvaal is commended for obtaining a clean audit outcome in 2015-16 and for sustaining this outcome for the last three years. This was as a result of the municipality institutionalising a number of best practices, which should be replicated across the province, such as monitoring the implementation of action plans to ensure that internal control deficiencies are addressed, maintaining stability in key positions, ensuring that governance structures are effective, and effectively applying consequence management. This in effect created a culture of accountability.

With transparency having been introduced, limited resources will be utilised more effectively.

Commendably, Gauteng is moving in the right direction as 100% of municipalities obtained an unqualified opinion. The achievement of this significant milestone was due to two municipalities in the West Rand district (Randfontein and Westonaria) improving from adverse opinions with findings to unqualified opinions with findings, thereby joining the ranks of the other 10 municipalities in the province that had obtained unqualified opinions over the last few years. The political leadership of these two municipalities held the administrative leadership accountable for implementing action plans that were responsive to internal control deficiencies and root causes. This was significantly influenced by the effective use of consultants (with the assistance of coordinating departments such as the provincial treasury and provincial Cogta) to assist in resolving the previous year's qualification areas, particularly relating to assets at both municipalities. The administrative leadership of Rand West City, which was established following the merger of Randfontein and Westonaria after the recent local government elections, should ensure that there is an adequate transfer of skills to sustain the unqualified opinion.

Although metros and district municipalities should lead by example in the local government sphere, all three metros and both district municipalities obtained unqualified opinions with findings. The City of Johannesburg Metro remained stagnant with an unqualified opinion with findings due to a number of control deficiencies relating to record management and the processing, reporting and reconciling of transactions. Furthermore, action plans did not address the root causes, resulting in repeat findings on, among others, material misstatements in the financial statements, non-compliance with legislation (including SCM prescripts) and inadequate performance reporting. Similarly, the City of Tshwane Metro remained stagnant with an unqualified opinion with findings. Although there was an improvement in performance reporting, there were repeat findings on material misstatements in the financial statements and non-compliance with legislation. This was due to inadequate review processes by finance officials and inadequate monitoring of compliance with SCM legislation. To enable the province to improve its audit outcomes, the political leadership should hold the administrative leadership accountable for the institutionalisation of internal controls and basic financial management practices. Furthermore, a culture of accountability together with timely and effective consequence management for non-performance and transgressions should be enforced.

Consistent with previous years, all municipalities (100%) submitted their financial statements for auditing on time. The quality of the financial statements can be improved, as seven municipalities (58%) had material misstatements in their financial statements that were identified and corrected during the audit. This was as a result of CFOs and finance officials not taking responsibility for implementing basic financial disciplines, such as regular reviews of financial information during the year, to ensure the credibility of the reported financial information. The continued reliance on auditors to identify errors in the financial statements, which are then corrected by municipalities to avoid qualifications, is not a sustainable practice.

The audit outcomes on reported performance information improved, as the number of municipalities with findings on the usefulness and reliability of their performance reports decreased from seven (58%) in 2014-15 to four (33%) in 2015-16. The quality of the performance reports submitted also improved, as the number of municipalities that submitted performance reports with material misstatements decreased from nine (75%) in 2014-15 to seven (58%) in 2015-16. This improvement in reporting on the extent of service delivery was due to municipalities implementing recommendations to ensure that their performance criteria were SMART (specific, measurable, achievable, relevant and time bound) and the stringent internal verification of reported performance information. The political and administrative leadership should continue to hold heads of monitoring and evaluation units accountable for the accurate reporting of performance information. This, in turn, allows residents to hold elected officials accountable for the service delivery targets contained in their approved service delivery and budget implementation plans.

Compliance outcomes regressed, as the number of municipalities with findings on compliance with legislation increased from eight (67%) in 2014-15 to 10 (83%) in 2015-16, with the most common findings relating to procurement and contract management, the prevention of unauthorised, irregular and fruitless and wasteful expenditure, and the quality of submitted financial statements. This was due to the slow response, diverted leadership attention due to the elections and lack of urgency by the administrative leadership to address compliance findings relating to uncompetitive or unfair procurement processes. As highlighted in the previous year, non-compliance with legislation remained the major obstacle preventing most municipalities from attaining clean audit outcomes.

Irregular expenditure remained high at R1,5 billion (2014-15: R1,5 billion). Systems to detect and record irregular expenditure continued to be a concern, as only 18% of the irregular expenditure was identified by the municipalities. The three metros were the highest contributors to irregular expenditure, accounting for R976 million (65%). The administrative leadership should be held accountable for strengthening the controls necessary to adhere to SCM prescripts and to prevent irregular expenditure. SCM officials should also be further trained on the application of SCM regulation 36, which is often incorrectly applied across the local government sphere. Where irregular expenditure is incurred, it should be properly investigated and appropriate consequence management should be instituted against transgressors.

The municipal entities' audit outcomes regressed from 11 clean audits (52%) in 2014-15 to nine (41%) in 2015-16. Two entities of the City of Johannesburg Metro, namely Pikitup Johannesburg and Johannesburg

Roads Agency, could not sustain their clean audits of the previous year and regressed to an unqualified opinion with findings in 2015-16. This was due to material non-compliance with legislation, particularly in respect of material misstatements in the financial statements and inadequate contract management.

In the context of the current economic climate, municipalities' financial health remained constrained, as they experienced difficulty in collecting debt from municipal consumers for basic services. Municipalities should focus particularly on improving debt-collection processes and prudent financial spending to ensure that they are still able to provide essential services to their citizens.

The status of the IT environment remained a concern, as municipalities still experienced challenges with implementing basic IT security and user access policies and procedures. CIOs and municipal managers should prioritise the implementation of these controls and ensure that action is taken where there are repeat findings. We are also concerned that none of the municipalities had demonstrated that they will be ready for the implementation of the mSCOA project by the set implementation date of July 2017. This should be prioritised to enable the province to meet the implementation date.

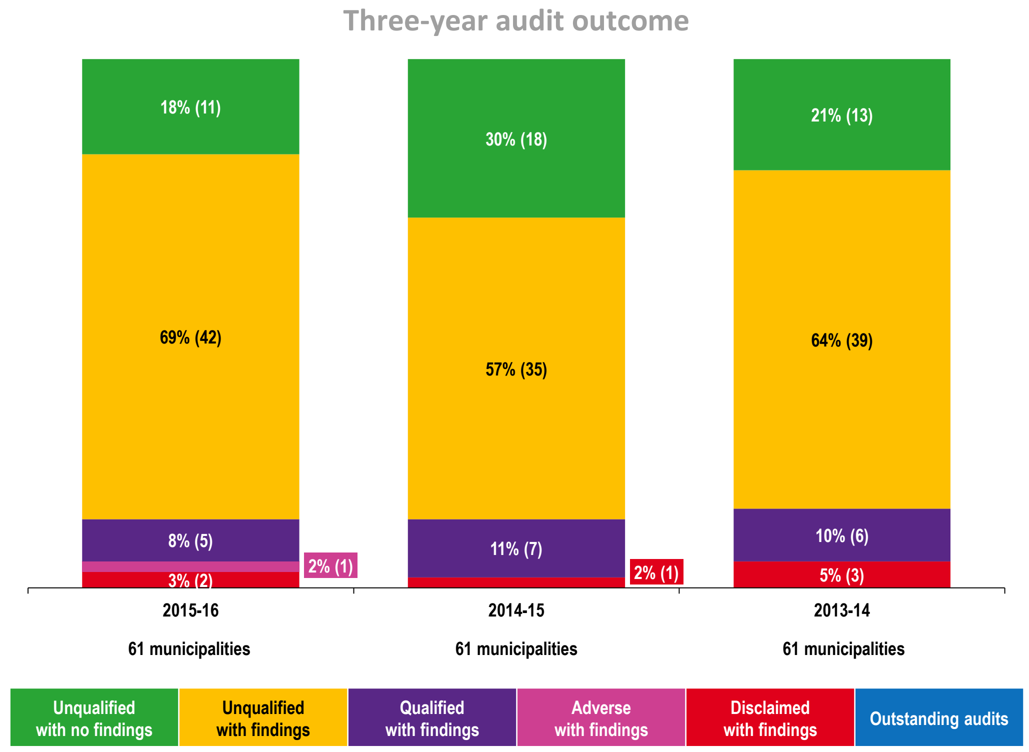
Our analysis of water infrastructure found, among others, that conditional assessments to inform the water infrastructure maintenance plan and budget were not performed at two municipalities (City of Tshwane Metro and Westonaria). There were also no approved water infrastructure maintenance policies at three municipalities (City of Johannesburg Metro, City of Tshwane Metro and Lesedi). These weaknesses could have an adverse impact on these municipalities' ability to deliver key basic services.

Large-scale infrastructure projects such as the integrated rapid public transport network at the metros had generally been successfully implemented and goods and services were received for the money spent. However, some quality issues were identified during site visits, such as the deterioration of bus lanes due to a lack of maintenance and the use of poor-quality materials in the construction of lanes at the City of Tshwane Metro. At Ekurhuleni Metro, a large number of variation orders were issued due to poor planning and designs. Other capital projects visited included Fleurhof at the City of Johannesburg Metro, which is the biggest housing project in the province, with approximately 11 000 mixed development units being constructed. Overall, the units built were of the required basic quality with an improvement in the standard of workmanship noted from the previous year.

The level of assurance provided regressed across the majority of role players. Senior management's slow response to implementing internal control disciplines and vacancies in key positions were root causes of municipalities not achieving a clean audit. Municipal managers should take ownership of the audit outcomes by holding senior management accountable for implementing the required controls to ensure compliance with legislation and to enable credible financial and performance reporting.

Key role players continued to be committed to improving the level of support provided to municipalities and intensifying oversight. Coordinating departments contributed to improved audit outcomes at Randfontein and Westonaria where commitments were implemented. We encourage key role players to sustain and intensify the support provided to other municipalities in the province going forward. This will translate into improved audit outcomes across the province as demonstrated by the impact of the intervention at the two municipalities in the West Rand district. We will therefore continue to monitor the impact and progress of the commitments made, as they are critical enablers to improving the overall audit outcomes in the province.

12.4 KwaZulu-Natal



The KwaZulu-Natal local government audit outcomes regressed in 2015-16 after a notable improvement in 2014-15. Eleven municipalities (18%) received clean audit opinions compared to 18 (30%) in 2014-15 and 13 (21%) in 2013-14. In terms of the budget, municipalities with clean audits represented 13% of the total provincial municipal expenditure budget of R66 billion for 2015-16. Municipalities with unqualified opinions constituted 76% of that budget, while those with qualified opinions represented 9% and those with adverse and disclaimed opinions accounted for 2%.

eThekwini Metro regressed from a clean audit to an unqualified audit opinion with findings on compliance. The metro's routine monitoring controls over procurement processes were not sufficient to prevent repeat instances of irregular expenditure. Zululand District also regressed to an unqualified opinion with findings in 2015-16 after retaining consecutive clean audits for the previous two years. This was due to a lack of oversight and review procedures over compliance with legislation and a failure to implement daily and monthly controls for processing and reconciling transactions. Msunduzi regressed from a clean audit to a qualified audit opinion with findings due to a systemic breakdown of key controls, as the municipality implemented a new organisational structure and decentralised key finance functions. The audit outcomes of five of the municipalities that were affected by the re-demarcation also regressed. The overall regression in the province was due to management not decisively responding to the breakdown in key control activities due to a lack of understanding of applicable financial and reporting requirements. Some municipalities also lacked clear lines of accountability and decisive direction due to vacancies in key positions, such as municipal manager posts that were not filled in good time to promote a sound control environment. Furthermore, the leadership did not act swiftly to ensure that commitments in the action plans were monitored regularly, as attention was diverted by the upcoming elections.

Newcastle notably improved its audit outcome from a qualified opinion with findings to an unqualified opinion with findings for the first time since 2007-08. This improvement stemmed from resolute leadership and a decisive approach to oversight and monitoring, especially of key financial statement account reconciliations and previously reported significant control deficiencies.

Three of the 10 district municipalities (Ilembe, uThungulu and Umgungundlovu) led by example in retaining their clean audits since 2013-14. These municipalities were characterised by leadership's zero tolerance for poor performance and commitment to good governance, coupled with institutionalised sound financial management disciplines and internal controls.

The provincial treasury, provincial Cogta and premier's office provided intensive support to Newcastle, Jozini, Hlabisa, Amajuba District, uThukela District and uMkhanyakude District that had displayed persistent control weaknesses. The support strengthened the overall state of governance and administration of these councils and resulted in five municipalities improving their audit outcomes since 2013-14, while uMkhanyakude District displayed a slight regression.

The quality of submitted financial statements remained a challenge, as management and oversight structures did not diligently and intensively review the financial statements on time for material omissions and misstatements. A total of 26 municipalities (43%) avoided qualifications only because they corrected the material misstatements that we identified during the audit process. Their reliance on auditors to identify errors is not a sustainable practice and municipalities should be proactive in addressing weaknesses in their internal annual financial reporting processes. Overall, 51 municipalities (84%) used consultants for their financial reporting at a total cost of R158 million, compared to the R117 million spent by 50 municipalities (82%) in 2014-15. These amounts exclude consultants paid by the provincial Cogta and provincial treasury. Of these, the financial statements of 19 municipalities (37%) still required material corrections in areas that were within the consultants' scope of work. To derive the most value from the use of consultants, they should be appointed on time, provided with the required records, and managed effectively.

Eight municipalities received qualifications in some areas of their financial statements, mainly because they did not provide supporting documentation. Furthermore, changes in leadership and key vacancies in the finance section, coupled with political infighting and the late involvement of consultants, were additional contributors at those municipalities that received disclaimed or adverse opinions. These qualifications largely related to expenditure, revenue and irregular expenditure.

Reporting on performance information improved, as 18 municipalities (30%) had material findings in 2015-16, compared to 24 municipalities (39%) in 2014-15. Daily and monthly checks and balances, regular and accurate reporting as well as effective oversight and risk management resulted in improved performance reporting. However, 26 municipalities (43%) avoided findings on reported performance by correcting the misstatements that we identified during the audit process. The municipalities that could not provide credible performance reports managed R8 billion (12%) of the total provincial local government budget. To further improve the quality of performance reports, accounting officers should provide effective oversight and hold the responsible officials accountable for the preparation of credible performance reports.

Senior management's response to implementing action plans was slower than expected, resulting in material non-compliance with legislation at 50 municipalities (82%) in 2015-16, compared to 42 (69%) in 2014-15. A significant contributor to this regression was the increase in material findings on the lack of consequence management, from 16 municipalities (26%) in the previous year to 25 (41%) in 2015-16. Disciplinary boards had not been set up to deal with and investigate instances of fraud and misconduct. In addition, policies and procedures to deal with consequences and performance management were not strictly applied, and investigations into unauthorised, irregular and fruitless and wasteful expenditure were unduly delayed. This created an environment where poor performance was tolerated, which was not conducive to good governance and accountability. Other common findings related to the quality of submitted financial statements, the prevention of unauthorised, irregular and fruitless and wasteful expenditure, and SCM.

The status of SCM and related controls regressed, with 56 municipalities (92%) reporting findings in 2015-16, compared to 52 (85%) in 2014-15. Procurement without competitive bidding or proper quotation processes, and general non-compliance with procurement processes, saw irregular expenditure levels increasing from R1,60 billion in the previous year to R2,43 billion in 2015-16. Pre-submission compliance checklists were not always reviewed and monitored before goods and services were procured. Five municipalities (uThukela District, uMkhanyakude District, uMzinyathi District, eThekwini Metro and Msunduzi) contributed R1,24 billion (51%) to the total irregular expenditure. The main cause of this irregular expenditure was deviations that were either not approved or not justifiable. Of the R1,50 billion in irregular expenditure audited, 95% of the goods and services were confirmed as received, despite the normal procurement processes not having been followed.

Unauthorised expenditure increased from R1,13 billion in 2014-15 to R1,62 billion in 2015-16. The majority of this was caused by non-cash items, such as depreciation and impairment of debtors, being incorrectly estimated during the budget process. Five municipalities (Newcastle, uMhlathuze, Ugu District, uThukela District and Harry Gwala District) contributed to R1,10 billion (68%) of the total unauthorised expenditure.

The slow collection of debt had a negative impact on municipalities' financial health. In total, 72% of the municipalities (2014-15: 64%) estimated that more than 10% of the amounts owed to them would not be paid and had an average debt-collection period of over 90 days. The severe drought in the province also resulted in revenue from water decreasing due to water restrictions being imposed. The drought crisis was made even worse by the high amount of water losses reported. Water losses can be reduced by effectively maintaining water infrastructure, addressing maintenance backlogs and replacing assets at proper intervals.

Road infrastructure projects in the province were mostly completed on time and within budget. Where projects were not completed or started, this was as a result of budget constraints. Many municipalities did not have an approved policy for the planning, management and reporting of road infrastructure projects and an approved road maintenance plan or priority list for the renewal and routine maintenance of roads.

Basic controls are still not being embedded in daily and monthly processes to prevent non-compliance with legislation.

The drivers of key controls relating to leadership and to financial and performance management regressed while those in respect of governance were stagnant. The leadership did not monitor the implementation of action plans to address compliance with legislation and was slow to fill critical vacancies. Record management, and processing and reconciling key accounts and transactions, also showed weaknesses. These areas are fundamental to supporting credible and reliable financial and performance reporting as well as strengthening accountability.

The dominant root cause of most of our findings was management's slow response. The leadership was slow in filling vacancies in key positions and support staff positions. This had a negative impact on outcomes as daily and monthly controls were not adequately performed, which resulted in control environments that did not contribute to accountability and good governance. Additionally, financial constraints at smaller municipalities and municipal demarcation changes contributed to positions remaining vacant. Some municipalities also failed to implement adequate succession planning, which resulted in a loss of institutional knowledge and a lack of embedded controls.

mSCOA, to be implemented on 1 July 2017, was piloted at two municipalities in the province (Umgungundlovu District and Umhlathuze) in the 2015-16 financial year. mSCOA has an impact on how information will be recorded and classified in the 2017-18 financial statements of all municipalities. Neither piloted municipality had material findings on their financial statements. While municipalities demonstrated improvements in IT controls, most have not fully attuned their systems and processes for mSCOA. Therefore, the leadership must direct concerted attention to addressing the mSCOA implementation risks.

The level of assurance provided by the executive and administrative leadership as well as senior management regressed. Mayors at 43 municipalities (70%) provided some or limited assurance. Their oversight of the credibility of reporting was not effective and their responses to honouring commitments made to address the previous year's audit findings were slow.

A majority of accounting officers (82%) did not adequately oversee the preparation of financial and performance reports or compliance with legislation. Their involvement was also limited when it came to monitoring the implementation of internal and external audit recommendations in a manner that created an environment of accountability. In addition, senior management at 49 municipalities (80%) did not stringently and diligently review the credibility of financial, performance and compliance reports.

Internal audit units and audit committees at 29 municipalities (48%) did not ensure that their reviews of financial and performance reports and compliance with legislation were sufficient to detect material errors, omissions and non-compliance. In most instances, senior management did not implement internal audit and audit committee recommendations, resulting in the internal control environment not being strengthened.

Overall, 66% of municipal councils and MPACs did not oversee officials and hold them accountable for verifying the credibility and reliability of financial and performance reports as well as compliance with SCM and other legislation. Findings recurred as a result of the outgoing councils not honouring commitments.

The provincial Cogta's initiatives to improve compliance monitoring did not reduce unauthorised, irregular and fruitless and wasteful expenditure. However, the provincial treasury's municipal support programme did assist some districts to reduce the number of compliance findings reported and improve the quality of performance reporting. The district mayors' coordinating forums should have reported their progress and concerns to the premier's coordinating forums, but some of the planned meetings did not take place.

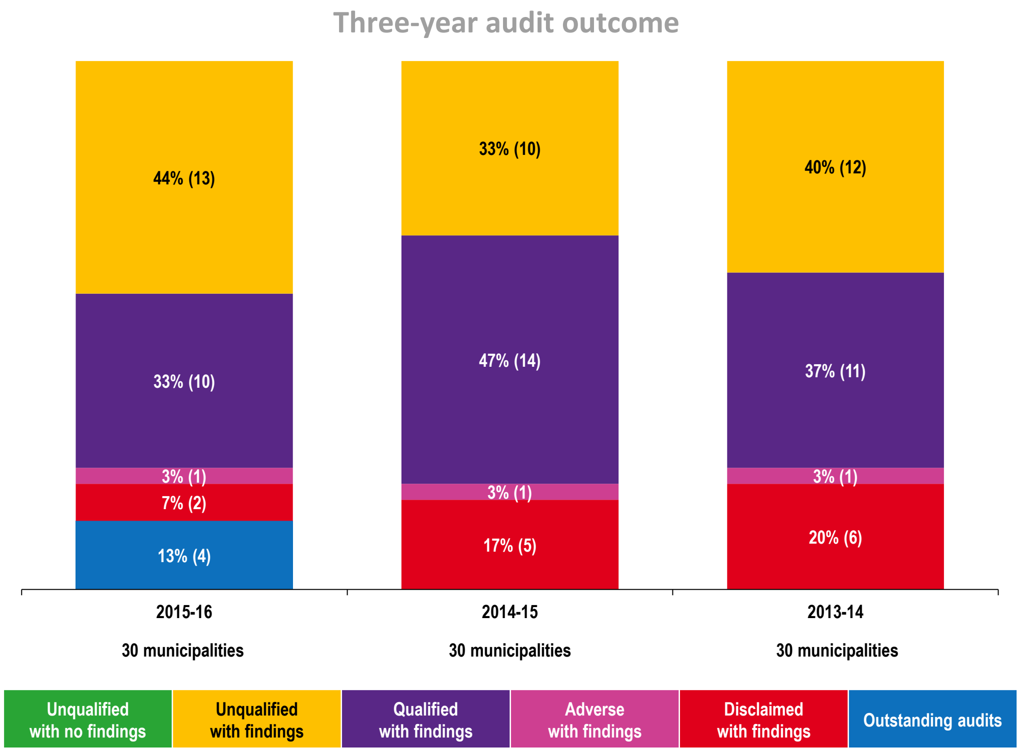
The provincial Cogta, provincial treasury and premier's office must diligently monitor the implementation of the support programmes at district level. This will assist municipalities to build and maintain sound institutional and administrative capabilities. These coordinating departments must also work together intensively to forge impactful relations and provide targeted training and support to municipalities in dire need.

The newly elected councils should implement the actions below to improve audit outcomes. The leadership should regularly monitor these actions to increase accountability and consequences for transgressions at all levels, and to instil financial discipline and prudence.

- The leadership should ensure that competent people are employed in financial and SCM positions. These individuals should embrace accountability and take responsibility for their actions, coupled with a comprehensive understanding of key policies, processes and procedures.
- The administrative and political leadership should set a tone of zero tolerance for transgressing legislation. Punitive action should be taken against those that breach legislative requirements.
- Both the administrative and political leadership must monitor engagements with new councils on the status of key controls, including previous commitments made that have a direct impact on the audit outcomes.
- Councillors need to fully understand their oversight responsibilities to be effective in their roles. The provincial Cogta and Salga need to intensify induction and training programmes for councillors and MPACs for these oversight structures to be effective.
- Audit committees, internal audit units and risk committees need to strengthen their roles in risk oversight and review to fortify governance, accountability and the sustainability of controls.

In order for local government to position itself to achieve the goals as set out in the MTSF, it is vital that the leadership and management diligently execute their responsibilities – resulting in a professionalised local government that embraces the concepts of transparency and accountability. The enabling role of the accounting officer and the oversight functions of councils will play an important part in creating an environment where effective, efficient and economical service delivery and a clean audit are natural products of performing the correct actions.

12.5 Limpopo



The local government in Limpopo consists of 33 auditees, made up of five district municipalities, three municipal entities and 25 local municipalities. At the cut-off date of 15 January 2017, the audit outcomes of four auditees were still outstanding and are therefore not included in this provincial summary. To date, Thabazimbi had not submitted its financial statements for auditing. Mogalakwena and Mutale submitted financial statements after the legislated date of 31 August and received an adverse and qualified opinion, respectively. Although Greater Giyani submitted its financial statements on time, the audit had not been finalised by the legislated deadline of 30 November due to a number of audit issues relating to property, plant and equipment and the cash flow statement that had to be addressed. The audit was subsequently finalised and the municipality again received a qualified audit opinion.

The 2014-15 financial reporting period was concluded with a stern warning by the premier to all mayors, municipal managers and CFOs that disclaimed and adverse audit opinions would not be tolerated. He made it clear that drastic action would be taken against municipalities that continued to receive such audit opinions. The premier further insisted that an addendum be attached to the performance contracts of all municipal managers to include audit outcomes as a performance indicator in order to ensure accountability. A number of resolutions were also made, which included commitments by the coordinating departments (provincial treasury, provincial Cogta and premier's office) to provide assistance to municipalities where skills and capacity constraints remained a challenge.

Following the warning issued by the premier, we noted an increased focus by municipalities to resolve audit findings that had led to qualifications. Our office held a number of engagements to explain the root causes of audit findings and to develop strategies to resolve these findings. As a result, we saw an improvement in the number of auditees that received unqualified audit opinions with findings from 12 to 16 and a decrease in disclaimers from four to two (excluding the outstanding audits of Mogalakwena and Thabazimbi that had been disclaimed in the prior year). Improvements at most municipalities were consultant-driven, rather than as a result of a concerted effort by the leadership to address internal control deficiencies. The continued reliance on consultants is unsustainable due to the continued instability in leadership positions.

Instability, highlighted by the number of vacancies at administrative leadership level at the 2015-16 year-end, particularly at the level of municipal manager (five vacancies) and CFO (nine vacancies), is a serious concern that contributes to a poor internal control environment. We noted that a number of positions were vacant for most of the year and were only filled at year-end. At a number of municipalities with vacancies at municipal manager and/or CFO level, we also noted a trend of appointing senior managers to act in these positions on a rotation basis (every three months to avoid compliance findings on acting positions). Such acting positions are not normally accompanied by the required commitment and accountability that constitute good governance. We further observed that during acting periods, non-compliance with legislation increased, particularly in the area of SCM. For example, at Vhembe District most of the officials at senior manager level were acting in their positions, while the posts of municipal manager and CFO had been vacant for 18 and 14 months, respectively. This instability contributed to the irregular expenditure of R181 million incurred by the municipality in the year under review.

As long as we have such high levels of irregular expenditure, with no consequences for responsible officials, we will not be able to deliver the required level of services to our people.

The instability in leadership also had an impact where municipalities implemented water projects without conducting proper feasibility studies, resulting in large infrastructure assets not being used after commissioning and left idle, increasing the risk of vandalism. Some of the contributing factors were poor planning, a lack of accountability and very limited or no consequence management. In the Mopani and Vhembe districts, for example, boreholes were sunk and completed, but on commissioning, the infrastructure could not operate as there was no underground water or electricity.

The accumulated amounts of unauthorised, irregular as well as fruitless and wasteful expenditure totalled R2 billion, R4 billion and R135 million, respectively. These amounts have been accumulating over a number of years and it is likely that information relating to the nature or cause of this expenditure may be lost due to poor record management and loss of institutional knowledge due to staff turnover or changes in the political landscape. The problem was made even worse by the instability at administrative leadership level, which could make it almost impossible to hold officials accountable. We identified poor planning resulting in ad hoc decisions, with no consideration of legislation, as a root cause in this regard. This was made even worse by a weak internal control environment, because the administrative leadership failed to set the right tone by enforcing adherence to legislation and holding officials accountable. At the root of this was the delay by councils to conduct and conclude their investigations, together with a lack of adequately capacitated oversight structures (such as MPACs), which play a critical role in the accountability cycle.

To address these matters, we recommend the following:

- The appointment of officials in acting positions should be based on the performance of officials and not merely be done for compliance purposes. Municipalities should request assistance from the coordinating departments if resources are not available internally.
- The provincial Cogta and the provincial treasury should provide a platform from where MPACs can source the necessary skills on technical issues, including legal competencies housed in these departments and other spheres of government.
- The administrative leadership (accounting officers and senior management), the political leadership (mayors and councils) as well as oversight bodies (MPACs and portfolio committees) should respond with the required urgency to our consistent messages about accountability, consequence management and improving internal controls.
- A culture of accountability and consequence management must be entrenched at leadership level to prevent non-compliance that could result in potential financial losses.

As we have reported in the previous general reports, the quality of the financial statements and performance reports submitted for auditing continued to pose a challenge at almost all auditees. Consultants were more commonly used for functions relating to financial reporting rather than performance reporting, with 27 auditees using consultants for financial reporting and only one using consultants for performance reporting. Municipalities spent R106 million (2014-15: R110 million) on consultants to assist with the preparation of financial statements, asset registers and other finance-related functions such as bank, creditor or debtor reconciliations. One would expect that municipalities would use consultants to address their skills and competency gaps; however, we found that consultants were responsible for the total financial reporting function to such an extent that they became responsible for responding to audit queries raised during the audits. It is concerning that consultants are appointed to do work which in fact forms part of the role and responsibilities of CFOs and finance staff employed by municipalities. This lack of ownership of the financial reporting cycle is becoming a trend at most of the municipalities in the province. The administrative leadership should ensure that a culture of basic financial management discipline and adherence to good controls is entrenched and that consultants are appointed to bridge the skills gap with a practical skills transfer plan that is monitored regularly to ensure sustained performance.

There was no improvement in reporting on performance information, with municipalities still unable to set useful indicators and targets at the beginning of the financial year and to reliably report on actual achievement against these targets at year-end. Overall, 20 auditees had findings on the usefulness and 21 on the reliability of their reported performance information. The lack of standardised key performance indicators for basic service delivery functions performed by all municipalities resulted in inconsistencies in setting indicators and targets that were useful. The continued failure of municipalities to report reliably on performance information was due to inadequate systems and processes to integrate reporting of performance information into the financial reporting process.

The provincial Cogta hosts a quarterly performance monitoring and evaluation forum to discuss issues relating to reporting on performance. We also attend this forum and have observed that municipal officials do not take the forum seriously and do not implement resolutions adopted or guidance given. Where municipalities fail to implement the resolutions, we recommend that the MEC responsible for cooperative governance engage with the leadership so that officials who are failing in their duties are held accountable and face consequences. We also recommend that the provincial Cogta assist the municipalities by developing standard key performance indicators to be included in the service delivery and budget implementation plan of all municipalities. Municipalities should further document standard operating procedures, which should detail the documents required for reporting and the process of filing for record keeping.

A lack of effective and efficient debt-collection processes was evident at 26 municipalities, where a high percentage of debtor balances (ratepayers and consumers of water and electricity) had to be impaired. A total of 22 municipalities faced challenges with timely debt collection, with the average collection period exceeding 90 days. Most municipalities appointed debt collectors on a contingent-fee basis to improve their cash-flow position. We also noted a concerning arrangement at Ba-Phalaborwa where a debt collector was appointed to recover current debt (30 days), which pointed to a lack of accountability by the leadership and the relevant municipal officials for the efficient use of consultants.

The inability of municipalities to effectively plan their IT function to enable other administrative functions to discharge their responsibilities contributed to a weak internal control environment. Shortcomings in the IT environment had a direct impact on the sustainability and improvement of audit outcomes and on the achievement of service delivery objectives. The chairperson of Salga in Limpopo has stressed the need for one transversal financial management system to be used at all municipalities in the province. The provincial treasury is looking into this initiative to determine its benefits and viability.

The level of assurance provided by key role players regressed, particularly at the levels of senior management and municipal manager. This was due to vacancies and the lack of ownership of the financial and performance reporting process, as evident in the high reliance placed on consultants to perform finance functions. This confirms our overall assessment that key internal controls remained weak and that the administrative leadership had not developed processes to strengthen them.

The assessment of the council and MPAC as second- and third-level assurance providers, respectively, remained a concern. This was because instances of unauthorised, irregular as well as fruitless and wasteful expenditure were not timeously investigated to determine whether any person was liable for the expenditure. In addition, findings raised by internal audit units and recommendations provided by audit committees were not taken seriously. For the councils to effectively discharge their oversight role, it is critical that they engage with audit committees on risks and internal controls.

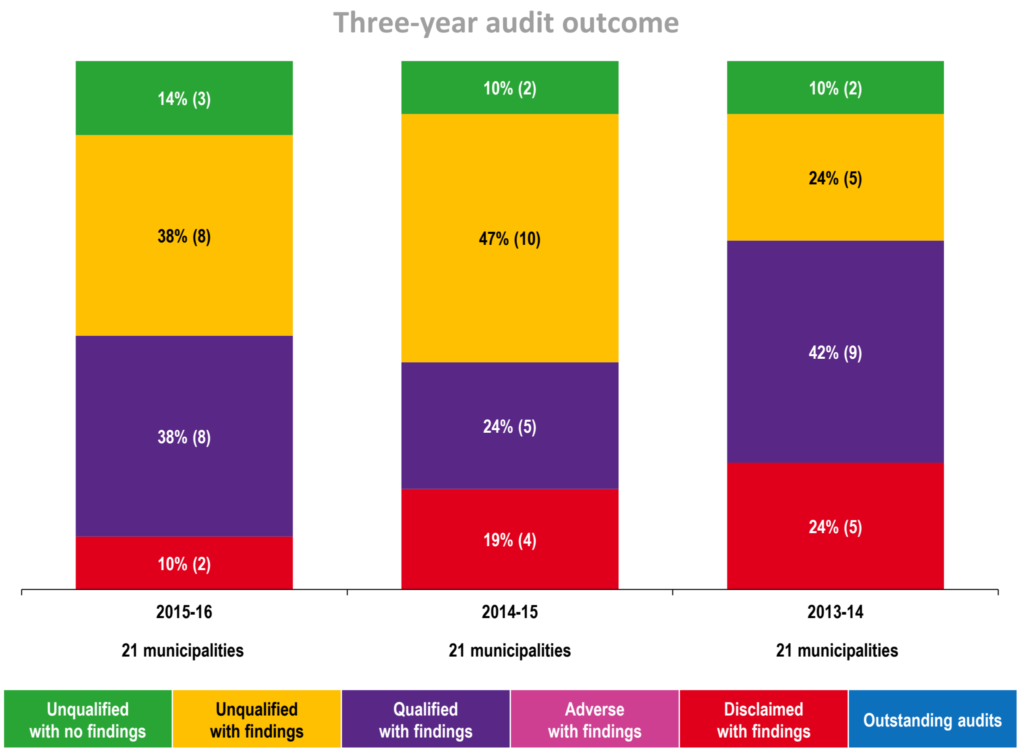
During the Limpopo local government summit in February 2017, the premier reiterated that persistent compliance findings and disclaimed audit opinions would not be tolerated. He made it very clear that not only would officials face consequences for disclaimed opinions, but that councils would also be held accountable. He also noted that vacant positions must be filled by people with skills and qualifications that were relevant to their positions. We will track the implementation of these commitments during the 2016-17 audit process to determine whether they have translated into tangible action, and report thereon.

The overall improvement in the audit outcomes is indeed encouraging but there are still significant deficiencies in the internal control environment, which should be given serious attention to bring about sustainable improvements. Once again, this was evident in the overall key control environment that had not improved in line with the improvement in audit outcomes. The municipal leadership needs to understand that the use of consultants will only be effective if a sound underlying control environment exists.

We commend those municipalities that have demonstrated the willingness, commitment and political will to improve their outcomes and financial administration. Fetakgomo is a point in case, as it has gradually improved from a disclaimer in 2013-14 to an unqualified opinion with findings in 2015-16. The political and administrative leadership was visibly involved throughout the audit process and during our in-year engagements. This proves that positive changes can be brought about if the tone at the top is governed by a culture of accountability and the political will to improve financial administration, which would ultimately benefit the citizens of Limpopo through improved service delivery.

The coordinating departments play a key role in ensuring that sound financial and performance management principles are implemented. Several commitments and resolutions were made at the provincial executive council lekgotla to eradicate maladministration and foster good governance. The premier further alluded to the importance of good governance and taking accountability in achieving clean audits. The success of the outcomes of these resolutions depends on effective and regular monitoring by these coordinating departments as well as the commitment of the municipal leadership. In this way, the level of governance and accountability required from local government in the province can be built.

12.6 Mpumalanga



Accountability is central to the attainment of clean administration. This involves defining and setting targets for achieving the strategic goals set in the integrated development plan, implementing basic internal controls with increased levels of supervision, adequate monitoring by all assurance providers, and instituting consequences for transgressions and a lack of action. The political leadership's acceptance of the responsibility to turn around the status quo at municipalities is central to the improvement of audit outcomes, which will in turn have a positive impact on the lives of citizens.

A strong and stable internal control environment provides a foundation for accountability, transparency and governance in the public sector. The administrative leadership had not prioritised the strengthening of internal controls at their institutions, but sought to implement short-term solutions to avoid qualified or disclaimed audit opinions. One such short-term measure was the appointment of consultants, the cost of which increased from R64,9 million in 2014-15 to R103 million in the current period. In addition, Salga and the National Treasury paid R18,4 million for consultants to assist with financial reporting.

This continued reliance on consultants, with little or no transfer of skills, remained one of the biggest challenges in the province. A total of 19 auditees (90%) used consultants to assist them in financial reporting, of which 52% still had poor audit outcomes due to significant weaknesses in internal control. While we acknowledge the need to appoint consultants to assist the public service, this must be needs-driven, with an emphasis on value for money, proper planning and monitoring, and the transfer of skills.

Further to over-reliance on consultants, seven of the 11 auditees that received unqualified audit outcomes made material amendments to their initially submitted financial statements as a result of errors identified during the audit process. This reliance on both consultants and the audit process to identify misstatements indicates that basic financial disciplines were not implemented throughout the year. The sustainability of the positive audit outcomes attained by these municipalities is therefore uncertain.

Basic financial management disciplines and observing controls, such as the prompt processing of transactions to ensure that accounting records are updated immediately, were still not in place at these auditees.
The weaknesses in internal control and poor financial management did not only affect the opinion on the financial statements, but also had an impact on the financial viability of these municipalities and resulted in an increase in unauthorised expenditure.

Poor revenue management by municipalities as well as a lack of implementation of controls to collect debts owed to them resulted in R6,9 billion (73% of the total debtors) being provided as doubtful debts during the 2015-16 financial period. This led to a delay in paying creditors (including Eskom), with an average creditor-payment period of 312 days, resulting in interest being charged. This was a major contributor to the fruitless and wasteful expenditure of R257 million (2014-15: R236 million). The lack of payments to Eskom does not only affect the finances of municipalities but ordinary citizens as well due to potential power outages by Eskom, thus affecting service delivery. This also puts further financial strain on municipalities, as evidenced by the increase in the net current liability position from R3,5 billion in 2014-15 to R4,4 billion in 2015-16.

The serious weaknesses in internal control and poor financial management were as a result of the slow response by management to implement sustainable long-term solutions aimed at strengthening the internal control environment. This was made worse by employees tasked to execute some of the measures to improve audit outcomes, lacking the required competencies to do so. The political leadership was also slow to ensure that consequences for poor performance and transgressions were instituted, thus creating an environment in which poor performance was seen to be tolerated. This was evidenced by the unauthorised expenditure and irregular expenditure that accumulated to a closing balance of over R4 billion each.

The effectiveness of the work performed by the assurance providers, such as internal audit units and audit committees, was hampered significantly by management's failure to implement their recommendations and resolutions. The role of councils also remained stagnant, as they did not insist on getting accurate financial and performance reports, which had a negative impact on the oversight responsibilities they needed to perform. In addition, MPAC resolutions were not tracked, monitored or implemented.

The implementation of the integrated municipal support plan developed by the provincial treasury, provincial Cogta, Salga and district municipalities was not monitored at the right level. The lack of coordination and concerted effort to implement the plan by these institutions made it difficult for the province to yield the desired outcomes of better financial management and service delivery.

The province's performance in 2015-16 can best be described as 'murky waters beginning to clear', as there was a net improvement in the audit outcomes. Steve Tshwete improved from unqualified with findings to unqualified with no findings, Bushbuckridge improved from qualified to unqualified with findings, Msukaligwa improved from disclaimed to qualified with findings, and Emakhazeni (which submitted financial statements late) was able to improve from disclaimed to qualified with findings. These improvements were negatively offset by the regression of Gert Sibande District and Chief Albert Luthuli from unqualified audit opinions with findings to qualified audit opinions.

The level of commitment, initiatives and investment poured by the province into the improvement of local government audit outcomes is not commensurate with the MFMA audit outcomes.

The continued weaknesses in the internal control environment of auditees resulted in the province struggling to improve its compliance with legislation for the past three years, most notably relating to the prevention of unauthorised, irregular as well as fruitless and wasteful expenditure and the poor quality of the financial statements submitted for auditing. This was further worsened by inadequate controls over the monitoring of compliance with legislation and a lack of timely and decisive action against transgressors.

Non-compliance with SCM legislation was the main cause of the escalating irregular expenditure, representing R2,263 billion (99%) of the total irregular expenditure of R2,279 billion in 2015-16. This was a significant increase from the R704 million reported in 2013-14. Mbombela and Bushbuckridge were the highest contributors in the province with irregular expenditure of R755 million and R570 million, respectively. The increase in irregular expenditure was mainly due to deviations from the normal procurement processes on the basis of emergencies and the multiple extension of contracts. In addition, there was an increasing trend in the number of contracts awarded through participating in contracts awarded by other municipalities (by using SCM regulation 32).

This was also now used for construction contracts that had not been the case in the past. As the principles in the regulation were incorrectly applied, it often led to irregular expenditure. The province's centralisation of the provision of water services to an implementing agent further contributed to the increased irregular expenditure in 2015-16, as the implementing agent did not follow a competitive bidding process in awarding the contracts on behalf of the municipalities concerned. These high levels of irregular expenditure indicated that disciplines to ensure that awards were made in a fair, equitable and transparent manner had not been institutionalised, which made the auditees susceptible to the risk of fraud.

The results on the reported performance information showed an improvement of 14% over the past three years, as 13 auditees (62%) reported findings in 2015-16 compared to 16 auditees (76%) in 2013-14. However, six auditees (29%) managed to avoid findings on their reported performance in 2015-16 because they corrected misstatements identified during the audit process. Auditees' inability to set quality indicators and to accurately report on their performance may have a negative impact on citizens' ability to accurately measure the performance of their municipalities and to hold their elected representatives accountable. Daily and monthly checks and balances, regular and accurate reporting as well as effective oversight and risk management are essential for improved performance reporting.

Despite this increase in transparency in reporting on performance information, the management of infrastructure projects such as water and road infrastructure remained a challenge in the province. A total of 18 municipalities are responsible for the delivery of water services in the province. At 12 auditees (67%), water infrastructure projects were not finalised on time, which resulted in the provision of water services being interrupted and the delivery of much-needed infrastructure to communities being delayed.

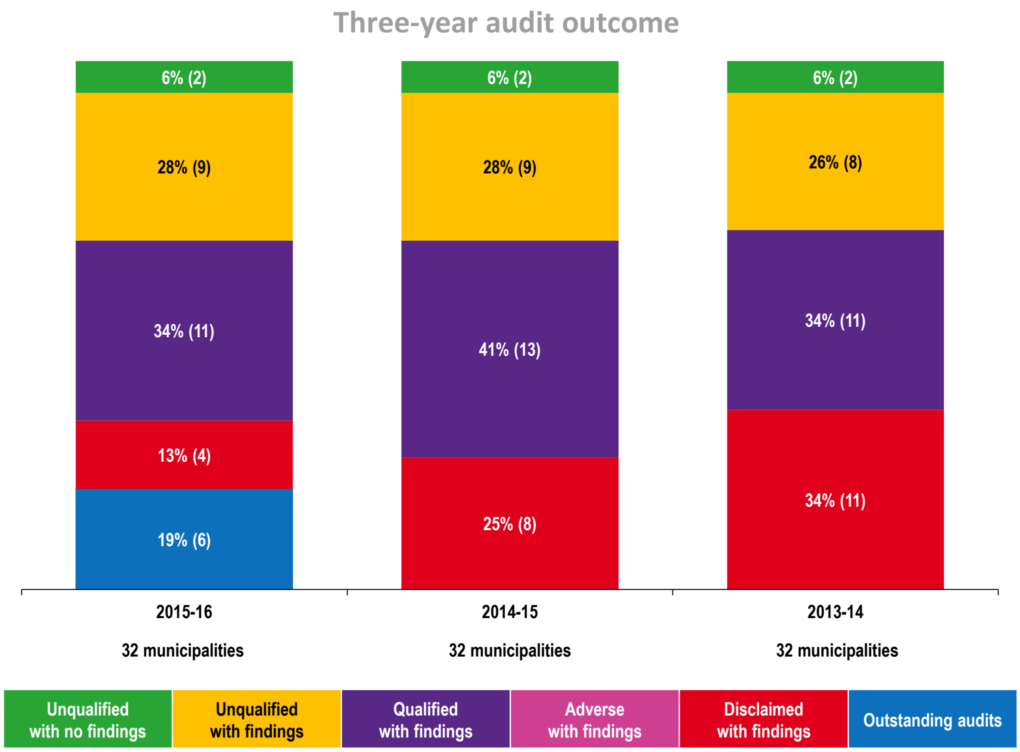
Furthermore, municipalities did not have proper plans to maintain the existing water infrastructure. Nine auditees (50%) did not perform conditional assessments, while eight (44%) did not have plans for the maintenance of infrastructure. This led to continuous pipe bursts and the interruption of basic services, which resulted in substantial water losses of R470 million (2014-15: R472 million). These losses added to the financial strain on municipalities.

It has been shown that those municipalities that progressed to, or maintained their previous, clean audits had adopted or gone back to the basics of clean governance. These include basic tasks such as the following:

- Political leadership and senior management that own the business of local government and are accountable for their actions and those of their subordinates.
- Leadership with clear responsibility and strategic direction for managing human resources, such as employing and retaining staff with the required level of technical competence and experience. Performance management is also cascaded to all employees of the institution.
- Leadership that institutes consequence management to address issues of non-compliance with key legislation and modifies compliance checklists based on past deficiencies.

By implementing these simple practical steps, substantially improved financial management and performance reporting in local government can be brought about. This is a goal within reach and a key ingredient in building trust in the credibility and accountability of local government and its capacity to deliver services to citizens.

12.7 Northern Cape



The overall audit outcomes of the Northern Cape stagnated over the past three years, with 11 municipalities achieving unmodified audit outcomes (unqualified with no findings and unqualified with findings) in 2015-16 compared to 10 in 2013-14. During the current year, two municipalities (Joe Morolong and Ubuntu) regressed from qualified audit opinions to disclaimed audit opinions. One municipality (Kgatelopele) managed to improve its audit outcome in the current year by moving from a disclaimed to a qualified audit opinion.

The areas in which municipalities struggled most over the past three years were to correctly measure and disclose property, infrastructure and equipment, receivables and revenue in the financial statements. The most common qualification area remained property, infrastructure and equipment, with 54% of municipalities being qualified in this regard (2014-15: 46%).

Most municipalities were still heavily reliant on the external auditors to identify misstatements in their financial statements, as only 23% (2014-15: 23%) were able to submit quality financial statements that did not require material adjustments. Most municipalities also remained heavily reliant on consultants although officials were available at these municipalities to perform the functions for which consultants were hired. The recurring appointment of consultants indicates that skills were not being transferred to the officials due to inadequate monitoring and/or the unwillingness of officials to acquire these skills.

The cost of using consultants for financial reporting (excluding consultants paid by other institutions) amounted to R38 million, compared to R42 million in 2014-15. Of concern is that we identified material misstatements at 75% of the 24 municipalities where consultants assisted with financial reporting (2014-15: 75%).

The timely submission of financial statements for auditing remained a concern, with 84% of municipalities submitting their financial statements on time compared to 88% in 2014-15. Oversight structures should intensify their efforts to monitor the municipalities that struggle every year to submit their financial statements on time.

The status of compliance with legislation remained of concern, with only 8% of municipalities avoiding findings on compliance (2014-15: 8%). This reconfirms that the area of compliance with legislation is not receiving the necessary attention from the municipal leadership. The most common compliance findings related to preventing unauthorised, irregular and fruitless and wasteful expenditure (88% of municipalities), managing procurement and contracts (85% of municipalities), and the quality of financial statements submitted for auditing (77% of municipalities).

The level of irregular expenditure, which had decreased since the previous year, amounted to R287 million (2014-15: R491 million). Of the R287 million, 97% resulted from instances of non-compliance with SCM legislation. The most common SCM findings related to uncompetitive or unfair procurement processes (88% of municipalities) and inadequate contract management (38% of municipalities).

The number of municipalities that incurred irregular expenditure remained high at 85% (2014-15: 85%). Eleven municipalities were still investigating the full extent of their irregular expenditure, confirming that the R287 million disclosed as irregular expenditure incurred in 2015-16 was understated. It is probable that a large portion of irregular expenditure may be disclosed in future years.

SCM findings, allegations of financial misconduct and unauthorised, irregular and fruitless and wasteful expenditure should all be investigated by the council and only written off after a proper investigation. During the current year, municipalities had to write off and condone irregular expenditure amounting to R609 million, but in no instance was any amount recovered from a liable person. The council should ensure that rigorous investigations are conducted and, where possible, steps are taken to recover losses.

The financial health of the province remained a concern, with a material uncertainty regarding the financial health of 50% of municipalities (2014-15: 54%). We favourably assessed only three municipalities (Frances Baard, Kareeberg and Sol Plaatje) on their financial health. We are concerned that 73% of municipalities were in a net current liability position at year-end, which meant that their total current liabilities exceeded their total current assets. Three municipalities were unable to meet their third-party obligations (such as to the South African Revenue Service, pension funds and medical aids) as they became due.

The year-end debtor balances of 92% of the municipalities included more than 10% of debt that should be considered irrecoverable. This is concerning considering that significant debtor balances had already been written off during the year. Poor debt collection from consumers places strain on municipalities' ability to pay creditors, as confirmed by the fact that 69% of municipalities had a creditor-payment period of more than 120 days. Consequently, municipalities run the risk of key suppliers discontinuing their services, which is likely to have a significant impact on service delivery going forward.

Predetermined objectives remained an area where progress was lacking, and 81% of municipalities (2014-15: 88%) were unable to produce performance reports that were useful and reliable – clearly indicating that this area was still not receiving the necessary attention.

It is concerning that 23% of municipalities (2014-15: 35%) did not submit performance reports in 2015-16. The main reason for the non-submission of performance reports was that at some municipalities there were no performance management systems in place or senior management lacked the skills and competencies to implement systems and to produce credible performance reports. At some municipalities, the focus was more on financial statements than on performance information, while officials were also not held accountable. The premier's office, provincial treasury, provincial Cogta and provincial legislature, as part of provincial oversight, need to consider rolling out training to reiterate the importance of performance information and to ensure that all municipalities understand the process to be followed when reporting on performance information. The internal auditors need to verify the accuracy of quarterly reports, while the state of record-keeping systems should be assessed.

We assessed the status of internal controls by considering the areas of leadership, financial and performance management, and governance. All three areas stagnated compared to the previous year and although new internal audit units and audit committees were established, only 31% of municipalities (2014-15: 27%) were assessed as having good governance controls.

Outcomes stagnated as the underlying internal control weaknesses had still not been addressed; the provincial leadership must pay attention to this.

The audit outcomes reflect the poor state of internal controls, with only 8% of municipalities (2014-15: 8%) being assessed as having good leadership controls, while only 12% (2014-15: 8%) were assessed as having good financial and performance management controls. The province will struggle to create stable and strong municipalities until senior management ensures that officials attain relevant skills and competencies to perform and produce work of the required quality. Senior managers must also ensure that the recommendations from audit committees, internal auditors and external auditors are taken seriously and given the necessary attention.

The assessment of vacancies in key positions (municipal manager, CFO and head of the SCM unit) showed regression over the past three years. The remoteness of most municipalities in the province remained a challenge and made it very difficult to attract skilled individuals to these municipalities in most instances. This meant that positions often remained vacant for a long period or were filled by a candidate with insufficient experience.

The majority of municipalities experienced challenges with the design of IT controls. These municipalities failed to design adequate controls to address the risks associated with IT security management, user access management and IT service continuity management. The regression can be attributed to a lack of accountability at various levels to ensure that the previous year's IT findings were resolved. Some municipalities had action plans in place to address the findings; however, due to inadequate oversight by CFOs and municipal managers, a lack of commitment from the IT unit as well as a shortage of skills and competence, also in the IT unit, no progress was made and no steps were taken to resolve these issues.

Sol Plaatje, being the only mSCOA pilot site in the province, made good progress in ensuring that the municipality would be in a better position to implement mSCOA by the due date of 1 July 2017. Although the municipality had implemented the new standard chart of accounts, we are concerned over the level of integration between asset management and financial systems. In addition to Sol Plaatje, 28% of the non-pilot municipalities were also assessed as making good progress, while 32% were assessed as making little progress.

A total of 40% of the non-pilot municipalities had made no progress towards mSCOA implementation. A lack of funds significantly contributed to these municipalities' inability to make progress, while mSCOA project governance policies, change communication plans, risk registers, data migration plans and data cleansing plans were not developed. The leadership at these municipalities, as well as the oversight structures, should become involved in this process to ensure that a plan is developed and implemented to enable municipalities to be ready to implement mSCOA on 1 July 2017.

As part of our audits, we performed procedures to evaluate the state of water management at municipalities. The number of findings that were raised is concerning. The following were the most common findings:

- No approved policy was in place to address routine maintenance of water infrastructure (71%).
- Backlogs in the provision of water services were not reported to the National Treasury in the section 71 reports (71%).
- No plan, with specific targets and time frames, was in place for the maintenance of water infrastructure (62%).

The key root causes that hindered progress were inadequate consequences for poor performance and transgressions (92%) (2014-15: 83%), a slow response by the political leadership (83%) (2014-15: 83%), and a slow response by management (79%) (2014-15: 71%).

The high occurrence of the root cause of inadequate consequences indicates that neither management nor staff are held accountable for non-performance. This brings into question the council's capacity to exercise oversight at the municipality. The slow response and inadequate attention (as a result of the upcoming election) by all relevant stakeholders highlighted above directly translated into inadequate assurance being provided at the expected levels.

These lower-than-expected levels of assurance, as well as management's slow response, are clearly evident where:

- municipal managers and senior managers are not holding their subordinates accountable for the quality of their work
- the recommendations of internal audit units and audit committees are not implemented, resulting in the external auditors raising the same findings highlighted by these governance structures
- due to a lack of capacity, the municipal councils and MPACs are not holding senior municipal officials accountable, resulting in a lack of consequences at most municipalities.

As recommended in previous years, district municipalities need to play a leading role in sharing their internal audit units and audit committees with local municipalities that do not have the means to establish their own.

During our meetings with oversight structures after the conclusion of the 2014-15 audit cycle, they committed to the following:

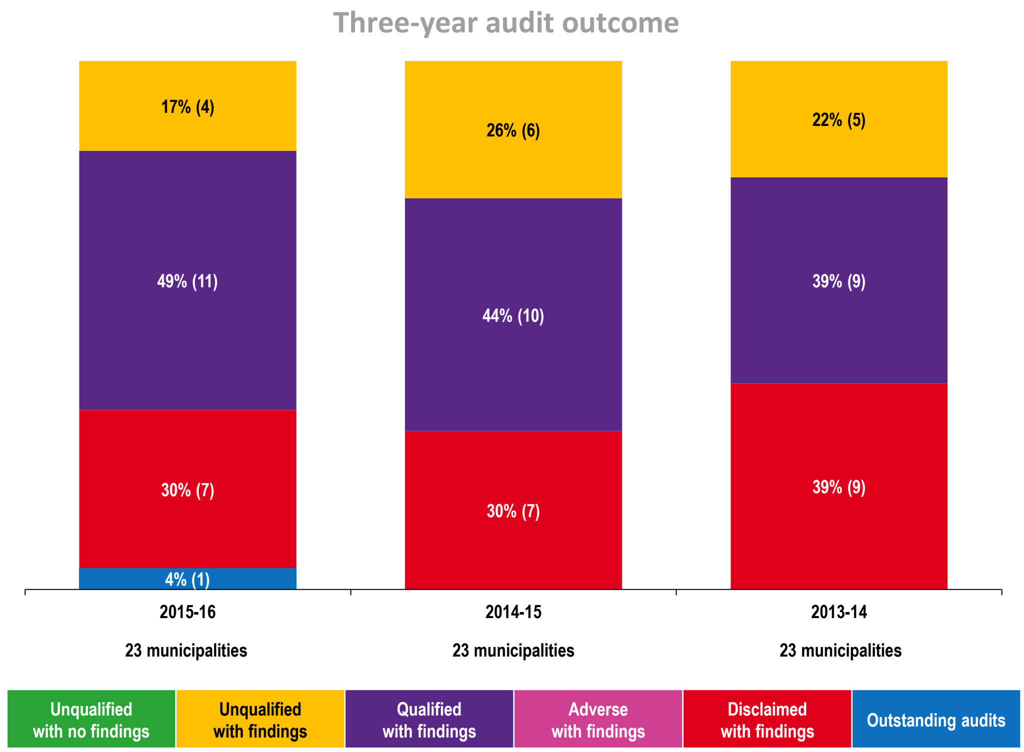
- Create capacity and an understanding of issues that the new councillors should be driving.
- Ensure that an action plan is in place to clear prior year findings.
- Promote a culture of accountability at municipalities.
- Increase the level of oversight at municipalities, focusing on SCM issues.

Limited progress was made with the implementation of the above commitments. If oversight structures want to have a meaningful impact on local government, they need to start tracking their commitments.

After the municipal elections in August 2016, new councils were formed and new mayors were elected. The challenge for the new political leadership would be to learn from their predecessors and lead the municipalities they are serving and the community they are representing to an improved state.

Mayors need to accept responsibility and be prepared to hold officials accountable for failing to improve audit outcomes and bettering the lives of citizens. This can only be achieved if mayors remain focused on achieving the goals they set for their municipalities, ensuring that accountability is clear to all levels of staff, and consequences follow if staff members do not perform as required.

12.8 North West



After the local government elections in August 2016, there was significant movement in the political leadership at the municipalities in the province, with new speakers at all municipalities except one, new mayors at 14 municipalities, and 61% newly elected councillors overall. During our interactions with the new leadership at councillor induction sessions and introductory meetings, the new councillors were eager to accept responsibility and to hold officials accountable. Increased accountability, specifically by those that manage resources intended for service delivery, will lead to improved controls and proper implementation and monitoring of municipal programmes intended to improve the lives of citizens.

The audit outcomes of municipalities regressed in 2015-16, with only four municipalities receiving unqualified audit opinions with findings. This was underpinned by the volatility in audit outcomes with five improvements offset by six regressions. The audit of Rustenburg had not been finalised by 15 January 2017, which was the cut-off date for inclusion in this report. The audit outcomes of the municipal entities in the province reflect a similar trend, with two remaining on unqualified with findings and one regressing to qualified with findings. The one outstanding audit and the three municipal entities are excluded from the further analysis in this section.

The fact that not a single municipality was able to achieve a clean audit outcome again highlights the lack of accountability by municipal management and other key role players in the province responsible for monitoring and assisting local government. The slow response by the political leadership to address the underlying root causes of continued poor audit outcomes will have to be countered with decisive action to hold officials accountable and implement consequence management for poor performance.

One of our key concerns is the poor quality of submitted financial statements. All municipalities continued to rely on consultants for financial reporting, including preparing financial statements at a cost of R126,9 million (2014-15: R130,9 million), yet all the financial statements submitted for auditing had material misstatements. Had the four unqualified municipalities not been given the opportunity to correct the misstatements identified by auditors during the audit process, none of the municipalities in the province would have obtained an unqualified opinion. Key controls that enable reliable and timeous financial reporting, such as proper record keeping, daily and monthly reconciliations and regular reporting, need to be institutionalised during the year without relying on the auditors to identify misstatements after year-end.

All municipalities again had material findings on compliance with key legislation. These include material misstatements in submitted financial statements, procurement and contract management findings, not preventing unauthorised, irregular and fruitless and wasteful expenditure, a lack of consequence management, and strategic and performance management findings. This is indicative of a leadership that lacks the political will to intervene and take decisive action against repeat offenders and transgressors.

A further R2,5 billion of irregular expenditure was incurred during 2015-16, which mostly related to SCM transgressions. This brings the total balance (excluding Rustenburg) of unresolved irregular expenditure as disclosed in the financial statements at 30 June 2016 to R7,4 billion. In addition, 15 of the 22 municipalities were qualified due to the irregular expenditure disclosed being either misstated or incomplete, while there was a further limitation of R283,8 million as contracts could not be provided for auditing. In terms of legislation, all irregular expenditure needs to be quantified and each transaction needs to be investigated. This did not happen, however, which reinforced a culture of non-compliance, transgression and no consequences, which in turn created an environment conducive to fraud and corruption.

Unauthorised expenditure of R2 billion was incurred in 2015-16, mainly as a result of overspending the approved budgets because of a general lack of understanding of the budget process and inadequate monitoring of spending. Furthermore, expenditure being incurred when it was known that the cash flow to fund this expenditure would not be collected from consumers, contributed to our assessment of 13 of 22 municipalities (59%) being in financial distress. At the end of June 2016, approximately R6,2 billion (84%) of the consumer debt of R7,4 billion due to municipalities in the province was expected to be irrecoverable. This could then result in municipalities not being able to pay their suppliers, including R874,9 million to Eskom and R923,5 million to bulk water providers.

Of the MIG allocation of R1,4 billion to municipalities, R146,4 million (11%) was not spent. Cash-flow constraints contributed to underspending, as in some cases the grant allocations were used to fund operational expenditure. Of the 60 key projects selected for auditing, most of the ones related to water, sanitation and road projects were behind schedule or completed late and therefore did not achieve the planned targets. We also raised SCM findings in the awarding of the contracts for the majority of these projects. Furthermore, most municipalities did not have approved policies for the maintenance of water, sanitation and road infrastructure and also did not perform conditional assessments of these infrastructure assets to inform the repair and maintenance budgets. As a result, dilapidated infrastructure due to a lack of maintenance was the main cause of pollution to the environment and resulted in water and electricity distribution losses in excess of R295,3 million and R542,3 million, respectively.

Only one municipality (5%) reliably reported on its performance against predetermined objectives. Another four municipalities were allowed to make material adjustments to their performance reports to achieve this. Most municipalities were unable to provide support for their reported results, due to poor record management and a lack of institutionalised controls to timeously and reliably report on their performance. Management should ensure that internal control weaknesses in financial and performance reporting are properly addressed in action plans, which should in turn be timeously monitored for compliance.

There was little improvement in the IT control environment of municipalities; and they need to attend to the IT control weaknesses as a matter of urgency. These weaknesses not only increase the risk of fraud, but also increase the risk of consumer accounts and IT systems being manipulated through unauthorised access as well as undermine the business continuity of municipalities. Concerns were raised at most municipalities regarding the readiness to implement mSCOA and SCM reforms of the National Treasury, including the use of the centralised supplier database and the eTender portal.

Municipal managers, CFOs and senior management were not always able to focus on their core responsibilities, as the environment in which they work made it easy for these individuals to be discouraged. Leadership attention was also focused on the upcoming election instead of driving improvements in the control environment. The culture of low performance and non-compliance together with the lack of effective political leadership and oversight should be turned around so that officials feel motivated to do their jobs well and take accountability for their performance. This will only happen if consequence management is implemented against non-performing officials at all levels and when the tone at the top encourages accountability. Where vacant positions were filled, some of the incumbents did not meet the required minimum competency levels or were not adequately supported by appropriately resourced and skilled units. This means that the province needs to invest in building and retaining capacity over the long term.

The high levels of instability and vacancies at the key levels of municipal manager and senior management resulted in inadequate assurance being provided by this first level of assurance providers to enable credible and reliable financial and performance reporting. This then directly contributed to the insufficient assurance provided by internal audit units and audit committees, whose recommendations were in most cases not implemented by management. The provincial coordinating departments also did not have the desired impact in assisting municipalities to address the root causes of poor audit outcomes, ensure that vacancies in key positions were addressed, make sure that consequence management was implemented, or otherwise intervene when it was necessary to do so.

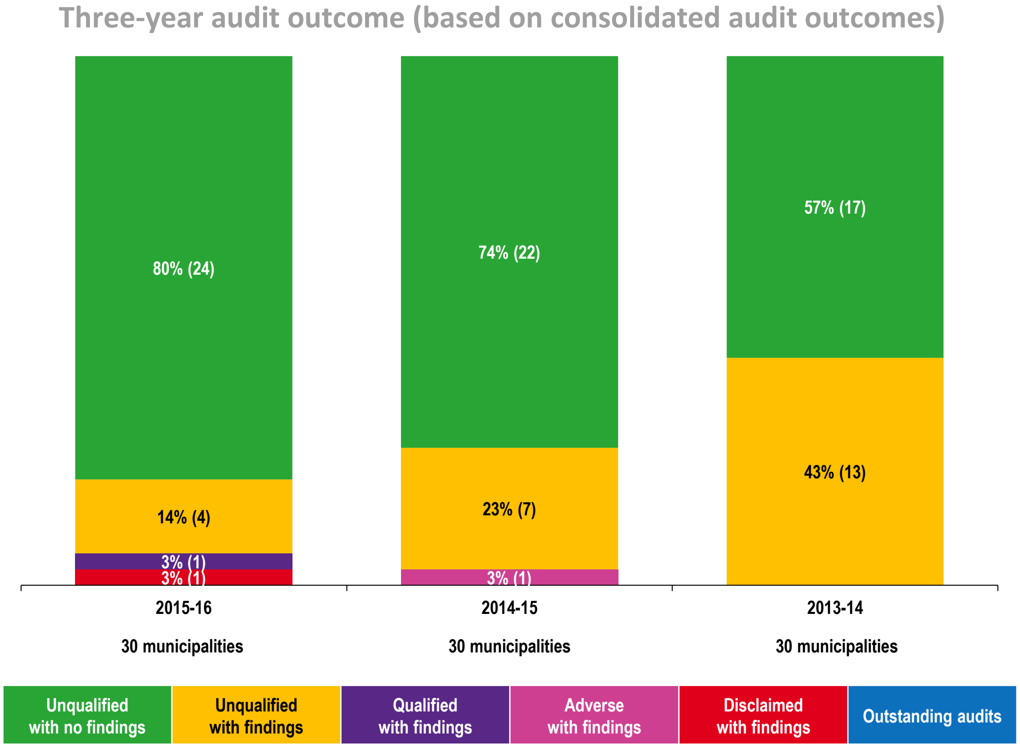
A few individuals with personal commitment to perform well in their jobs were able to exercise good practices, such as investigating and clearing irregular expenditure as well as improving the audit outcomes. However, if these good practices are not institutionalised, it is easy for audit outcomes to regress when these individuals leave.

Consequence management, accountability and action by the leadership in addressing root causes are the key cornerstones to improve audit outcomes.

The newly elected mayors and councillors, together with the provincial executive leadership, can step up and take accountability by understanding the root causes of poor audit outcomes and implementing the key controls required to improve these outcomes. To achieve this, we recommended that a provincial turnaround strategy be developed. The premier committed during our roadshow in March 2017 to develop a 10-point plan to address the identified root causes and key control weaknesses. This plan will also include mechanisms on consequence management, a fraud hotline, and policies on investigations and disciplinary procedures.

We will continue to engage with management and the political leadership to make recommendations for improvement and track the progress of commitments made.

12.9 Western Cape



After the local government elections in August 2016, there was significant movement in the political leadership at the municipalities in the province, with new speakers at 25 municipalities, new mayors at 22 municipalities, and 55% newly elected councillors overall. Our interactions with the new leadership at councillor induction sessions and introductory meetings indicated that they were eager to accept responsibility and drive accountability.

The progress towards clean audits had slowed down when compared to the previous year and had improved when compared to 2013-14. This was due to leadership focus being on the upcoming election and not driving the improvement plans as strongly as before. Of significant concern is the regression of Kannaland, which received a disclaimer in the current year compared to a financially unqualified opinion with findings in 2014-15. On a positive note, those municipalities that achieved a clean audit outcome in the previous year maintained the same outcome for 2015-16. Bergrivier improved from financially unqualified with findings to a clean audit outcome, while Oudtshoorn improved from an adverse opinion to a financially qualified opinion with findings. Central Karoo District's consolidated outcome improved to clean, but the individual municipality's audit outcome remained unchanged on financially unqualified with findings.

The quality of submitted financial statements improved considerably, with only five sets (17%) of financial statements requiring material adjustments compared to seven (23%) in 2014-15, as a result of continuous effort to improve the control environment.

Non-compliance with the MFMA and in particular SCM regulations continued to be one of the main obstacles to increasing the number of clean audits in the province. Six auditees (20%) had material findings on compliance with procurement processes, compared to five (17%) in 2014-15. It is concerning that the Central Karoo district continued to be plagued by material findings on compliance with SCM regulations, with three of the five municipalities in the district attracting such findings. The district municipality itself regressed, with seven material findings relating to procurement compared to none in 2014-15. Notable, however, was that Prince Albert improved significantly by reducing the eight material compliance findings they received in 2014-15 to only one, namely in the area of the prevention of irregular expenditure. This was as a result of the diligent implementation and monitoring of their action plan to address prior year matters.

A lack of understanding of SCM prescripts, vacancies, instability and a lack of SCM processes and procedures contributed to non-compliance with procurement processes. The incorrect application of SCM regulation 36 relating to deviations was one of the most common findings. SCM officials require further training, while consequence management must be implemented in instances of non-compliance with legislation.

Irregular expenditure decreased from R344 million in 2014-15 to R210 million in 2015-16. A total of 55% of this expenditure was identified by auditors in 2015-16 compared to 54% in 2014-15. Overall, allegations of misconduct and unauthorised, irregular and fruitless and wasteful expenditure were investigated by the council and related expenditure or losses were recovered or written off as irrecoverable if no one was found to be liable. At four municipalities (13%), investigations were not performed to determine whether any person was liable for the expenditure. At one municipality, irregular expenditure was not properly investigated.

On the issue of financial health, we also draw attention to the importance of casting an eye on the issues that could cause financial pressure, especially when it comes to the management of working capital at municipalities.

The status of financial health at five municipalities (17%) remained a concern. This was due to difficulty in collecting debt from consumers as well as weak financial management, especially at municipalities within the Central Karoo district and the inland municipalities in the Eden district. These districts have a much poorer economic outlook when compared to the rest of the province. Plans that are currently in place at these municipalities include filling key vacancies within the finance unit, which will result in better financial management, as well as the implementation of financial management plans (also relating to debt collection), which are supported by the provincial treasury and local government, with the aim of improving cash-flow management.

The quality of submitted performance information remained a concern, as 19 (63%) of the municipalities relied on the audit process to identify adjustments needed to the performance report, compared to 14 (47%) in 2014-15. The usefulness of performance information is now at a mature level, as municipalities have in the main ensured that their planning documents meet the SMART criteria (in other words, indicators are specific, measurable, achievable, relevant and time bound) and processes are in place to report on actual achievements. Oudtshoorn did not submit performance information for auditing, while Kannaland was the only municipality that still had audit report findings on usefulness and reliability.

Of concern is that six municipalities (20%) did not have approved policies for the maintenance of water infrastructure. Seven municipalities (23%) did not have a plan with specific time frames and targets for the maintenance of water infrastructure. The lack of policies and plans for the maintenance of water infrastructure could have a negative impact on the reliability and sustainability of future water services. Water and sanitation projects at Kannaland did not address the cause of backlogs. Furthermore, the budget allocated to water and sanitation infrastructure projects was underspent by 45% and 76%, respectively. Three municipalities (10%) reported water losses above the acceptable norm of 30%.

Municipalities continued to rely on consultants for financial and performance reporting. The number of municipalities using consultants for performance information decreased from 15 in 2014-15 to 12 in 2015-16. There was no change in the number of municipalities using consultants for financial reporting, which can be attributed to the vacancies at municipalities and the extent to which municipalities continued to rely on the skills of consultants. We identified areas for improvement in the appointment and management of consultants at nine (35%) of the 26 municipalities that used consultants. Some of the more common issues included the absence of a strategy or policy for the use of consultants (27%), a lack of measures to monitor contract performance and failure to define and/or implement delivery (23%), and failure to implement measures to monitor the transfer of skills according to the contract (19%). The total amount spent on consultants decreased by R3,8 million to R42,2 million in 2015-16.

The status of key controls remained mostly unchanged, which is consistent with the audit outcomes. There was a slight deterioration in the assessment of controls in the areas of leadership and of financial and performance management, which was largely driven by the regression of Kannaland, as well as an increase in the number of municipalities that required material adjustments to their performance reports to prevent material findings relating to performance information.

Of concern is the regression in the assurance provided by municipal managers and senior management overall, while the audit outcomes remained largely unchanged. The senior management at various auditees with clean audits was rated as ‘provides some assurance’ due to the following:

- Material corrections to performance reports to avoid material findings on performance information in the audit report.
- Compliance findings reported in the management report. Although these findings were not material in 2015-16, it is possible that material findings on compliance may be raised in future years if the underlying issues are not appropriately addressed by senior management.

If appropriate actions are not taken by senior management to remedy the situation, those municipalities could regress in future years.

The overall assessment of the IT control environment improved, with certain municipalities maintaining their status of no IT audit findings in the general control environment of the prior year. A few municipalities still experienced challenges in implementing IT controls, with significant IT risks identified in the areas of user access management, security management and IT service continuity management. This was as a result of the lack of skilled IT resources at these municipalities and limited financial resources available for strategic IT initiatives. We performed a high-level checklist exercise on the mSCOA readiness of municipalities in the province, looking at aspects such as governance structures, project planning, change management, data migration plans and risk management. Overall, 23 municipalities (77%) made good progress in getting ready for mSCOA implementation, four municipalities (13%) had some gaps which caused concern, while three municipalities (10%) had made little progress.

In line with the prior year commitments, the premier continued to use the premier’s coordinating forum to coordinate and monitor provincial oversight as well as her interactions with MECs on a monthly basis to determine what progress had been made towards clean administration.

The provincial executive renewed its commitment to ensure that operation clean audit, coordinated by the ministries of provincial treasury and local government (Troika), remained a standing agenda item of the premier’s coordinating forum for monitoring and evaluating municipalities’ key controls and commitments, and sharing best practices to achieve sustainable clean audit outcomes.

In addition to the above commitments, the premier and all role players again pledged their support for the municipal governance review and outlook process, which will address the remaining shortcomings in the province. These processes will be followed through at the premier’s coordinating forum. The premier and the provincial executive, together with the coordinating ministries of provincial treasury and local government, also undertook to focus intensively on Central Karoo District, which continued to display significant weaknesses in basic financial and performance management controls and disciplines, including a lack of proper record keeping, daily processing of transactions, reconciliations as well as effective review and monitoring of compliance.

While we are satisfied with the improvement in the oversight demonstrated by councils at an overall level, we remain concerned about the need for continued improvement and the sustainability of oversight. Of particular concern is our assessment at four municipalities (13%) where the municipal councils provided limited/no assurance. In all instances we encourage councils to periodically review progress made by municipal management in addressing external audit findings and to take timeous action in instances of identified weaknesses or failure by management and staff to perform their statutory duties.

The audit outcomes that had not progressed to clean are a reflection of the root causes below that were common at these auditees. These require attention from all role players to improve the audit outcomes:

- A slower-than-expected response by management (weak operational plans) to implement commitments and action plans relating to the quality of financial statements, performance information and compliance at four auditees (13%).
- Key officials lacking competencies and/or instability at four municipalities (13%).
- Lack of consequences at two municipalities (7%), which remained unchanged from 2014-15.

Going forward, the following are recommended:

- Develop detailed action plans to address the recurring findings relating to the financial statements, performance reports and compliance with key legislation (including SCM).
- Establish or enhance the function to monitor and review action plans, with appropriate consequence management for non-adherence.
- Focus on upskilling staff to ensure that basic daily and monthly financial, performance and compliance disciplines are implemented to ensure proper record keeping, timely processing of transactions, reconciling of transactions, and regular monitoring of compliance.

Accountability can be seen as the core principle where municipalities are answerable to the public and accept responsibility for their actions, decisions and policies, which can be closely linked to good governance. Governance is the establishment of policies and the continuous monitoring of their proper implementation. It includes the mechanisms required to balance powers and a primary duty of enhancing the prosperity and viability of the organisation.

In the Western Cape, many municipalities have demonstrated accountability and good governance, which has led to an overall outcome of clean audits for the majority of municipalities. A further indication of accountability is the implementation of consequences for transgressions. Many municipalities have instituted disciplinary action, resulting in the dismissal of employees and recovery of losses, thereby setting the tone from the top that action will be taken where transgressions occur.

All municipalities should keep striving to improve accountability, good governance and consequence management to attain or maintain clean administration.

NOTES

13 Need to know

13.1 Our audit processes and focus

What is our audit and reporting process?

We audit every municipality and municipal entity in the country to report on the quality of their financial statements and performance reports and on their compliance with key legislation.

We also assess the root cause of any error or non-compliance, based on the internal control that had failed to prevent or detect it. We report in the following three types of reports:

- We report our findings, the root causes of such findings and our recommendations in **management reports** to the senior management and municipal managers, or chief executive officers (CEOs) in the case of municipal entities, which are also shared with the mayors and audit committees.
- Our opinion on the financial statements, material findings on the performance report and compliance with key legislation, as well as significant deficiencies in internal control, are included in an **audit report**, which is published with the auditee's annual report and dealt with by the municipal council.
- Annually, we report on the audit outcomes of all auditees in a **consolidated report** (such as this one), in which we also analyse the root causes that need to be addressed to improve audit outcomes. Before the general reports are published, we share the outcomes and root causes with the national and provincial leadership, Parliament and the legislatures, as well as key role players in national and provincial government.

Over the past few years, we have intensified our efforts to assist in improving audit outcomes by identifying the **key controls** that should be in place at auditees, assessing these on a regular basis, and sharing the results of the assessment with mayors, municipal managers, CEOs and audit committees.

During the audit process, we work closely with the municipal managers, CEOs, senior management, audit committees and internal audit units, as they are **key role players** in providing assurance on the credibility of the auditee's financial statements, performance report as well as compliance with legislation.

We also continue to strengthen our relationship with the mayors, ministers and MECs responsible for cooperative governance, premiers, treasuries, departments of cooperative governance as well as Parliament and provincial legislatures, as we are convinced that their involvement and oversight have played – and will continue to play – a crucial role in the performance of local government. We share our messages on key controls, risk areas and root causes with them, and obtain and monitor their commitments to implementing initiatives that can improve audit outcomes.

The overall audit outcomes fall into five categories:

1. Auditees that received a **financially unqualified opinion with no findings** are those that were able to:

   - produce financial statements free of material misstatements (material misstatements mean errors or omissions that are so significant that they affect the credibility and reliability of the financial statements)
   - measure and report on their performance in line with the predetermined objectives in their integrated development plans and/or service delivery and budget implementation plans in a manner that is useful and reliable
   - comply with key legislation.

   This audit outcome is also commonly referred to as a clean audit.

2. Auditees that received a **financially unqualified opinion with findings** are those that were able to produce financial statements without material misstatements, but are struggling to:

   - align their performance reports to the predetermined objectives to which they had committed in their integrated development plans and/or service delivery and budget implementation plans
   - set clear performance indicators and targets to measure their performance against their predetermined objectives

- report reliably on whether they had achieved their performance targets
- determine which legislation they should comply with, and implement the required policies, procedures and controls to ensure that they comply.

3. Auditees that received a **financially qualified opinion with findings** face the same challenges as those that were financially unqualified with findings in the areas of reporting on performance and compliance with key legislation. In addition, they were unable to produce credible and reliable financial statements. Their financial statements contained misstatements which they could not correct before the financial statements were published.

4. The financial statements of auditees that received an **adverse opinion with findings** included so many material misstatements that we disagreed with virtually all the amounts and disclosures in the financial statements.

5. Those auditees with a **disclaimed opinion with findings** could not provide us with evidence for most of the amounts and disclosures in the financial statements. We were unable to conclude or express an opinion on the credibility of their financial statements.

   Auditees with adverse and disclaimed opinions are typically also:

   - unable to provide sufficient supporting documentation for the achievements they report in their performance reports
   - not complying with key legislation.

What is the purpose of the annual audit of the financial statements?

The purpose of the annual audit of the financial statements is to provide the users thereof with an opinion on whether the financial statements fairly present, in all material respects, the key financial information for the reporting period in accordance with the financial framework and applicable legislation. The audit provides the users with reasonable assurance regarding the degree to which the financial statements are reliable and credible on the basis that the audit procedures performed did not reveal any material errors or omissions in the financial statements. We use the term 'material misstatement' to refer to such material errors or omissions.

We report the poor quality of the financial statements we receive in the audit reports of some auditees as a material finding on compliance, as it also constitutes non-compliance with the MFMA. The finding is only reported for auditees that are subject to the MFMA and if the financial statements we received for auditing included material misstatements that could have been prevented or detected if the auditee had an effective internal control system. We do not report a finding if the misstatement resulted from an isolated incident or if it relates to the disclosure of unauthorised, irregular or fruitless and wasteful expenditure identified after the financial statements had been submitted.

What does compliance with key legislation mean?

We annually audit and report on compliance by auditees with key legislation applicable to financial and performance management and reporting as well as related matters. We focused on the following areas in our compliance audits if they apply to the particular auditee: ■ the quality of the financial statements submitted for auditing ■ asset and liability management ■ audit committees and internal audit units ■ budget management ■ expenditure management ■ unauthorised, irregular as well as fruitless and wasteful expenditure ■ consequence management ■ revenue management ■ strategic planning and performance management ■ financial statements and annual report ■ transfer of funds and conditional grants ■ procurement and contract management (in other words, SCM) ■ HR management and compensation.

In our audit reports, we report findings that were material enough to be brought to the attention of auditee management, municipal councils, boards of municipal entities as well as oversight bodies and the public.

What is the scope of supply chain management audits?

We test whether the prescribed procurement processes had been followed to ensure that all suppliers were given equal opportunity to compete and that some suppliers were not favoured above others. The principles of a fair, equitable, transparent, competitive and cost-effective SCM process are fundamental to the procurement practices of the public sector and are enshrined in our country's constitution and prescribed in the MFMA and its SCM regulations. The MFMA and these regulations define what processes should be followed to adhere to the constitutional principles, the level of flexibility available, and the documentation requirements.

We also focus on contract management, as shortcomings in this area can result in delays, wastage as well as fruitless and wasteful expenditure, which in turn have a direct impact on service delivery.

We further assess the financial interests of employees and councillors of the auditee and their close family members in suppliers to the auditee. The requirements in this regard are as follows:

- SCM regulation 44 prohibits the awarding of contracts to, and acceptance of quotations from, employees, councillors or other state officials, or entities owned or managed by them, if they are in the service of the auditee or if they are in the service of any other state institution. Such expenditure is also considered irregular. During our audits, we identify such prohibited awards and also test whether the legislated requirements with regard to declarations of interest were adhered to.
- Awards to close family members of persons in the service of the state, whether at the auditee or another state institution, are not prohibited. However, such awards of more than R2 000 must be disclosed in the financial statements of the auditee for the sake of transparency and as required by SCM regulation 45. A close family member is a spouse, child or parent of a person in the service of the state.

What is irregular expenditure?

Irregular expenditure is expenditure that was **not incurred in the manner prescribed by legislation**; in other words, somewhere in the process that led to the expenditure, the auditee did not comply with the applicable legislation. Such expenditure does not **necessarily mean that money had been wasted or that fraud had been committed**. It is an indicator of irregularities in the processes followed in the procurement of goods and services and a measure of a municipality's ability to comply with legislation relating to expenditure and procurement management.

The MFMA requires municipal managers to take all reasonable steps to prevent irregular expenditure. If they persistently disregard the need for strengthening this control, opportunities may be inadvertently created for the commission of fraudulent transactions. Auditees should have processes in place to detect non-compliance with legislation that results in irregular expenditure and disclose the amounts in the financial statements. Irregular expenditure is reported when it is identified – even if the expenditure was incurred in a previous year.

The MFMA provides steps that municipal managers and councils should take to investigate irregular expenditure to determine whether any officials are liable for the expenditure and to recover the money if liability is proven. The investigation should also confirm whether fraud had been committed or money had been wasted.

What is fruitless and wasteful expenditure?

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

The MFMA requires municipal managers to take all reasonable steps to prevent fruitless and wasteful expenditure. Auditees should have processes in place to detect fruitless and wasteful expenditure and disclose the amounts in the financial statements. Fruitless and wasteful expenditure is reported when it is identified – even if the expenditure was incurred in a previous year.

The MFMA also sets out the steps that municipal managers and councils should take to investigate fruitless and wasteful expenditure to determine whether any officials are liable for the expenditure and to recover the money if liability is proven.

What is unauthorised expenditure?

Unauthorised expenditure refers to expenditure that auditees incurred without provision having been made for it in the budget approved by the council or which does not meet the conditions of a grant.

The MFMA requires municipal managers to take all reasonable steps to prevent unauthorised expenditure. Auditees should have processes in place to identify any unauthorised expenditure incurred and disclose the amounts in the financial statements. The MFMA also includes the steps that municipal managers and councils should take to investigate unauthorised expenditure to determine whether any officials are liable for the expenditure and to recover the money if liability is proven.

What are conditional grants?

Conditional grants are funds transferred from national government to auditees, subject to certain services being delivered or on compliance with specified requirements. Municipalities receive two types of allocations from the national revenue fund, namely equitable share and conditional allocations. Equitable share allocations are non-conditional, based on the municipality's share of revenue raised nationally. Conditional allocations are made for a specific purpose, and include:

- allocations to municipalities to supplement the funding of functions funded from municipal budgets
- specific-purpose allocations to municipalities
- allocations-in-kind to municipalities for designated special programmes
- funds not allocated to specific municipalities that may be released to municipalities to fund immediate disaster response.

Conditional allocations are approved each year through DoRA. DoRA will indicate the approved allocation per type of allocation per institution for that particular year, together with a forward estimate of allocations for the next two years.

With regard to forward estimates, the following take place before a set deadline for the final allocation to be approved through DoRA:

- Each municipality must agree on the provisional allocations and the projects to be funded from those allocations. This information is sent to the national transferring officer.
- After consolidating the information for each municipality, the transferring national officer submits the final allocation list and the draft grant framework for each allocation to the National Treasury for approval.

Municipalities may only use a conditional allocation for its intended purpose in accordance with the requirements of each grant framework and for projects or programmes included in their business plans.

What is the purpose of the grants that were audited?

The DCoG introduced the **MIG** in 2004-05 with the core outcome to improve access to basic service infrastructure for poor communities by providing specific capital finance for basic municipal infrastructure backlogs for poor households, micro-enterprises and social institutions servicing poor communities.

In achieving the core outcome, annual targets must be set in respect of the following expected outputs derived from the MIG framework:

- Number of additional poor households receiving basic water and sanitation services
- Number of additional poor households serviced by sport and recreation facilities

- Number of additional kilometres of municipal roads developed
- Number of additional poor households serviced by solid waste disposal sites and transfer stations
- Number of additional poor households serviced by street or community lighting
- Number of work opportunities created using the guidelines of the expanded public works programme for the above outputs

For this purpose, municipalities must annually submit business plans to the DCoG. The grant uses the registration requirements of the MIG management information system to register, track and monitor projects as per the business plans. Such plans should include timelines regarding project designs, initiation of procurement, environmental impact assessments, and relevant permit or licence approvals in the prescribed format.

The **USDG** was introduced to assist metropolitan municipalities in improving access to basic services by households through the provision of bulk and reticulation infrastructure as well as urban land production to support broader urban development and integration, while the **PTNG** aims to provide accelerated construction and improvement of non-motorised transport infrastructure.

What is the purpose and nature of the annual audit of the performance reports?

Auditees are required to measure their actual service delivery against the performance indicators and targets set for each of their predetermined performance objectives as defined in their integrated development plans and/or service delivery and budget implementation plans, and to report on this in their performance reports.

On an annual basis, we audit **selected objectives** to determine whether the information in the performance reports is useful and reliable enough to enable the council, the public and other users of the reports to assess the performance of the auditee. The objectives we select are those that are important for delivery by the auditee on its mandate. In the audit report, we report findings arising from the audits that were material enough to be brought to the attention of these users.

As part of the annual audits, we audited the **usefulness of the reported performance information** by determining whether it was presented in the annual report in the prescribed manner and was consistent with the auditees' planned objectives as defined in their integrated development plans and/or service delivery and budget implementation plans. We also assessed whether the performance indicators and targets that were set to measure the achievement of the objectives were well defined, verifiable, specific, time bound, measurable and relevant.

We further audited the **reliability of the reported information** by determining whether it could be traced back to the source data or documentation and whether it was accurate, complete and valid.

When is human resource management effective?

HR management refers to the management of an auditee's employees or human resources, which involves adequate and sufficiently skilled people as well as the adequate management of staff performance and their productivity. HR management is effective if adequate and sufficiently skilled staff members are in place and if their performance and productivity are properly managed.

Our audits included an assessment of HR management, focusing on the following areas: ■ HR planning and organisation ■ management of vacancies ■ appointment processes ■ performance management ■ acting positions ■ management of leave, overtime and suspensions.

Our audits further looked at the management of vacancies and stability in key positions, the competencies of key officials, performance management as well as consequences for transgressions, as these matters directly influence the quality of auditees' financial and performance reports and their compliance with legislation.

Based on the results of these audits, we assessed the status of auditees' HR management controls.

When are internal controls effective and efficient?

A key responsibility of municipal managers, CEOs, senior managers and municipal officials is to implement and maintain effective and efficient systems of **internal control**.

We assess the internal controls to determine the effectiveness of their design and implementation in ensuring reliable financial and performance reporting and compliance with legislation. This consists of all the policies and procedures implemented by auditee management to assist in achieving the orderly and efficient conduct of business, including adhering to policies, safeguarding assets, preventing and detecting fraud and error, ensuring the accuracy and completeness of accounting records, and timeously preparing reliable financial and service delivery information. To make it easier to implement corrective action, we categorise the principles of the different components of internal control under leadership, financial and performance management, or governance. We call these the drivers of internal control.

The key basic controls that should be focused on are as follows:

Providing effective leadership

To improve and sustain audit outcomes, auditees require **effective leadership** that is based on a culture of honesty, ethical business practices and good governance, protecting and enhancing the interests of the auditee.

Audit action plans to address internal control deficiencies

Developing and monitoring the implementation of action plans to address **identified internal control deficiencies** are a key element of internal control.

The MTSF defines the implementation of audit action plans and the quarterly monitoring thereof by a coordinating structure in the province as key measures to support financial management and governance at municipalities. It is also echoed in the DCoG's B2B strategy, which tasks local government with addressing post-audit action plans and the National Treasury, provincial treasuries and departments of cooperative governance with assessing the capacity of municipalities to develop and implement such plans.

Proper record keeping and document control

Proper and timely record keeping ensures that complete, relevant and accurate information is accessible and available to support financial and performance reporting. Sound record keeping will also enable senior management to hold staff accountable for their actions. A lack of documentation affects all areas of the audit outcomes.

Some of the matters requiring attention include the following:

- Establish proper record keeping so that records supporting financial and performance information as well as compliance with key legislation can be made available when required for audit purposes.
- Implement policies, procedures and monitoring mechanisms to manage records, and make staff members aware of their responsibilities in this regard.

Implement controls over daily and monthly processing and reconciling of transactions

Controls should be in place to ensure that **transactions** are processed in an accurate, complete and timely manner, which in turn will reduce errors and omissions in financial and performance reports.

Some of the matters requiring attention include the following:

- Daily capturing of financial transactions, supervisory reviews of captured information, and independent monthly reconciliations of key accounts.
- Collecting performance information at intervals appropriate for monitoring, setting service delivery targets and milestones, and validating recorded information.
- Confirming that legislative requirements and policies have been complied with before initiating transactions.

Review and monitor compliance with legislation

Auditees need to have mechanisms that can identify applicable legislation as well as changes to legislation, assess the requirements of legislation, and implement processes to ensure and **monitor compliance** with legislation.

What is information technology and what are information technology controls?

IT refers to the computer systems used for recording, processing and reporting financial and non-financial transactions. IT controls ensure the **confidentiality**, **integrity** and **availability** of **state information**, enable service delivery, and promote national security. Good IT governance, effective IT management and a secure IT infrastructure are therefore essential.

During our audits, we assessed the IT controls that focus on IT governance, security management, user access management and IT service continuity.

To evaluate the status of the IT controls in the areas we audited, we grouped them into the following three categories, with reference to the control measures that should be in place:

1. Where IT controls are being designed, management should ensure that the controls would reduce risks and threats to IT systems.
2. Where IT controls are being implemented, management should ensure that the designed controls are implemented and embedded in IT processes and systems. Particular attention should be paid to ensuring that staff members are aware of, and understand, the IT controls being implemented, as well as their roles and responsibilities in this regard.
3. Where IT controls have been embedded and are functioning effectively, management should ensure that the IT controls that have been designed and implemented are functioning effectively at all times. Management should sustain these IT controls through disciplined and consistent daily, monthly and quarterly IT operational practices.

Information technology governance

IT governance refers to the **leadership**, **organisational structures** and **processes** which ensure that the auditee's IT resources will sustain its business strategies and objectives. Effective IT governance is essential for the overall well-being of an auditee's IT function and ensures that the auditee's IT control environment functions well and enables service delivery.

Security management

Security management refers to the **controls preventing unauthorised access** to the computer networks, computer operating systems and application systems that generate and prepare financial information.

User access management

User access controls are measures designed by business management to **prevent and detect the risk** of unauthorised access to, and the creation or amendment of, financial and performance information stored in the application systems.

Information technology service continuity

IT service continuity controls enable auditees to **recover**, within a reasonable time, the **critical business operations** and **application systems** that would be affected by disasters or major system disruptions.

What are root causes?

Root causes are the underlying **causes or drivers** of audit findings; in other words, the reason why the problem occurred. Addressing the root cause helps ensure that the actions address the real issue, thus preventing or reducing incidents of recurrence, rather than simply providing a one-time or short-term solution.

Our audits included an assessment of the root causes of audit findings, based on the identification of internal controls that had failed to prevent or detect the error or non-compliance. These root causes were confirmed with management and shared in the management report with the municipal managers or CEOs and the mayors. We also included the root causes of material findings reported as internal control deficiencies in the audit report, classified under the key drivers of leadership, financial and performance management, or governance.

Who provides assurance?

Mayors and their municipal managers use the annual report to report on the financial position of auditees, their performance against predetermined objectives and overall governance, while one of the important oversight functions of councils is to consider auditees' annual reports. To perform their oversight function, they need **assurance that the information in the annual report is credible**. To this end, the annual report also includes our audit report, which provides assurance on the credibility of the financial statements, the performance report and the auditee's compliance with legislation.

Our reporting and the oversight processes reflect on history, as they take place after the financial year. Many other role players in local government contribute throughout the year to the credibility of financial and performance information and compliance with legislation by ensuring that adequate internal controls are implemented.

The mandates of these role players differ from ours, and we have categorised them as follows:

1. Those directly involved in the management of the auditee (management/leadership assurance)
2. Those that perform an oversight or governance function, either as an internal governance function or as an external monitoring function (internal independent assurance and oversight)
3. The independent assurance providers that give an objective assessment of the auditee's reporting (external independent assurance and oversight)

We assess the level of assurance provided by the role players based on the status of internal controls of auditees and the impact of the different role players on these controls. In the current environment, which is characterised by inadequate internal controls, corrected and uncorrected material misstatements in financial and performance information, and widespread non-compliance with legislation, all role players need to provide an extensive level of assurance.

What is the role of each key role player in providing assurance?

Senior management

Senior management, which includes the CFO, CIO and head of the SCM unit, provides assurance by implementing the following basic financial and performance controls:

- Ensure proper record keeping so that complete, relevant and accurate information is accessible and available to support financial and performance reporting.
- Implement controls over daily and monthly processing and reconciling of transactions.
- Prepare regular, accurate and complete financial and performance reports that are supported and evidenced by reliable information.
- Review and monitor compliance with applicable legislation.
- Design and implement formal controls over IT systems.

Municipal managers and municipal entities' chief executive officers

While we recognise that municipal managers and the CEOs of municipal entities depend on senior management for designing and implementing the required financial and performance management controls, they are responsible for creating an environment that helps to improve such controls in the following ways:

- Provide effective and ethical leadership and exercise oversight of financial and performance reporting and compliance with legislation.
- Implement effective HR management to ensure that adequate and sufficiently skilled staff members are employed and their performance is monitored, and that there are proper consequences for poor performance.
- Establish policies and procedures to enable sustainable internal control practices and monitor the implementation of action plans to address internal control deficiencies and audit findings.
- Establish an IT governance framework that supports and enables the achievement of objectives, delivers value and improves performance.
- Implement appropriate risk management activities to ensure that regular risk assessments, including the consideration of IT risks and fraud prevention, are conducted and that a risk strategy to address the risks is developed and monitored.
- Ensure that an adequately resourced and functioning internal audit unit is in place and that internal audit reports are responded to.
- Support the audit committee and ensure that its reports are responded to.

The MFMA also defines the role of the municipal manager as follows:

Role of the municipal manager

Robust financial and performance management systems	Oversight and accountability	Commitment and ethical behaviour
Full and proper records of financial affairs Effective, efficient and transparent systems for **financial and risk management** and **internal control** System of **internal audit** Develop and implement **policies** – tariffs, rates, credit control, debt collection and SCM Appropriate **management, accounting and information systems** – assets, liabilities, revenue and expenditure	Effective, efficient, economic and transparent **use of resources** Prevention of **unauthorised, irregular and fruitless and wasteful expenditure** as well as other losses	Act with **fidelity, honesty, integrity** and in the **best interest** of the municipality Manage and safeguard **assets and liabilities** Take appropriate **disciplinary steps** against any official who commits an act of financial misconduct or an offence **Disclose** all material facts to the council or mayor

The **role of the municipal manager** is critical to ensure:
timely, credible information + accountability + transparency + service delivery

Mayors

Mayors have a monitoring and oversight role at both municipalities and municipal entities. They have specific oversight responsibilities in terms of the MFMA and the MSA, which include reviewing the integrated development plan and budget management and ensuring that auditees address the issues raised in audit reports.

Mayors can bring about improvement in the audit outcomes of auditees by being actively involved in key governance matters and managing the performance of municipal managers.

Internal audit units

The internal audit units assist municipal managers and the CEOs of municipal entities in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation. The establishment of internal audit units is a requirement of legislation.

Audit committees

An audit committee is an independent body, created in terms of legislation, which advises the municipal manager or CEO, senior management and the council on matters such as internal controls, risk management, performance management as well as the evaluation of compliance with legislation. The committee is further required to provide assurance on the adequacy, reliability and accuracy of financial and performance information.

Coordinating or monitoring departments

Our country's constitution stipulates that national and provincial government must support and strengthen the capacity of municipalities to manage their own affairs, to exercise their powers and to perform their duties. The MFMA further requires national and provincial government to assist municipalities in building capacity to support efficient, effective and transparent financial management. Both the MFMA and the MSA define responsibilities to monitor financial and performance management.

Municipal councils

The council is the executive and legislative authority of the municipality. In order for the council to perform its oversight and monitoring role, the municipal manager and senior managers must provide the council with regular reports on the financial and service delivery performance of the municipality. The MFMA and the MSA also require the council to approve or oversee certain transactions and events, and to investigate and act on poor performance and transgressions, such as financial misconduct and unauthorised, irregular as well as fruitless and wasteful expenditure.

Municipal public accounts committees

The MPAC was introduced as a committee of the council to deal specifically with the municipality's annual report, financial statements and audit outcomes as well as to improve governance, transparency and accountability. The committee is an important provider of assurance, as it needs to give assurance to the council on the credibility and reliability of financial and performance reports, compliance with legislation as well as internal controls.

The primary functions of the MPAC can be summarised as follows:

- Consider and evaluate the content of the annual report and make recommendations to the council when adopting an oversight report on the annual report.
- Review information relating to past recommendations in the annual report; this relates to current in-year reports, including the quarterly, mid-year and annual reports.
- Examine the financial statements and audit reports of the municipality and municipal entities and consider improvements, also taking into account previous statements and reports.
- Evaluate the extent to which our recommendations and those of the audit committee have been implemented.
- Promote good governance, transparency and accountability in the use of municipal resources.

Portfolio committees on local government

In terms of our country's constitution, the National Assembly and provincial legislatures must maintain oversight of the executive authority responsible for local government. This executive authority includes the minister and MEC responsible for cooperative governance and other executives involved in local government, such as the minister and MEC responsible for finance. The mechanism used to conduct oversight is the portfolio committee on local government.

13.2 Glossary of key terminology used in this report

Asset (in financial statements)	Any item belonging to the auditee, including property, infrastructure, equipment, cash, and debt due to the auditee.
Backups (IT)	A backup, or the process of backing up, refers to the copying and archiving of computer data so that it may be used to restore the original after a data loss event. The primary purpose of a backup is to recover data after its loss, be it by data deletion or corruption.
Business continuity plan (IT)	A business continuity plan is a plan to continue operations if an auditee is affected by different levels of disaster, which can be localised short-term disasters, to days-long building-wide problems, to a permanent loss of a building. Such a plan typically explains how the auditee would recover its operations or move operations to another location after damage by events like natural disasters, theft or flooding. For example, if a fire destroys an office building or data centre, the people and auditee or data centre operations would relocate to a recovery site.
Cash flow (in financial statements)	The flow of money from operations: incoming funds are revenue (cash inflow) and outgoing funds are expenses (cash outflow).
Chief information officer or government information technology officer (IT)	The most senior official of the auditee who is accountable for aligning IT and business strategies; for planning, resourcing and managing the delivery of IT services and information; and for the deployment of associated human resources. The CIOs in the South African public sector are referred to as government information technology officers. The position was established by a cabinet memorandum in 2000.
Commitments from role players	Initiatives and courses of action communicated to us by role players in local government aimed at improving the audit outcomes.
Configuration (IT)	The complete technical description required to build, test, accept, install, operate, maintain and support a system.
Consolidated financial statements	Financial statements that reflect the combined financial position and results of a municipality and those of the municipal entities under its control.
Creditors	Persons, companies or organisations to whom the auditee owes money for goods and services procured from them.
Current assets (in financial statements)	These assets are made up of cash and other assets, such as inventory or debt for credit extended, which will be traded, used or converted into cash within 12 months. All other assets are classified as non-current, and typically include property, infrastructure and equipment as well as long-term investments.

Current liability (in financial statements)

Money owed by the auditee to companies, organisations or persons who have supplied goods and services to the auditee.

Disaster recovery plan (IT)

A disaster recovery plan is a documented process or set of procedures to recover and protect an auditee's IT infrastructure in the event of a disaster. Usually documented in written form, the plan specifies the procedures that an auditee is to follow in the event of a disaster. It is a comprehensive statement of consistent actions to be taken before, during and after a disaster. The disaster could be natural, environmental or man-made. Man-made disasters could be intentional (e.g. the act of an attacker) or unintentional (i.e. accidental, such as the wall of a man-made dam breaking).

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

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

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

Firewall (IT)

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

Going concern

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

Governance (as one of the drivers of internal control)

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

Implementing agent

Government institutions (e.g. the Independent Development Trust), non-governmental organisations or private sector entities appointed by the auditee to manage, implement and deliver on projects.

IT infrastructure (IT)

The hardware, software, computer-related communications, documentation and skills that are required to support the provision of IT services, together with the environmental infrastructure on which it is built.

Leadership (as one of the drivers of internal control)

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

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

Material finding (from the audit)

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

Material misstatement (in financial statements or performance reports)

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

Misstatement (in financial statements or performance reports)

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

Net current liability

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

Net deficit (incurred by auditee)

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

Oversight structures as well as coordinating and monitoring departments

Oversight structures consist of the provincial legislatures, the portfolio committees on local government and the NCoP.

Coordinating or monitoring departments include the DPME, the National Treasury and provincial treasuries, the DCoG and provincial Cogtas as well as the offices of the premier.

Refers to role players (1) that are directly involved with the management of the auditee (management/leadership assurance) – in other words, the first line of defence; (2) that perform an oversight or governance function, either as an internal governance function or an external monitoring function (internal independent assurance and oversight); and (3) that give an objective assessment of the auditee's reporting (external independent assurance and oversight).

Password (IT)	In access control, confidential authentication information, usually composed of a string of characters, may be used to control access to physical areas and to data. Passwords have to comply with certain complexity rules to ensure that they are not easy to guess.
Patch management (IT)	A piece of programming code that is added to an existing program to repair a deficiency in the functionality of the existing routine or program. It is generally provided in response to an unforeseen need or set of circumstances. Patching is also a common means of adding a new feature or function to a program until the next major version of the software is released.
Platform (IT)	A platform consists of an operating system, the computer system's coordinating program, which in turn is built on the instruction set for a processor or microprocessor, and the hardware that performs logical operations and manages data movement in the computer.
Property, infrastructure and equipment (in financial statements)	Assets that physically exist and are expected to be used for more than one year, including land, buildings, leasehold improvements, equipment, furniture, fixtures and vehicles.
Reconciliation (of accounting records)	The process of matching one set of data to another; for example, the bank statement to the cheque register, or the accounts payable journal to the general ledger.
Receivables or debtors (in financial statements)	Money owed to the auditee by companies, organisations or persons who have procured goods and services from the auditee.
Vulnerability (IT)	In information security, a weakness or flaw (in location, physical layout, organisation, management, procedures, personnel, hardware or software) that may be exploited by an attacker to cause an adverse impact.

13.3 Acronyms and abbreviations used in this report

AGSA	Auditor-General of South Africa
APAC	Association of Public Accounts Committees
B2B	back-to-basics
bn	billion
CEO	chief executive officer
CFO	chief financial officer
CIO	chief information officer
DCoG	Department of Cooperative Governance
DM	district municipality
DoRA	Division of Revenue Act
DPME	Department of Planning, Monitoring and Evaluation
DWS	Department of Water and Sanitation
EC	Eastern Cape
FS	Free State
GP	Gauteng
HR	human resources
IMFO	Institute of Municipal Finance Officers
IT	information technology
KZN	KwaZulu-Natal
LM	local municipality
LP	Limpopo
m	million
ME	municipal entity

MEC	member of the executive council
MET/metro	metropolitan municipality
MFMA	Municipal Finance Management Act, 2003 (Act No. 56 of 2003)
MIG	municipal infrastructure grant
Misa	Municipal Infrastructure Support Agent
MP	Mpumalanga
MPAC	municipal public accounts committee
MSA	Municipal Systems Act, 2000 (Act No. 32 of 2000)
mSCOA	Municipal Regulations on a Standard Chart of Accounts
MTSF	Medium-Term Strategic Framework
NC	Northern Cape
NCoP	National Council of Provinces
NW	North West
provincial Cogta	provincial department responsible for cooperative governance
PTNG	public transport network grant
Salga	South African Local Government Association
SCM	supply chain management
USDG	urban settlement development grant
WC	Western Cape

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