CONSOLIDATED
GENERAL REPORT ON THE LOCAL GOVERNMENT AUDIT OUTCOMES

MFMA
2016-17

AUDITOR-GENERAL
SOUTH AFRICA

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Auditing to build public confidence

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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.

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.

PERFORMANCE SNAPSHOT

(Refer to section 2 for explanations on how to interpret these figures and movements)

Clean audits

13% ▼

(2015-16: 20%)

OVERALL REGRESSION IN AUDIT OUTCOMES ▼

45 ∨ *Regressed*

16 ∧ *Improved*

Quality financial statements

61% ▼

(2015-16: 68%)

22% *(53)*

Municipalities submitted financial statements without material misstatements

R757 million

(2015-16: R752 million)

Cost of consultants to assist in financial statement preparation

42% *(101)*

Financial statements submitted for auditing included **material misstatements in the areas in which consultants did work**

No findings on compliance with legislation

14% ▼

(2015-16: 21%)

Irregular expenditure

▼

R28,376 bn

(2015-16: R16,212 bn)

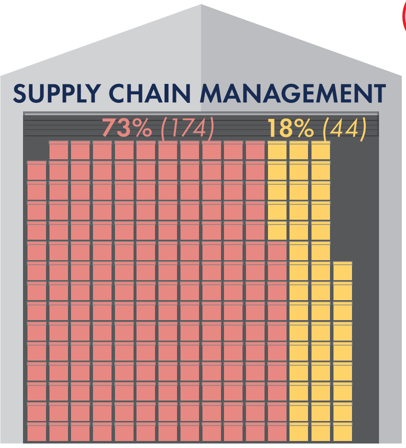
Quality performance reports

37% ▼

(2015-16: 48%)

51% *(120)* *Achievement reported not reliable*

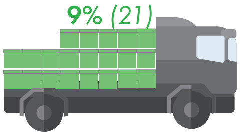
▼ SUPPLY CHAIN MANAGEMENT COMPLIANCE



Not able to audit procurement of **R1,296 billion** due to missing or incomplete information

R2,075 billion in prohibited awards to other state officials

False declarations of interest made by **1 440 suppliers**



Uncompetitive and unfair procurement processes at **67% of municipalities**

🟩 With no findings 🟨 With findings 🟥 With material findings

EFFECTING CONSEQUENCES

55% Compliance with legislation on implementation of consequences **regressed**

39% Investigation of previous year's unauthorised, irregular and fruitless and wasteful expenditure **regressed** (*closing balance not dealt with is R66,925 billion*)

29% Investigations into supply chain management findings we reported in previous year **slightly regressed**

STATUS OF CONTROLS

22% Overall internal controls **slightly regressed**

17% Basic financial and performance management controls **regressed**

20% Information technology controls **slightly improved**

HUMAN RESOURCE MANAGEMENT

MUNICIPAL MANAGER

VACANCIES **27% (65)** ▼

VACANT for 6 months or more - **17% (41)**

CHIEF FINANCIAL OFFICER

VACANCIES **28% (68)** ▼

VACANT for 6 months or more - **21% (51)**

FINANCIAL HEALTH

DEFICIT (expenditure exceeded revenue)			*CREDITOR-PAYMENT PERIOD > 30 DAYS*	
2016-17	31% (66)	▲	87% (183)	▼
2015-16	33% (68)		82% (170)	

VULNERABLE FINANCIAL POSITION

2016-17	31% (73)	▼
2015-16	26% (59)	

Fruitless and wasteful expenditure of **R1,1 billion** incurred by those in vulnerable financial position

ASSURANCE PROVIDERS

▼ OVERALL REGRESSION IN ASSURANCE PROVIDED BY ROLE PLAYERS

Senior management and municipal managers **regressed**

Mayors, councils and municipal public accounts committees **slightly regressed**

Internal audit units and audit committees **regressed**

National and provincial role players **regressed**

INFRASTRUCTURE

26% water projects exceeded completion date

46% had no water maintenance plan

22% did not budget for maintenance of water infrastructure

40% had water losses of more than 30%

35% did not assess condition of water infrastructure

26% road projects exceeded completion date

55% did not have approved road maintenance plan/priority list for renewal and routine maintenance ▼

27% did not assess condition of all road infrastructure ▼

METROS ▼

Almost **55% (R195 billion)** of the total municipal expenditure budget of **R362 billion** was managed by metros

Financial statements	▶
Compliance	▼
Performance reports	▶
Irregular expenditure **R12,456 bn** *(8 metros [100%])*	▼

ROOT CAUSES

77% ▼ Slow response in improving internal controls and addressing risk areas

61% ▼ Inadequate consequences for poor performance and transgressions

59% ▼ Instability or vacancies in key positions or key officials lacking appropriate competencies

NOTES

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, supply chain management 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

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 2016-17 (municipalities)

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

EASTERN CAPE

Ingquza Hill
Senqu

FREE STATE

No municipality in the Free State achieved a clean audit

GAUTENG

Midvaal

KWAZULU-NATAL

Okhahlamba
Ray Nkonyeni
uMhlabuyalingana
uMhlathuze
uMuziwabantu
Umzumbe

LIMPOPO

No municipality in Limpopo achieved a clean audit

MPUMALANGA

Ehlanzeni District
Nkangala District

NORTHERN CAPE

ZF Mgcawu District

NORTH WEST

No municipality in North West achieved a clean audit

WESTERN CAPE

Cape Winelands District
Overberg District
West Coast District
Bergriver
Breede Valley
Cape Agulhas
Cederberg
Drakenstein
George
Hessequa
Langeberg
Matzikama
Mossel Bay
Overstrand
Prince Albert
Saldanha Bay
Stellenbosch
Swartland
Swellendam
Theewaterskloof
Witzenberg

SECTION 1

Executive summary

1 EXECUTIVE SUMMARY

Accountability and the need for appropriate consequences for accountability failures featured as prominent elements of our messages in 2015-16. Through the previous general report and the many engagements we had with the newly elected mayors and councillors, **we highlighted the shortcomings** we identified through our audits and we provided many recommendations to improve accountability. We called on leadership to prioritise accountability and **highlighted the fact that there might be regressions in audit outcomes** following changes in the political leadership – which we also witnessed in 2011-12. Some of the media headlines following that regression are reflected just after this section.

The key message that we can take from the 2016-17 audits is that **accountability continues to fail in local government.**

There are three main indicators of these accountability failures:

1. **Audit outcomes regressed and irregular expenditure increased**

- **Overall, the audit outcomes regressed.** The audit outcomes of 45 municipalities regressed while those of 16 improved. Only 33 municipalities (13%) managed to produce quality financial statements and performance reports and to comply with key legislation, thereby receiving a clean audit.

- Credible **financial statements and performance reports** are crucial to enable accountability and transparency, but municipalities are failing in these areas. Not only did the unqualified opinions on the financial statements decrease from 68% to only 61%, but the financial statements provided to us for auditing were even worse than in the previous year. Only 22% of the municipalities could give us financial statements without material misstatements. In addition, the performance reports of 62% of the municipalities that produced reports had material flaws and were not credible enough for the council or the public to use.

- Municipalities were in various stages of readiness for the implementation of the **Municipal Standard Chart of Accounts** by 1 July 2017. This is a significantly revised classification framework and required changes to the accounting processes and information systems. We identified various challenges with implementation, which need to be addressed to ensure that these do not affect the ability of municipalities to produce reliable financial statements in 2017-18.

- We reported **material non-compliance** with key legislation at 86% of the municipalities. This is the highest percentage of non-compliance since 2012-13. Municipalities with material compliance findings on supply chain management increased from 63% to 73%.

- **Irregular expenditure increased** from R16,212 billion to R28,376 billion (a 75% increase). It is important to note, however, that municipalities made a significant effort in 2016-17 to identify and transparently report on irregular expenditure incurred in previous years – this accounts for R15,026 billion of the total. The remaining R13,350 billion relates to payments or expenses in 2016-17 by the new local government administration, which represented 4% of the local government expenditure budget. It includes payments made on contracts irregularly awarded in a previous year – if the non-compliance was not investigated and condoned, the payments on these multi-year contracts continue to be viewed and disclosed as irregular expenditure. By analysing the top 26 contributors to irregular expenditure, we estimated that 16% (±R4,5 billion) represented non-compliance by the new administration.

2. **There has been little improvement in the accountability (plan+do+check+act) cycle**

- The **recommendations** we made last year to improve audit outcomes and accountability **did not receive the necessary attention**. This is evidenced by the findings from our audits that included attention not being paid to audit action plans, poor performance planning and budgeting (resulting in unauthorised expenditure of R12,6 billion), and regressions of varying degree in the status of internal control and the assurance provided by the different role players in local government.

- Of most concern is that our consistent and insistent calls to increase consequences have not been heeded – we reported material non-compliance with legislation on the implementation of consequences at 55% of the municipalities. This **lack of consequences** is also evident in municipalities again not paying sufficient attention to the findings on supply chain management and the indicators of possible fraud or improper conduct that we reported and recommended for investigation. In 2015-16, we reported such findings at 148 municipalities, but 47% of them investigated none of the findings and 24% only some of the findings. In 2016-17, we reported these types of findings at 61% of the municipalities, of which 71% also had such findings in 2015-16.

- At 61% of the municipalities, the council failed to conduct the **required investigation** into all instances of unauthorised, irregular and fruitless and wasteful expenditure reported in the previous year – a regression from 52% in the previous year. Sufficient steps were also not taken to recover, write off, approve or condone unauthorised, irregular and fruitless and wasteful expenditure as required by legislation. As a result, the year-end balance of irregular expenditure that had accumulated over many years and had not been dealt with totalled R65,32 billion, while that of unauthorised expenditure was R43,5 billion and that of fruitless and wasteful expenditure was R4,24 billion.

3. **Increasingly difficult environment for auditing**

- **The audit environment became more hostile** with increased contestation of audit findings and pushbacks whereby our audit processes and the motives of our audit teams were questioned. At some auditees, pressure was placed on audit teams to change conclusions purely to avoid negative audit outcomes or the disclosure of irregular expenditure – without sufficient grounds. Some auditees used delaying tactics whereby information and evidence were not provided as requested. Leadership should set the tone for accountability – if audit outcomes are not as desired, energy should be directed to addressing the problem and not to coercing the auditors to change their conclusions.

The accountability failures in local government result in municipalities not achieving their objectives, which in turn has a negative impact on the lives of citizens. Our audits highlighted **two key areas of impact**: the financial health of municipalities and the delivery and maintenance of municipal infrastructure. The following are examples of how accountability failures negatively affect the lives of citizens:

- The **inability to collect debt** from municipal consumers was widespread. In these circumstances, it is inevitable that municipalities will **struggle to balance the books**. In total, 31% of the municipalities disclosed a deficit – the total deficit for these municipalities amounted to R5,6 billion. The financial woes of local government also weighed heavily on municipal creditors. The impact of this **inability to pay creditors** was most evident in the huge sums owed for the provision of electricity and water to Eskom and the water boards, respectively. A combination of various factors, including poor revenue and budget management and the non-payment of creditors, led to 31% of the municipalities disclosing in their financial statements that they **might not be able to continue operating**. Although they have to continue to do so, they were reporting that they were in a particularly vulnerable financial position at the end of the financial year.

- While the poor economic climate does play a role in the deterioration of municipalities' financial health, many are just not managing their finances as well as they should. **Fruitless and wasteful expenditure** amounted to R1,5 billion (a 71% increase from the previous year). It is difficult to say how much money is lost through irregular processes, as this needs to be determined through an investigation, but the non-compliance we reported at 78% of the municipalities can potentially lead to a financial loss.

- Our audits again identified a number of shortcomings in **the development and maintenance of infrastructure**. These included the underspending of grants, delays in project completion, poor quality workmanship, and inadequate monitoring of contractors. These are symptoms of the larger problem that local government has with managing finances, performance and projects and with taking accountability for outcomes. Although funding and support are generally available from national government for the development and maintenance of municipal infrastructure, the non-delivery thereof at some municipalities and the impact on communities are the issues that need the most focused attention by all role players to ensure that the objective of a better life for all is achieved.

There were **varied reasons for the accountability failures**:

- **Vacancies and instability in key positions** slowed down systematic and disciplined improvements.

- **Inadequate skills led to a lack of oversight** by councils (including the mayor) and insufficient implementation and maintenance of financial and performance management systems by the administration.

- **Political infighting** at council level and interference in the administration weakened oversight and the implementation of consequences for transgressions, and made local government less attractive for professionals to join.

- Leadership's inaction, or inconsistent action, created a culture of **'no consequences'**, often due to inadequate performance systems and processes.

- At some municipalities there was a **blatant disregard** for controls (including good record keeping) and compliance with key legislation, as it enabled an environment in which it would be easy to commit fraud.

- Leadership did not take our **repeated recommendations and warnings** of risks for which they needed to prepare seriously.

- Municipalities focused on obtaining **unqualified financial statements** at a great cost by using consultants and auditors, which was to the detriment of credible performance reporting and compliance with key legislation.

- Provincial and national role players **did not sufficiently support** municipalities.

We have seen again and again that many of these problems can be turned around through strong, ethical and courageous leadership in the administration and council, with the support of provincial government. The audit outcomes and levels of accountability varied among the municipalities in the different provinces.

The trend of improvements in the past few years in the **Eastern Cape** did not continue. Six municipalities in the province improved their outcomes but seven regressed. We warned these municipalities to keep the administration as stable as possible, fill vacant positions, and not underestimate the complexities of the mergers of municipalities. Of greatest concern in this province were the accountability failures in the areas of supply chain management and infrastructure development. Infrastructure projects were not delivered as a result of poor planning and project management. Irregular expenditure of R13,558 billion (48% of the total irregular expenditure) was incurred by municipalities in the Eastern Cape. This represented 35% of their provincial local government expenditure budget.

The continued lack of accountability and leadership failures in the **Free State** were the main causes of governance failures, which led to a significant regression in audit outcomes from the prior year. Seven municipalities regressed while no auditees were able to improve. The deterioration in municipalities' financial health was due to leadership not considering the budget when committing to strategic projects, not always paying the best price for goods and services, and wastage caused by poor planning. Without improved fiscal disciplines for the more effective, efficient and economical use of resources, municipalities' financial health and service delivery will continue to deteriorate.

The results in **Gauteng** held steady with all municipalities maintaining their outcomes from the previous year. This was the only province that had 100% unqualified audit opinions. We continue to highlight that non-compliance with legislation remains the major obstacle preventing most municipalities in the province from attaining a clean audit.

KwaZulu-Natal continued on its downward path that started in 2015-16, with 13 municipalities regressing. We cautioned that at these municipalities, complacency and a lack of follow-through on the previous administration's commitments had an effect. Leadership did not decisively deal with the weaknesses we reported and warned them about. If these lapses in accountability are not dealt with, the regressions will continue.

Limpopo had five municipalities that regressed during the year under review. The province is characterised by complacency with unqualified financial statements being seen as good enough, underperformance as no action is taken to improve, and poor performers with high levels of transgressions and no consequences. This took place notwithstanding the premier's commitment in the previous year to implement stricter consequences. Accountability failures are also evident in inadequate infrastructure development and financial management, which have an impact on the delivery of services.

Mpumalanga saw an improvement in the overall 2016-17 audit outcomes – a continuation of the trend of slow but steady improvements over the past few years. While this is commendable, a lot of work is still needed to ensure that the improvements are sustainable, to curb irregular expenditure (which amounted to 10% of the provincial local government expenditure budget), and to address delays in infrastructure and basic service delivery.

In the **Northern Cape**, the overall outcomes remained the same (two municipalities improved and two regressed). The stagnation confirms that our previous year's message of mayors, municipal managers and senior management needing to hold each other and their subordinates accountable, was blatantly disregarded, resulting in many instances where similar findings were raised during the audit process.

North West stood out when it came to irregular expenditure – contributing 15% of the total irregular expenditure in 2016-17, which represented 22% of their provincial local government expenditure budget. We are also particularly concerned about infrastructure delivery and maintenance as well as the use of grants in North West. The lack of accountability for sound financial management by the leadership had a negative impact on municipalities' financial viability. At eight (35%), the financial information was not reliable enough to analyse financial viability (as they had disclaimed opinions), while a further 20% were in a vulnerable financial position. Given the already vulnerable position of local government, we are very concerned about the overspending of budgets by 16 municipalities, resulting in unauthorised expenditure of R1,19 billion. The financial viability of municipalities needs to be addressed urgently, as it has a direct impact on their ability to continue rendering services.

At 70%, the **Western Cape** still had the largest concentration of municipalities with clean audits, but the audit results of six municipalities, including the City of Cape Town, regressed in the year under review. The changes after the local government elections caused some instability at council level and in key senior positions, but the regressions can mostly be attributed to our messages on risks and recommendations not receiving the attention these warranted.

Overall, the **audit outcomes of the eight metros** regressed with Buffalo City improving but Mangaung and the City of Cape Town regressing. Although six of the metros produced unqualified financial statements, only 50% had credible performance reports and all of them had material compliance findings. The irregular expenditure increased significantly at the metros, but it was mostly as a result of uncovering and disclosing irregular expenditure from previous years. The financial health of half of the metros was stable, but we raised concerns about the City of Johannesburg, City of Tshwane and Nelson Mandela Bay, with Mangaung being in a particularly vulnerable financial position.

As the Auditor-General of South Africa, we have **an important role to play in the accountability chain** and we go beyond the basic auditing and reporting role of the auditor. Through our management, audit and general reports, we have been reporting the weaknesses in internal control and the risks that need attention in local government. In our reports, we provide the root causes of audit findings and recommendations to address the root causes. We ensure that our messages are heard through engagements with senior officials, municipal managers, mayors, municipal public accounts committees, and councils. We will continue with adding value through these practices, but they have not had the desired impact yet – as evidenced in the poor audit outcomes.

Hence, we are increasing our efforts through extending our engagements with municipal managers to a **status of records review**. Such a review is an assessment of records, risks and progress made by the municipality to address prior year issues early in the financial year. This provides an early warning system whereby municipal managers can be alerted to matters that can potentially lead to undesirable audit outcomes. All of these measures are aimed at assisting the municipal leadership and the council to prevent accountability failures, or to provide them with information on how to deal with such failures where they have occurred.

The accountability mechanisms in local government are not working as they should and there have been continued calls for more to be done – particularly by my office. Through the support of our parliamentary oversight committee, we are thus busy **amending the Public Audit Act** to provide us with more power to ensure accountability in the public sector.

The intent of the amendments is not to take over the functions of the municipal manager, the mayor or the council, as their accountability responsibilities are clear in municipal legislation. It is rather to step in where those responsibilities are not fulfilled in spite of us alerting leadership to material irregularities that need to be investigated and dealt with. The amendments, if approved, will provide us with the **power to refer** material irregularities to appropriate authorities to investigate as well as the **power to recover** money lost as a result of such irregularities.

If we had those powers today already, there would have been a number of cases in local government that would have been referred based on **material irregularities that we had reported to municipal management and the council to deal with, without any success**. The extension of our mandate to deal with these types of irregularities will assist in restoring public confidence, solidifying accountability, and entrenching the ethical behaviour that is expected of entrusted officials and elected representatives. It will also mean that our reports will be taken seriously and we could start to see an improvement in the audit outcomes.

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 for accountability and doing the basics right. We encourage the municipal leadership and all stakeholders involved in local government to intensify their efforts to ensure that communities experience an improvement in the way their municipalities operate.

MEDIA PERSPECTIVES ON MFMA 2011-12 AUDIT OUTCOMES

‘Wasteful expenditure doubles to R10-billion’

14 August 2013 – *Sowetan* –

‘Councillors must be “accountable” ’

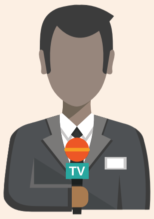
14 August 2013 – *New Age* –

‘Public officials in dire straits’

14 August 2013 – *The Times* –

‘Lack of accountability distressing’

19 August 2013 – *Herald* –



‘SLOW MARCH TO CLEAN AUDITS’

14 August 2013 – *Cape Argus* –

‘MUNICIPAL MESS!’

14 August 2013 – *Daily Sun* –

‘Lack of political will, root cause of problems’

14 August 2013 – *Cape Times* –

‘Municipalities squander millions of rands’

23 August 2013 – *Letaba Herald* –

‘CT stumbles on officials doing business with city, says AG’

14 August 2013 – *Cape Times* –

Municipalities must be able to do better than this

19 AUGUST 2013 - MARK BARNES

THE most depressing comment I heard in relation to the recently concluded auditor-general's report on our municipalities (or, perhaps, the one that made me most angry) was: "Well, what did you expect?"

I expect better.

We can do better.

Running a municipality properly is not rocket science. It requires no artistic flair or innovative genius – you've just got to do it right.

Running a municipality is a fairly simple business, compared to most businesses in the private sector.

You know who your clients are. Not just their cellphone numbers or e-mail addresses, you know where they live – because they live within your jurisdiction.

What's more, if even one of them leaves, another inevitably moves in. You don't even have to Fica them (capture their details for the Financial Intelligence Centre Act) – you are the provider of their Fica information; they need you more than you need them.

How do you deal with competitors? Hang on, you have no competitors – there's only one city council, only one municipality per municipality. No need for the Competition Commission here.

You don't even have to advertise your products and services, no need for loyalty programmes or summer sales. Your clients are here to stay. Actually, your clients stay here.

What about pricing policy? Anything you like, really. You're a government legislated monopoly. You can charge what you like, and if they don't pay, regardless of the quality of your delivery, you cut off their vital services until they do. Simple.

What if you need to raise funding? Well, you don't really. You just have to balance your books. Expenses must not exceed income. That's easy, because you control both.

In fact, if you run this kind of business well, because of the predictable nature of its cash flows, capital can be raised at very competitive rates to build things that improve your municipality and attract even more ratepayers to live there. The virtuous circle of competence. Around the world there is a well-developed asset class of muni-bonds that find their place in most income-focused portfolios. Not here, though. And the reasons behind that become abundantly clear when we examine the findings of the Consolidated General Report on the Audit Outcomes of Local Government.

The report covers 317 municipalities, auditees as they are referred to (I like that word, we're all auditees at some point). The number of auditees exceeds the number of municipalities by 21, those that didn't bother even to submit a report. I love it. "Sorry, we're not going to do a report this year, okay? I thought maybe next year?" How do you get away with that? Surely if you break the law you go to jail? Of course not. Who's going to lock themselves up in their own jail? Silly.

> “If you run this kind of business well, because of the predictable nature of its cash flows, capital can be raised at competitive rates to build things that improve your municipality

Throughout the report it becomes clear that the leadership weren't able to persuade those under their authority to do the right thing – most often because the leadership themselves don't know what to do, and don't have the required competence and skills. Not great.

In the private sector there is a remedy for nonperformance or breaking the rules. You get fired. It seems to work.

The real worry is that things seem to be getting worse, "regressing".

It has almost become endemic in our society that procurement processes and contract management are fraught with opportunity for fraud and favouritism. Our municipalities have the dubious distinction that 84% of them show a flagrant disregard for governance and transparency in awarding lucrative contracts (that means that only 16%, one in six, don't). Contracts to the value of "at least" R118m were awarded to employees or councillors.

MONDAY
COMMENT

Mark **Barnes**

Twitter: @mark_barnes56

That's astounding. In the real world that would be directors and staff getting company deals. Such activities have caused the downfall of significant players in the private sector. It is not okay.

Our framework for good behaviour in the private sector is well and visibly governed by many overlapping pieces of legislation and oversight, particularly when you're using other people's money. An obvious example is the rules that govern whether or not you may list your company on the JSE to enable participation in the capital markets. If you don't comply, you get suspended. There are no exceptions.

Of those audit reports that were in on time, about a quarter had not passed the "going concern" test. How does a municipality go bust? In our world, no going concern, never mind no listing, means no bank facilities, no supplier credit, no second chance, no next year, no nothing.

"Technical knowledge of financial management and reporting, performance management and legislation is not a prerequisite for elected office bearers". I understand that, this is no different in any democratic election process. However, successful leaders recognise their skills gaps and fill them. Those who try to cover them up or appoint even less qualified people always get found out, always fail.

Here's the best part. Instead of training people or setting about finding qualified people to do the job (or at least make progress towards doing the job), what did our municipalities do? You guessed it – they hired consultants. Those who can't do, consult, we all know that. I'm sure consultants can be useful, but they have to be a catalyst, not a substitute. Often, consultants, armed with slick presentations and MBA catch-phrases present generic solutions to the described problem. But then they leave, with nobody qualified to implement the proposed solution, never mind whether it's right or wrong. Perhaps it could have worked for our municipalities, but it didn't. More than two-thirds of our municipalities spent nearly R400m collectively on consultants in the 2011-12 financial year. The auditor-general found that, "Overall, 75% of the auditees that had material misstatements in their submitted financial statements were assisted by consultants." How about that? Why didn't these consultants get fired? Why did they get paid at all?

In a world where the uninspired lead the incompetent on a path of nondelivery it will be no surprise that one of the root problems identified is a lack of accountability, and a tolerance for continued poor performance. If you don't even know what is right, how can you possibly sit in judgment, let alone effect change?

In the result, only 5% of all auditees got clean bills of health. Remarkably, not one of the eight metros did. You would've thought that the metros would at least have the resources and experience base to address the challenges. Stories abound on how past experience has been set aside (or at least made to feel unwelcome) in favour of new employees with no previous experience. I heard recently that the government employs something like 70% of all new school-leavers. Is that true? If it is, is it a good thing? Is it part of the job-creation strategy or is it a political imperative to retain support from the obviously disappointed youth – many of whom remain unemployed regardless?

In the case of 299 of the 317 auditees, material noncompliance with legislation was reported. Wow.

> Taken together they've blown more than R20bn of our money. That's a whole bunch of dustbins, or repaired potholes, or water piping or electric wiring or painted road signs or toilets

Now for the juicy stuff. There was "unauthorised" expenditure of R9.8bn, "irregular" expenditure of a similar amount (both up 30% on the previous year), and "wasteful" expenditure of R600m.

Taken together, they've blown more than R20bn of our money – now that's real!

That's a whole bunch of dustbins, or repaired potholes, or water piping or electric wiring or painted road signs or inside toilets connected to the sewage system, or whatever. New schools or police stations or hospitals. I could go on and on, it's a lot of cash. This can surely be fixed, no training required. Come on all you mayors out there, zero tolerance for stealing the money?

There are 330 companies listed on the JSE. If their performance was as bad as our municipalities have been found out to be, then only 17 wouldn't be suspended, only 148 would be given a second chance to get their act together. The rest would simply get delisted.

That would be a fatal blow for the efficient capital market for business. Unthinkable, unacceptable.

I applaud the transparency and brutal criticism of the report.

In fact it could be found to be a little harsh. For instance, about half the auditees received an unqualified report on their financial statements but failed to get a clean report for other reasons, so maybe things aren't all bad.

Audit reports and auditors aside, it is the reality that counts. Of course there is much to fix and even more to complain about, but, somehow, with some terribly notable lavatorial exceptions, the country still kind of works, most of the time.

So what can we do? I think it all has to start with amnesty and acceptance. Yeah, I know, there's a lot of that going around nowadays. But it's the only sure way to get people to put up their hands and ask for help. Can you imagine how soul-destroying it must be to go to work every morning, not knowing what you're doing?

Pick some of the leaders from the places that work and spread them around. Go on Gauteng, ask the Western Cape how they did it.

By the way, I recently met one of the candidates for the next Gauteng premier, Mmusi Maimane. Maybe there is hope? Okay, so rule one is find the proven leaders and deploy them nationally.

Rule two is educate, educate, educate. We all know this, but I've heard it's somewhat down the hierarchy of aspirations – probably because you can't eat it. Well, if you educate yourself more now, you'll eat more later, so get started.

In the meantime, fire all those consultants. Instead, go and hire back some of that prematurely retired expertise that you got rid of in a power moment. Not forever, just until the expertise has actually been transferred. One of the most valuable aspects of authority is that you can require of people that they teach you.

Whatever you do, Mr Government, don't nationalise anything!

NOTES

SECTION 2

Introduction

2 INTRODUCTION

In this first year of the new administration, our 2016-17 report reflects on the lack of progress made in improving financial and performance management in local government. In our 2015-16 report, we focused on the need for accountability in local government and warned against regressions in audit outcomes as a result of the instability following changes in the political leadership and of disowning the messages and not honouring the commitments made by the previous administration – which we also witnessed in 2011-12. This report shows that the audit outcomes did regress and that our recommendations were not heeded.

This led us to choose the **impact of accountability failures** in local government as the central theme for this report. This year, our report is also more focused as we have been reporting on many of the matters in a lot of detail, including explanations and recommendations, with seemingly little impact.

In section 3, we report on the **accountability failures in local government** to share what we see as the indicators, impact and root causes of such failures, while we also look at our current and future role as the Auditor-General of South Africa in strengthening the accountability chain.

Section 4 **summarises the audit outcomes**. It covers all the areas we had reported on in previous general reports (with the addition of a section on the metros), but now more simply and concisely. We provide an overview of the **results and reflections per province** in section 5. We explain more about our audit process and terminology in section 6. Our website (**www.agsa.co.za**) includes **detailed annexures** that provide the key results per municipality and municipal entity.

Please note the following important matters when reading this report:

- We audited 257 municipalities and 21 municipal entities in 2016-17. The number of municipalities decreased from 278, with the amalgamation of some municipalities during 2016 (37 municipalities were closed down and 16 new municipalities were established).
- To simplify our reporting and ensure that our message is focused, this report centres on only the municipalities. The audit outcomes of the municipal entities are included in the annexures to this report (which are available on our website), but not in the analysis in this report.
- When studying the figures, please note that the percentages are calculated based on the 239 completed audits (18 audits were not finalised), unless indicated otherwise.
- To determine the movements from the previous year, we compared the results of the municipalities with completed audits with their results in 2015-16, for which a denominator of 225 was used. The difference was as a result of the amalgamations – the newly formed municipalities are viewed as municipalities without a prior year history, which is consistent with how it was dealt with by the National Treasury.

Movement from the previous year is depicted as follows:

▲ Improved

▶ Unchanged

▼ Regressed

Movement of 5% or less: ▲ Slightly improved ▼ Slightly regressed

We use the following icons in this report to indicate:

💡 Accountability failures

📖 Explanations of terminology – we also explain more about our audit process and terminology in section 6

🔍 What we have found

🔍 Examples to illustrate the effects of weaknesses

// SECTION 3

Accountability failures in local government

3 ACCOUNTABILITY FAILURES IN LOCAL GOVERNMENT

In local government administration, 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. **Accountability is critical** and means that municipal leaders are answerable to local communities 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 Medium-Term Strategic Framework (derived from the National Development Plan) 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, with the support of national and provincial government and oversight.

Through the 2015-16 general report and the many engagements we had with the newly elected mayors and councillors, **we highlighted the shortcomings** we identified in financial and performance management and compliance with legislation as well as in the development and maintenance of infrastructure. We also called on the municipal leadership to ensure that accountability is given the highest priority, as the 2016-17 audit outcomes could be negatively affected if the new administration 'disowned' the audit outcomes of the previous year and did not follow through on the commitments made by their predecessors to improve audit outcomes. We urged them to take responsibility for the role that they play and to ensure that accountability is enforced and that failures are adequately dealt with by implementing consequences. We **warned leadership against regressions in audit outcomes** as a result of the instability following changes in the political leadership – which we also witnessed in 2011-12.

Consequences and accountability featured as prominent elements of our messages and we provided many recommendations, including the use of the **accountability cycle**. The cycle encourages a commitment to continuous improvement, which will ensure a solid foundation for accountability in the work of municipalities.

Additional information on the contents of this section is available in the summary of audit outcomes in section 4.

THREE INDICATORS OF ACCOUNTABILITY FAILURES

The key message that we can take from the results of the 2016-17 audits is that **accountability continues to fail in local government**. There are three main indicators of these accountability failures, as detailed below.

INDICATOR 1: AUDIT OUTCOMES REGRESSED AND IRREGULAR EXPENDITURE INCREASED

Clean audits: 13%
(2015-16: 20%)

Quality financial statements: 61%
(2015-16: 68%)

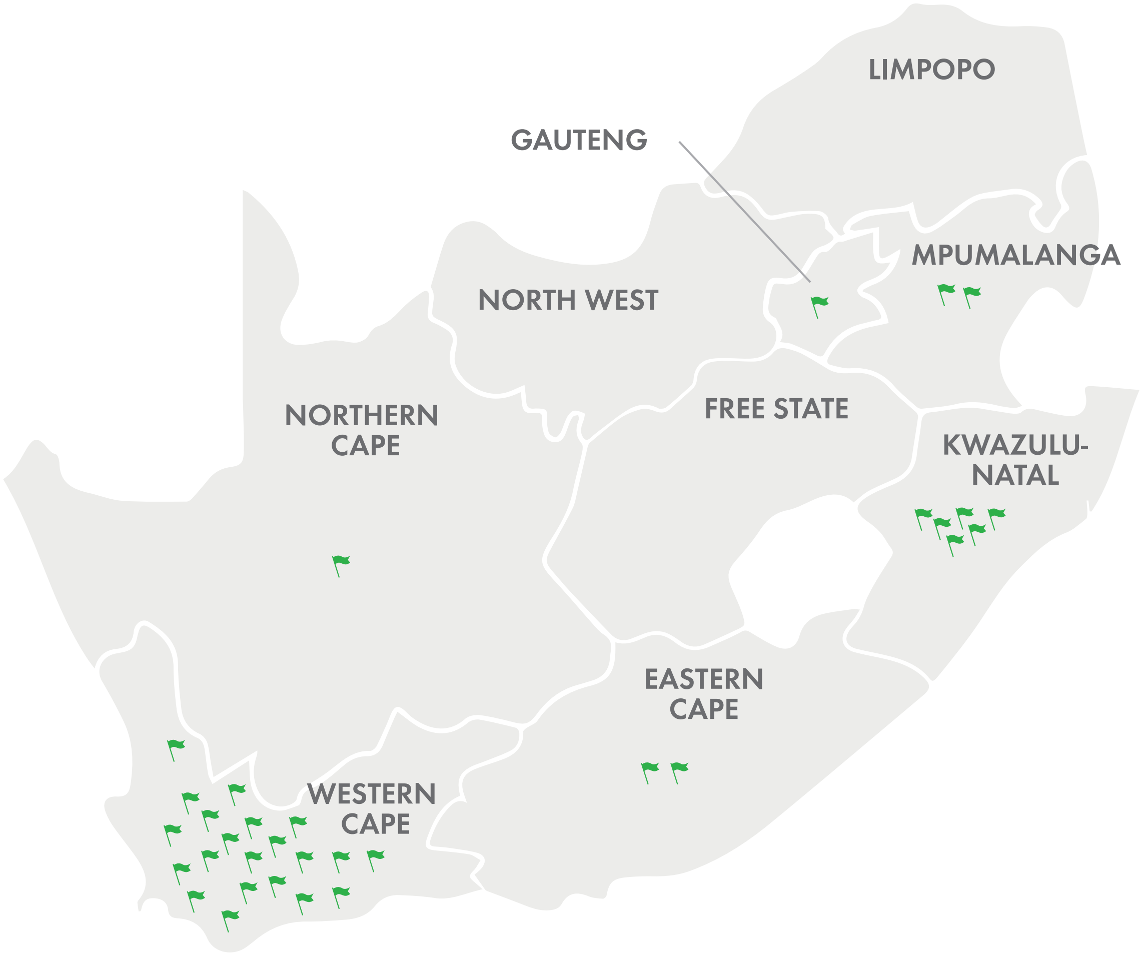
Quality performance report: 37%
(2015-16: 48%)

No findings on compliance with legislation: 14%
(2015-16: 21%)

Irregular expenditure: R28 376 m
(2015-16: R16 212 m)

The **audit outcomes of 45 municipalities regressed** (of which 17 were from a clean audit status) and those of only 16 improved. **Only 33 municipalities** (13%) managed to produce quality financial statements and performance reports and to comply with key legislation, thereby **receiving a clean audit**.

Only six of the nine provinces had municipalities with clean audits, as illustrated below.



Credible financial statements and performance reports are crucial to enable accountability and transparency, but municipalities are failing in these areas.

WHY ARE THE FINANCIAL STATEMENTS IMPORTANT?

The financial statements of a municipality show how it spends its money, where its revenue comes from, its assets and the state of those assets, how much it owes creditors, how much is owed to the municipality, and whether it is expected that the money owed will be received.

It also provides crucial information on how the budget was adhered to, the unauthorised, irregular and fruitless and wasteful expenditure incurred as well as the overall financial position of the municipality – whether its operations are financially sustainable.

The financial statements are used by the municipal council to call the municipal manager to account and to make decisions on the financial management of the municipality. It is also used by creditors, banks and rating agencies to determine the level of risk in extending debt to a municipality and by the public to know how well the municipality is using the rates and taxes they pay to provide services.

WHAT DID WE FIND?

Not only did the overall quality of the financial statements regress, the **financial statements provided to us for auditing were even worse than in previous years.** Only 22% of the municipalities could give us financial statements without material misstatements.

This means that if we had not identified the misstatements for the municipalities and allowed them to correct these, 78% of the municipalities would have published financial statements that were not credible.

This is a poor reflection on the financial management and capabilities in local government. Even bringing in consultants at a cost of R757 million to prepare financial statements and underlying records did not have the desired impact – at 101 municipalities (42%), the financial statements submitted for auditing included material misstatements in the areas in which consultants did work.

WHY IS THE PERFORMANCE REPORT IMPORTANT?

The performance report describes the progress made on commitments to the community on services and developments through the integrated development plan for the five years of the new administration. In its simplest form, this is where election promises are accounted for.

Municipalities determine how the progress will be measured (through performance indicators) and what the annual targets will be. The budget of a specific year is then matched to what the municipality needs to achieve for that year. This annual performance plan is included in the service delivery and budget implementation plan prepared by the municipality.

The performance report shows the performance measures, planned targets and achievements for the year. The municipal council represents the community's interest as its elected officials – they use this report to determine if the municipality achieved the objectives for the year, to make decisions on the next year's budget, and to hold the administration to account for any failings in delivery. This is also the report that the public uses to assess delivery by the municipality.

WHAT DID WE FIND?

The poor results for 2016-17 mean that **the performance reports of 62% of the municipalities had material flaws and were not credible enough for the council or the public to use**.

At 46% of the municipalities, these flaws were caused by poor planning as evidenced by performance indicators that were not well defined or verifiable; and targets that were not measurable or specific enough to ensure that the required performance could be measured and reported in a useful manner. We also found municipalities reporting on indicators or targets that differed significantly from what was in the plans.

At 51% of the municipalities, the achievement reported was not reliable – we either found evidence that disputed what was reported or could not find evidence for the reported achievements.

Four municipalities did not even prepare reports, while 10 prepared a report but could not give us the plans or any evidence in support of the report.

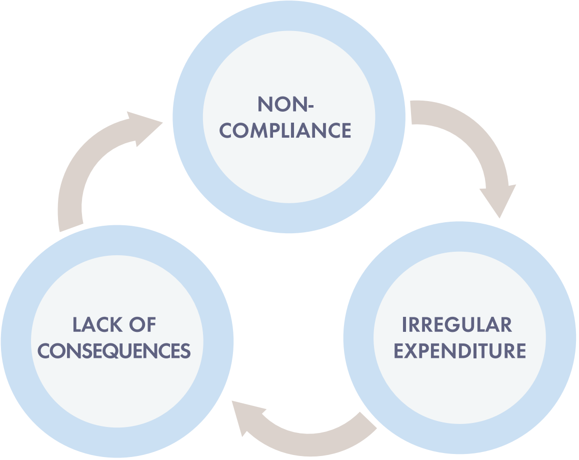
As with the financial statements, we had to point out misstatements in the reports and allowed municipalities to correct these. If we had not done so, 90% of the municipalities would have published performance reports that were not credible.

The poor planning, management and reporting of performance do not bode well for the delivery of services and the achievement of commitments contained in integrated development plans.

We reported material non-compliance with key local government legislation at 86% of the municipalities. This is the highest percentage of non-compliance since 2012-13.

The non-compliance was common in most of the areas for which the municipal manager is accountable – the preparation of financial statements, prevention of unauthorised and fruitless and wasteful expenditure, strategic and performance management as well as management of expenditure, assets, revenue, and human resources.

But the areas with consistently the highest non-compliance were the prevention of irregular expenditure, procurement and contract management, and effecting consequences. These three areas are interrelated: non-compliance with procurement and contract management most often leads to irregular expenditure, while a lack of consequences for the irregular expenditure leads to an environment in which further non-compliance is likely.



Municipalities with material non-compliance findings on procurement and contract management increased from 141 (63%) to 174 (73%).

At 67% of the municipalities, the material findings related to uncompetitive and unfair procurement processes – the most common findings being municipalities not inviting quotations or competitive bids. Often the reasons sighted for these deviations were that it was an emergency or that no other suppliers were available – but the real reasons were either poor planning or a deliberate attempt to favour a specific supplier.

The aim of the Preferential Procurement Regulations is to support socio-economic transformation. The public sector should lead by example in its procurement processes to achieve this goal, but we again found municipalities failing in this area. Countrywide, 38% of the municipalities did not apply – or incorrectly applied – the preference point system, while 57% of the 102 municipalities where we audited local content did not comply with the requirements to procure certain commodities from local producers.

We identified material non-compliance with legislation on **contract management** at 33% of the municipalities – the most common findings being municipalities not monitoring the performance of contractors on a monthly basis and/or inadequate contract performance measures and monitoring.

Although prohibited by legislation, we identified that contracts and quotations worth R15 million were **awarded to suppliers in which employees and councillors have an interest**. Legislation also prohibits awards to any suppliers in which any state official has an interest – we identified such awards worth R2 075 million.

Often this non-compliance was caused by **suppliers falsely declaring** that they have no connection to anyone at the municipality or any other state institution or to their close family members – we identified such false declarations by 1 440 suppliers, while such declarations were not even requested as part of the procurement processes at 82 municipalities.

We were **unable to audit procurement processes of contracts and quotations** worth R1 296 million at 52 municipalities, as the required documentation was missing or incomplete. There was no evidence that these municipalities had followed a fair, transparent and competitive process for all awards. We could not determine whether these awards were irregular and, as a result, could not determine the true extent of irregular expenditure.

The effect of accountability failures on procurement and contract management can be seen in the following examples:

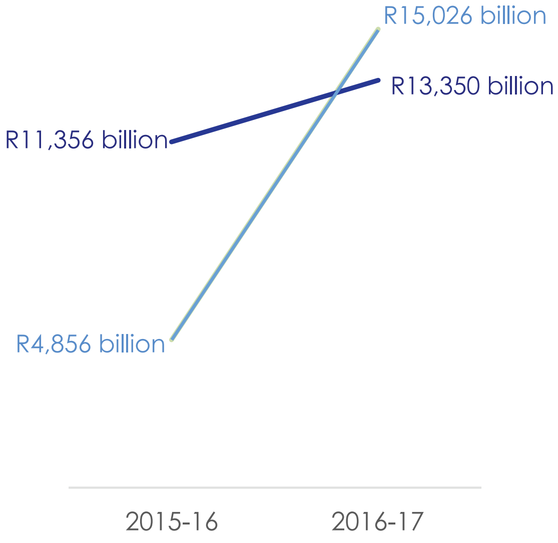
- A common supply chain management transgression was participating in contracts secured by other organs of state (in terms of supply chain management regulation 32) without ensuring that all of the conditions for participation were met. For example, one municipality in the Eastern Cape used a contract secured by another municipality to appoint consultants to assist with financial reporting at a cost of R62 million over three years. The original contract stipulated a contract value of R7 million over 10 months, which the second municipality exceeded by R55 million and 26 months. Thus, this municipality did not comply with the requirements of regulation 32, as it was not participating in an existing contract but rather entered into a new contract with the supplier. Therefore, this contract was irregular and should have gone out on open tender.

- A municipality in North West awarded a tender for information technology services for R2,7 million per month for 36 months. Although the tender was awarded through a tender process, the contract signed with the supplier then included services not covered in the original bid specifications. At year-end, R3,6 million had been paid for services not included in the original tender. Furthermore, no services were rendered for payments of R2,4 million during the year.

We report all our findings on supply chain management compliance and weaknesses to management for follow-up. If there are **indicators of possible fraud or improper conduct in the supply chain management processes**, we recommend that management conduct an investigation. These findings include the false declarations of interest submitted by suppliers (as mentioned above), employees failing to declare their interest in suppliers, payments in spite of poor delivery by suppliers, and payments to possible fictitious suppliers. In 2016-17, we reported these types of findings at 145 municipalities (61%) – a slight improvement from the 148 municipalities (66%) in 2015-16. In total, 105 (71%) of the municipalities that had such findings in 2015-16 again had similar findings in 2016-17.

The irregular expenditure disclosed by municipalities increased by 75% – it is important to understand what this means.

Irregular expenditure increased from R16,212 billion to R28,376 billion (75% increase)



Irregular expenditure incurred in previous years, identified in current year

53% of the irregular expenditure were payments/expenses in previous years only uncovered and disclosed for the first time in 2016-17.

Municipalities made a significant effort in 2016-17 to identify and transparently report on irregularities in previous years – just over R10 billion more than in 2015-16.

Irregular expenditure identified in current year

47% of the irregular expenditure were payments/expenses in 2016-17.

This represents **4%** of the local government expenditure budget. It includes payments made on contracts irregularly awarded in a previous year – if the non-compliance was not investigated and condoned, the payments on these multi-year contracts continue to be viewed and disclosed as irregular expenditure.

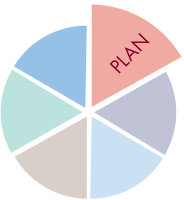
How much of the R28,376 billion then represents **non-compliance in 2016-17?** Based on our analysis of the top 26 contributors, it is estimated to be **16%** (±R4,5 billion).

In other words, 84% of the irregular expenditure relates to non-compliance of prior years that remains unaddressed.

INDICATOR 2: THERE HAS BEEN LITTLE IMPROVEMENT IN THE ACCOUNTABILITY (PLAN+DO+CHECK+ACT) CYCLE

The recommendations we made last year to ensure that the basics are in place and thereby improve audit outcomes and accountability did not receive the necessary attention, as evidenced by the findings from our audits.

PLAN



We recommended: 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.

Findings – audit action plans

The Medium-Term Strategic Framework 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 national Department of Cooperative Governance's back-to basics strategy, which tasks local government with addressing post-audit action plans; and the National Treasury, provincial treasuries and provincial departments responsible for cooperative governance with assessing the capacity of municipalities to develop and implement such plans.

The **status of audit action plans regressed** to only 17% of municipalities having good action plans that addressed the root causes of audit findings and are being implemented. In total, 48% of the municipalities had inadequate audit action plans and 35% had no or very poor action plans.

Findings – performance planning

Although integrated development plans and service delivery and budget implementation plans were developed and adopted, we raised material **findings on the usefulness of performance indicators and targets** in the plans of 46% of the municipalities. This is a regression from the 39% in the previous year.

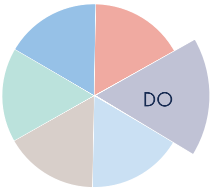
Findings – budgets

Unauthorised expenditure of R12 603 million was incurred at 161 municipalities (67%). Overspending of the budget or main sections within the budget was the reason for R12 540 million (99,5%) of this expenditure, caused by poorly prepared budgets, inadequate budget control, and a lack of monitoring and oversight.

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.

In total, 40% of the overspending that had caused the unauthorised expenditure related to these estimates that had been incorrectly budgeted for at 111 municipalities. 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.

DO

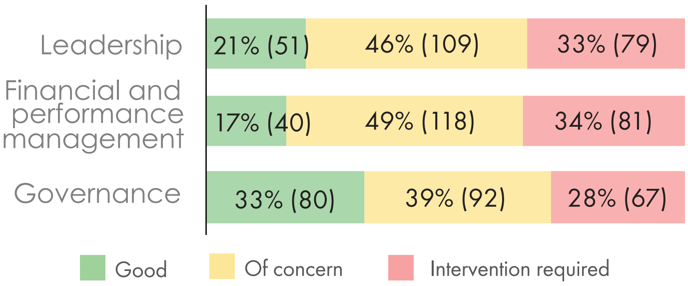


We recommended: Good **internal control** is the key to ensuring that municipalities deliver on their priorities in an effective, efficient and economical manner, produce quality financial statements and performance reports, and comply with applicable legislation – especially in the area of procurement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

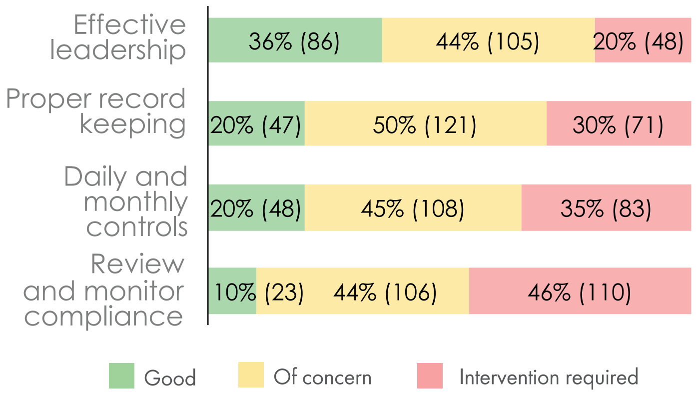
It is the responsibility of municipal managers, senior managers and municipal officials to implement and maintain effective and efficient systems of internal control; hence, it is crucial that the **key positions** of municipal manager, chief financial officer and head of the supply chain management unit are filled with people with the required competencies. Stability in these positions also correlates 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, proper record keeping, daily and monthly disciplines, and the review and monitoring of compliance.

Findings – status of controls

The status of **internal control slightly regressed overall**, caused by slight regressions in the areas of leadership and governance and a regression in the area of financial and performance management.



The **basic controls** we recommended municipalities to focus on also **regressed**.

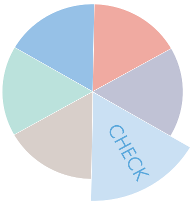


Findings – key positions

The changes in the political leadership after the elections created instability in key positions, as it also did after the 2011 elections. At year-end, **28% of the chief financial officer positions were vacant** (21% for longer than six months) – a slight regression from the 24% at the end of the previous year. **Municipal manager positions were vacant at 27% of the municipalities** (17% for longer than six months) – a regression from the previous year's 20%.

After year-end there were further terminations and resignations, which resulted in a very difficult audit process. The instability in municipal manager positions could become even more evident in 2017-18, as most of these contracts expire in this period.

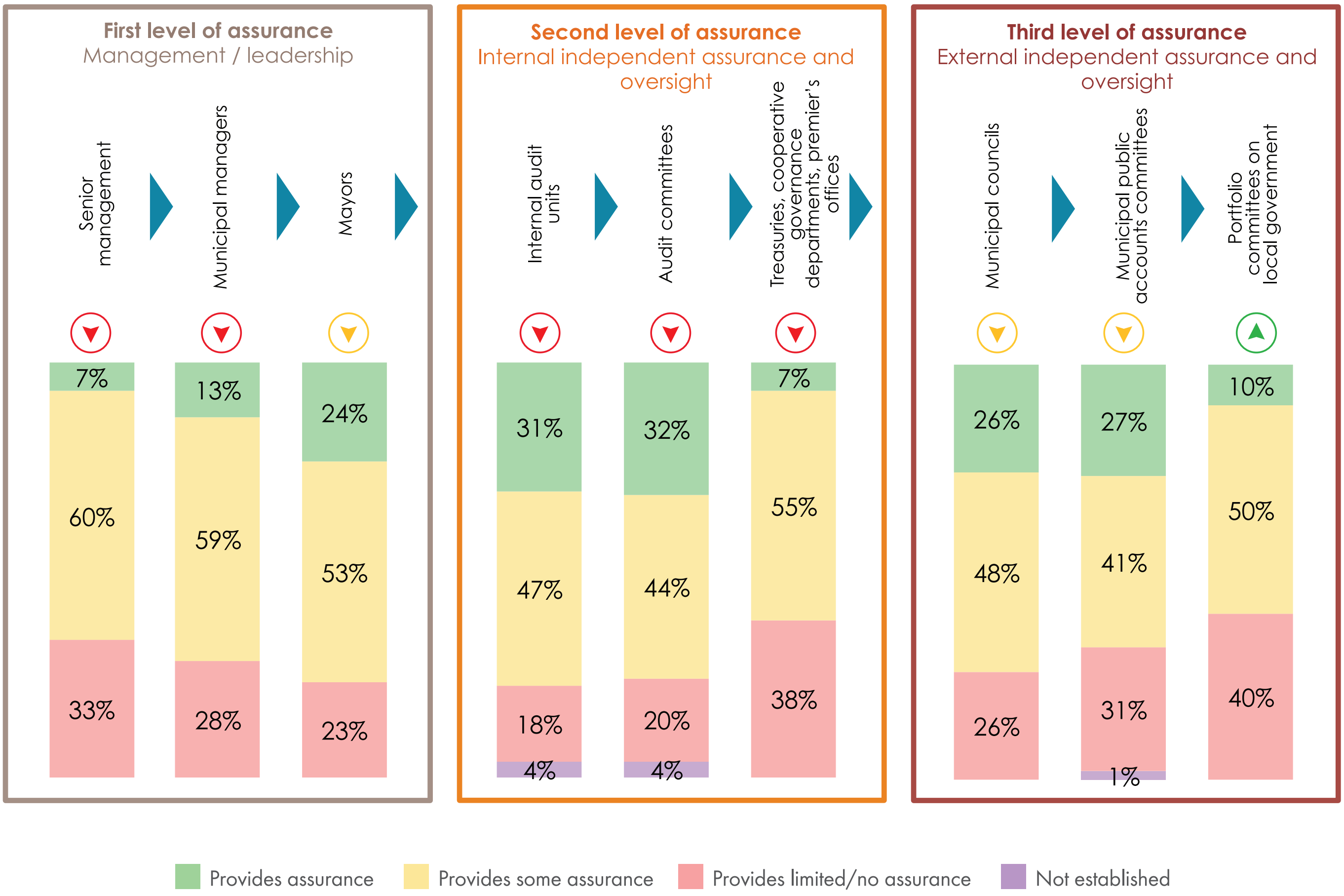
CHECK



We recommended: 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 urged 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.

Findings – assurance provided

The **assurance provided** by the different role players in local government **regressed overall**.



ACT

We recommended: 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 **strict consequences** 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.

Findings – compliance with legislation on implementation of consequences

We reported **non-compliance with the legislation on the implementation of consequences** at 63% of the municipalities – at 132 municipalities (55%), we reported **material non-compliance** with this legislation – a slight increase from the 50% in the previous year.

Findings – reporting and follow-up of allegations of financial and supply chain management misconduct and fraud

Our audits showed that 34% of the municipalities **did not have all the required mechanisms for reporting and investigating transgressions or possible fraud**. This contributed to 60 (70%) of the municipalities having findings on **inadequate follow-up of allegations of financial and supply chain management misconduct and fraud**. The findings included allegations not being investigated (34%) and investigations that took longer than three months (33%).

Findings – supply chain management findings reported for investigation

In 2016-17, municipalities again **did not pay sufficient attention to the findings on supply chain management** compliance and weaknesses with indicators of possible fraud or improper conduct that we reported and recommended for investigation. In 2015-16, we reported such findings at 148 municipalities. Although 43 of the municipalities (29%) investigated all of the findings reported for investigation in the previous year, 70 (47%) investigated none of the findings and 35 (24%) only some of the findings.

Findings – investigation and follow-up of unauthorised, irregular and fruitless and wasteful expenditure

At 133 (61%) 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 – a regression from 113 (52%) in the previous year. A total of 94 of the 113 municipalities (83%) that did not conduct investigations in 2015-16, again did not do so in 2016-17.

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 a result, the year-end balance of irregular expenditure that had accumulated over many years and had not been dealt with totalled R65,32 billion, while that of unauthorised expenditure was R43,5 billion and that of fruitless and wasteful expenditure was R4,24 billion.

INDICATOR 3: INCREASINGLY DIFFICULT ENVIRONMENT FOR AUDITING

The **audit environment became more hostile** with increased contestation of audit findings and pushbacks whereby our audit processes and the motives of our audit teams were questioned. It is acceptable for auditees to question and challenge the outcome of audits based on evidence and solid accounting interpretations or legal grounds. We further acknowledge that many of the accounting and legal matters dealt with in the audits are complex and often open to interpretation. But at some auditees, **pressure is placed on audit teams to change conclusions purely to avoid negative audit outcomes or the disclosure of irregular expenditure** – without sufficient grounds. Often the findings are communicated throughout the audit and even from previous years, but only at the end of the audit when outcomes become apparent does the contestation arise.

Some auditees also used delaying tactics whereby information and evidence were not provided as requested.

This points to a lack of accountability as a problem is not acknowledged and corrected, but rather the messenger (being the auditor) is attacked. **Leadership should set the tone for accountability** – if audit outcomes are not as desired, energy should be directed to addressing the problem and not to coercing the auditors to change their conclusions.

IMPACT OF ACCOUNTABILITY FAILURES

The accountability failures in local government result in municipalities not achieving their objectives, which in turn has a negative impact on the lives of citizens. Our audits highlighted two key areas of impact: the financial health of municipalities and the delivery and maintenance of municipal infrastructure.

EFFECT OF ACCOUNTABILITY FAILURES ON MUNICIPAL FINANCES

Our analysis of financial health shows a continuing weakening in local government finances at a time when municipalities are under increasing pressure to provide services while financial resources are dwindling.

Revenue management

The **inability to collect debt** from municipal consumers was widespread – 92% of the municipalities disclosed that they will need to write off more than 10% of their debt. The average debt-collection period was 187 days.

▼

Deficits

In these circumstances, it is inevitable that municipalities will s**truggle to balance the books**. In 2016-17, 31% of the municipalities disclosed a deficit – the total deficit for these municipalities amounted to R5,6 billion.

▼

Creditor payments and liabilities

The financial woes of local government weighed heavily on municipal creditors. In total, 87% of the municipalities exceeded the 30-day payment period to their creditors – the average payment period was 161 days. In addition, 43% had more liabilities than assets, which means that they will not be able to pay their creditors.

The impact of this **inability to pay creditors** was most evident in the huge sums owed for the provision of electricity and water. Eskom reported arrears of R9,4 billion by March 2017 and implemented power cuts at non-paying municipalities. By September 2017, the water boards were owed arrears of R6,5 billion.

▼

Municipalities in vulnerable position

A combination of various factors, including poor revenue and budget management and the non-payment of creditors, led to 31% of the municipalities disclosing in their financial statements that they **might not be able to continue operating**. Although they have to continue to do so, they were reporting that they were in a particularly vulnerable position at the end of the financial year. These municipalities also incurred fruitless and wasteful expenditure of R1,1 billion in the same period – mostly as a result of penalties and interest on the late or non-payment of creditors such as Eskom.

While the poor economic climate does play a role in the deterioration of financial health, many municipalities are just not managing their finances as well as they should. They do not produce credible financial statements and in-year reports (which are essential for good financial management), their budgets are underfunded, and their expenditure is not controlled within the budget (leading to the R12,5 billion in unauthorised expenditure). Many have poor collection systems, with billing systems and debtor registers (including indigent registers) that are not credible.

Municipalities also lose money, which they can ill afford. Fruitless and wasteful expenditure amounted to R1,5 billion (a 71% increase from the previous year). It is difficult to say how much money is lost through irregular processes, as this needs to be determined through an investigation, but the non-compliance we reported at 78% of the municipalities can potentially lead to a financial loss.

The impact of accountability failures on municipal financial management is felt directly by the communities and businesses the municipalities serve – particularly so when it comes to inadequate access to basic services and the lack of economic development. It also puts pressure on the country's finances overall, as national and provincial government have to contribute through grants to keep the municipalities functioning.

RESULT OF ACCOUNTABILITY FAILURES ON MUNICIPAL INFRASTRUCTURE

Municipalities are responsible for developing and maintaining infrastructure to ensure that municipal services are delivered. Funding of infrastructure projects is a challenge for most municipalities and as such they receive infrastructure grants from national government for this purpose.

Our audits again identified a number of shortcomings in the development and maintenance of infrastructure. These are symptoms of the larger problem that local government has with managing finances, performance and projects and with taking accountability for outcomes.

Municipal infrastructure grant	R902 million (6%) **was not spent** – 22% of the municipalities underspent by more than 10%.	At 38% of the 518 projects we audited, the **targets for the project were not achieved** or not evaluated, and at 14% the achievement was not reliable.	We identified **supply chain management non-compliance** on 27% of the projects.
Road infrastructure	55% of the municipalities responsible for road infrastructure **did not have a maintenance plan or priority list** for renewal and routine maintenance.	27% of the municipalities **did not do conditional assessments** of all their roads.	26% of the municipalities responsible for road projects **exceeded their planned completion dates**.
Water infrastructure development projects	At 27% of the municipalities, funding for the projects **was not spent** – 17% by more than 10%.	We identified **supply chain management non-compliance** at 21% of the municipalities.	26% of the municipalities responsible for water infrastructure projects **exceeded their planned completion dates**.
Maintenance of water infrastructure	46% of the municipalities responsible for the delivery of water **did not have a maintenance plan** for their infrastructure and 22% **did not budget for maintenance**. 35% **did not do any conditional assessments** of their infrastructure to inform their plans and budget.	The **targets and time frames for routine maintenance of infrastructure were not achieved at** 24%.	41% had **water losses of more than 30%**.

The effect of accountability failures on municipal infrastructure can be seen in the following examples:

- Themba water purification plant (City of Tshwane Metro) – The project was delayed due to the late or non-payment of contractors, contributing to non-compliance on expenditure management and interest being incurred on late payments. The reasons for non-achievement on the project were inadequate project management of key milestones; lack of planning before appointing the contractor, resulting in overspending on the project; and inadequate monitoring of the contractor.

- Construction of Thabong T16 waterborne sanitation (Matjhabeng) – The project started in 2014-15 at a budgeted amount of R62 million. The municipality prioritised the construction of the toilet structures, plumbing and internal sewers ahead of the bulk network at the pump station, while the sewer pipeline was also not connected to the pump station. This resulted in sewage overflow around the area of construction, which caused pollution and which could potentially compromise the health and safety of the Thabong residents. The appointment of the contractors was irregular and the project was still in progress. To date, R54 million had been spent on this contract.

Additional examples are included in the provincial overviews in section 5.

Although funding and support are generally available from national government for the development and maintenance of municipal infrastructure, the non-delivery thereof at some municipalities and the impact on communities are the issues that need the most focused attention by all role players to ensure that the objectives of a better life for all are achieved.

ROOT CAUSES OF ACCOUNTABILITY FAILURES

Our message on the root causes of poor audit outcomes has remained consistent over the years, but we saw a regression in the rate that municipalities are addressing these three root causes.

Slow response in improving internal controls and addressing risk areas	Inadequate consequences for poor performance and transgressions	Instability or vacancies in key positions or key officials lacking appropriate competencies
77% ▼	61% ▼	59% ▼

The root causes in 2016-17 can be expanded as follows:

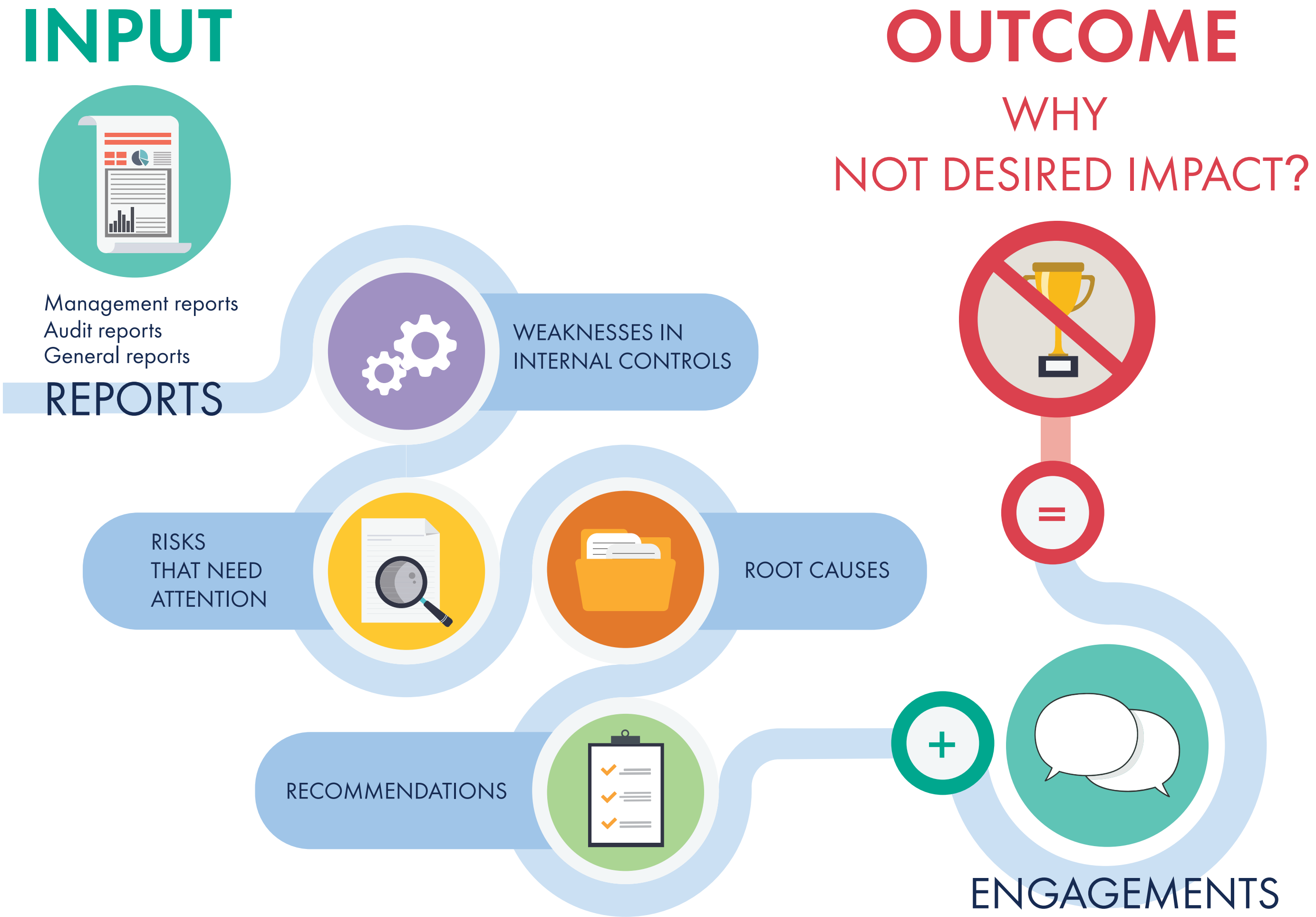
- **Vacancies and instability in key positions** slowed down systematic and disciplined improvements.
- **Inadequate skills led to a lack of oversight** by councils (including the mayor) and insufficient implementation and maintenance of financial and performance management systems by the administration.
- **Political infighting** at council level and **interference** in the administration weakened oversight and the implementation of consequences for transgressions, and made local government less attractive for professionals to join.
- Leadership's inaction, or inconsistent action, created a culture of '**no consequences**', often due to inadequate performance systems and processes.
- At some municipalities there was a **blatant disregard** for controls (including good record keeping) and compliance with key legislation, as it enabled an environment in which it would be easy to commit fraud.
- Leadership did not take our **repeated recommendations** and warnings of risks for which they needed to prepare seriously.
- Municipalities focused on obtaining **unqualified financial statements** at a great cost by using consultants and auditors, which was to the detriment of credible performance reporting and compliance with key legislation.
- Provincial and national role players **did not sufficiently support** municipalities.

These issues are mostly behavioural in nature and can be addressed through strong, ethical leadership at the political and administrative level.

OUR ROLE IN THE ACCOUNTABILITY CHAIN

Our role as auditors is to report to oversight structures on the credibility of the financial statements and performance reports and on whether the municipality complied with key legislation. It is the role of these oversight structures (the council and its committees) to use our audit report to determine whether they can rely on the financial statements and performance reports for oversight and decision-making purposes and to call the administration to account for matters we report in the audit report.

But as public sector auditors with a keen interest in seeing local government succeed, we have always done more than just report.



Through our management, audit and general reports, we have been **reporting the weaknesses in internal controls** and the **risks that need attention** in local government. We have consistently highlighted the need to address the following:

- Quality of financial statements and performance reports submitted for auditing
- Compliance with legislation, supply chain management and irregular expenditure
- Vacancies and instability
- Lack of consequences
- Internal controls

In our reports, we provide **root causes** of audit findings and **recommendations** to address the root causes. We ensure that our messages are heard through **engagements** with senior officials, municipal managers, mayors, municipal public accounts committees, and councils. We will continue with adding value through these practices, but they have not had the desired impact yet – as evidenced in the poor and stagnated audit outcomes.

Hence we are increasing our efforts through extending our engagements with municipal managers to a **status of records review**, which we have been implementing in a phased approach. Such a review is an assessment of records, risks and progress made by the municipality to address prior year issues early in the financial year. This provides an early warning system whereby municipal managers can be alerted to matters that can potentially lead to undesirable audit outcomes. Where it has been implemented in 2016-17, the general response from municipal managers was positive but the results of the engagements were mixed: some municipalities did not respond to the issues we had raised, but where there were stability in leadership and the capacity and competence to respond appropriately, it assisted in improving outcomes or maintaining good audit outcomes.

All of these measures are aimed at assisting the municipal leadership and the council to prevent accountability failures, or to provide them with information on how to deal with such failures where they have occurred. The accountability mechanisms in local government are not working as they should and there have been continued calls for more to be done – particularly by us as the Auditor-General of South Africa. Through the support of our parliamentary oversight committee, we are thus busy **amending the Public Audit Act** to provide us with more power to ensure accountability in the public sector.

The intent of the amendments is not to take over the functions of the municipal manager, the mayor or the council, as their accountability responsibilities are clear in municipal legislation. It is rather to step in where those **responsibilities are not fulfilled** in spite of us alerting leadership of material irregularities that need to be investigated and dealt with.

The amendments, if approved, will provide us with the **power to refer** material irregularities to appropriate authorities to investigate as well as with a level of **remedial power**, including the recovery of money lost as a result of the irregularities. Material irregularities will include any non-compliance with legislation, fraud or theft, or a breach of fiduciary duty that caused or is likely to cause a material financial loss, the misuse or loss of a material public resource, or substantial harm to a public sector institution or the general public.

If we had those powers today already, there would have been a number of cases in local government that would have been referred. This would have been done on the basis of these cases being seen as material irregularities that we had reported to municipal management and the council to deal with, without any success.

If the Public Audit Act had already been amended, these are a few examples of material irregularities identified in 2016-17 that would have been referred:

- We identified various irregularities in the contracting of a consultant in 2015-16 to assist with financial reporting at a municipal entity at a cost of R3,8 million. These included the absence of a signed service level agreement, regular contract extensions, excessive rates per hour, and a lack of monitoring of the work performed by the consultant. Despite us reporting to the board that this contract was potentially fraudulent, the board did not take any action to investigate the matters raised.
- A district municipality incurred R164 million in fruitless and wasteful expenditure relating to a water project initially done by the municipality. Due to substandard work, the Department of Water Affairs had to redo the project from the start. The municipal leadership did not act in the best interest of the municipality, which not only resulted in substantial financial losses but also in service delivery delays.
- A municipality had obtained a disclaimed audit opinion with material findings on performance reporting and compliance with legislation for the past three years. During this period, there was instability in the municipal manager's position, with this position being filled for only two months in the 2016-17 year. As a result, incorrect and misleading information was provided to us, without any consequences.
- Irregular expenditure was common at a municipality, but none of the reported instances were investigated. The municipal manager did not afford the council the opportunity to decide on investigations by deliberately not providing the details. The provincial treasury tried to assist but also hit a stumbling block due to missing information. As a result, it cannot be determined if there are losses that should be recovered.

The extension of our mandate to deal with these types of irregularities will assist in restoring public confidence, solidifying accountability, and entrenching the ethical behaviour that is expected of entrusted officials and elected representatives. It will also mean that our reports will be taken seriously – we could start to see an improvement in the audit outcomes and a definite shift towards municipalities living up to the expectations of the communities they serve.

The information provided in section 4 is meant to expand on the issues raised above. Nothing more needs to be said about the seriousness of the accountability failures in local government. It is now up to the leadership and administration to act decisively on our recommendations, to ultimately ensure a better life for the citizens of South Africa.

SECTION 4

Summary of audit outcomes

4 SUMMARY OF AUDIT OUTCOMES

Overall regression in audit outcomes

OVERALL AUDIT OUTCOMES

							TOTAL
2015-16	48	108	60	4	21	0	241
2016-17	33	112	66	4	24	18	257

LOCAL GOVERNMENT EXPENDITURE BUDGET

2016-17 *R362 billion*	7%	68%	17%	1%	5%	2%

MOVEMENT

16 ∧ *Improved* **45** ∨ *Regressed*

CLEAN AUDIT MOVEMENTS

30 > *Remained clean*
17 ∨ *Regressed*
3 ∧ *New clean audits*
1 *Outstanding*

OUTSTANDING AUDITS

Cut-off date for inclusion of the audit outcomes in this report is **15 January 2018**

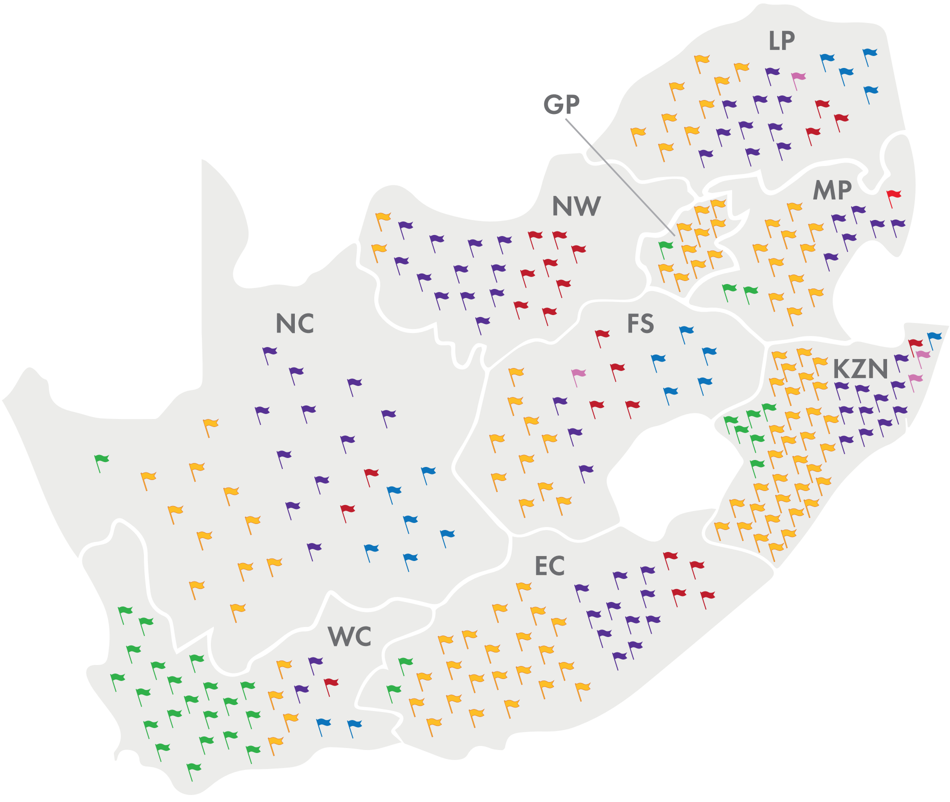
REASONS FOR **18** *OUTSTANDING AUDITS*

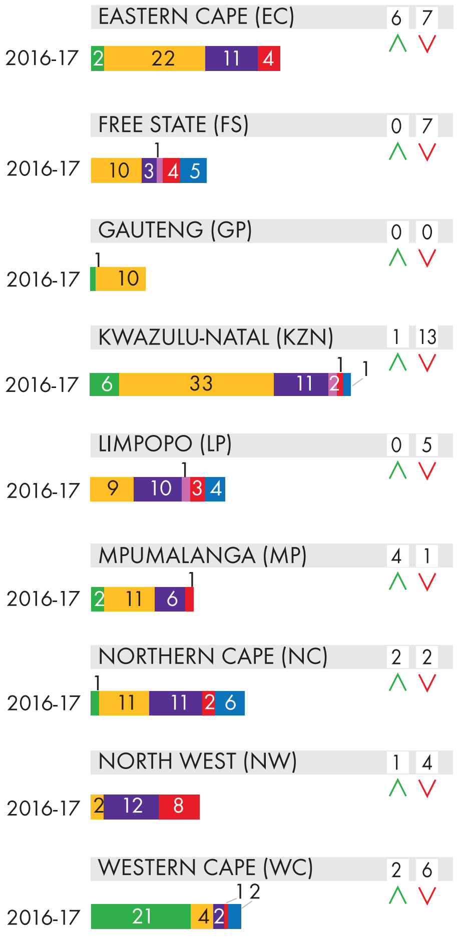
Financial statements not submitted - **2 (11%)**
Financial statements submitted late - **15 (83%)**
Delay in the audit - **1 (6%)**

RESULTS OF 11 AUDITS SUBSEQUENTLY FINALISED BEFORE DATE OF THIS REPORT

2 ∧ *Improved* **5** ∨ *Regressed*

PROVINCIAL AUDIT OUTCOMES AND MOVEMENTS





🟩 Unqualified with no findings
🟨 Unqualified with findings
🟪 Qualified with findings
■ Adverse with findings
🟥 Disclaimed with findings
🟦 Outstanding audits

FINANCIAL STATEMENTS

▼ REGRESSION IN QUALITY OF FINANCIAL STATEMENTS

TARGET	MOVEMENT	2016-17	2015-16
Timely submission of financial statements	▲	97% (231)	96% (217)
Quality of financial statements submitted for auditing	▼	22% (53)	34% (76)
Quality of published financial statements	▼	61% (145)	68% (153)

92 municipalities (39%) *achieved unqualified audit opinions only because they* ***corrected all misstatements*** *identified during the audit*

QUALIFICATION AREAS
(on audited financial statements)

	MOVEMENT	2016-17	2015-16
Property, infrastructure, plant and equipment	▼	27% (64)	20% (44)
Receivables	▼	24% (57)	15% (34)
Revenue	▼	23% (55)	18% (40)
Irregular expenditure	▼	23% (54)	22% (49)

AUDIT OPINIONS VS MEDIUM-TERM STRATEGIC FRAMEWORK (MTSF) TARGETS FOR 2019

AUDIT OPINIONS		MTSF TARGETS	ACHIEVED?
Financially unqualified	61% (145)	65% or more	X
Qualified	27% (66)	Less than 20%	X
Adverse and disclaimed	12% (28)	Less than 15%	✓

PROVINCIAL VIEW

PROVINCE	TIMELY SUBMISSION OF FINANCIAL STATEMENTS		QUALITY OF FINANCIAL STATEMENTS SUBMITTED FOR AUDITING		QUALITY OF PUBLISHED FINANCIAL STATEMENTS	
	Number	Movement from 2015-16	Number	Movement from 2015-16	Number	Movement from 2015-16
Eastern Cape	38 (97%)	▼	4 (10%)	▼	24 (62%)	▼
Free State	16 (89%)	▲	1 (6%)	▼	10 (56%)	▼
Gauteng	11 (100%)	►	4 (36%)	▼	11 (100%)	►
KwaZulu-Natal	53 (100%)	►	15 (28%)	▼	39 (74%)	▼
Limpopo	20 (87%)	▼	0 (0%)	►	9 (39%)	▼
Mpumalanga	20 (100%)	▲	4 (20%)	▼	13 (65%)	▲
Northern Cape	24 (96%)	▲	1 (4%)	▼	12 (48%)	▲
North West	22 (100%)	►	0 (0%)	►	2 (9%)	▼
Western Cape	27 (96%)	▼	24 (86%)	▼	25 (89%)	▼
Total	231 (97%)	▲	53 (22%)	▼	145 (61%)	▼

PERFORMANCE REPORTS

▼ REGRESSION IN QUALITY OF PERFORMANCE REPORTS

TARGET	MOVEMENT	2016-17	2015-16
Performance reports prepared	▲	98% (235)	97% (219)
Quality of performance reports submitted for auditing	▼	10% (23)	19% (41)
Quality of published performance reports	▼	38% (89)	50% (109)

66 municipalities (28%) *had no material findings only because they* **corrected all misstatements** *identified during the audit*

FINDINGS ON PERFORMANCE REPORTS

FINDINGS ON PERFORMANCE REPORTS	MOVEMENT	2016-17	2015-16
Performance indicators and targets not useful	▼	46% (108)	39% (86)
Achievement reported not reliable	▼	51% (120)	45% (99)
No underlying records or planning documents	—	4% (10)	*New focus area*

MOST COMMON USEFULNESS FINDINGS

28% Not well defined **20%** Not consistent **17%** Not verifiable **16%** Not measurable **14%** Not specific

PROVINCIAL VIEW

PROVINCE	PERFORMANCE REPORTS PREPARED		QUALITY OF PERFORMANCE REPORTS SUBMITTED FOR AUDITING		QUALITY OF PUBLISHED PERFORMANCE REPORTS	
	Number	Movement from 2015-16	Number	Movement from 2015-16	Number	Movement from 2015-16
Eastern Cape	39 (100%)	►	2 (5%)	▼	12 (31%)	▼
Free State	18 (100%)	►	0 (0%)	▼	3 (17%)	▼
Gauteng	11 (100%)	►	1 (9%)	▼	4 (36%)	▼
KwaZulu-Natal	53 (100%)	►	7 (13%)	▼	25 (47%)	▼
Limpopo	23 (100%)	►	1 (4%)	▲	3 (13%)	▼
Mpumalanga	20 (100%)	►	2 (10%)	▼	8 (40%)	▲
Northern Cape	22 (88%)	▲	0 (0%)	▼	6 (27%)	▲
North West	21 (95%)	▼	0 (0%)	▼	2 (9%)	▼
Western Cape	28 (100%)	▲	10 (36%)	▼	26 (93%)	▼
Total	235 (98%)	▲	23 (10%)	▼	89 (38%)	▼

COMPLIANCE WITH KEY LEGISLATION

▼ Increase in non-compliance from **79% (177)** to **86% (206)**

MOST COMMON NON-COMPLIANCE AREAS	MOVEMENT	2016-17	2015-16
Quality of financial statements	▼	78% (186)	66% (149)
Management of procurement and contract management	▼	73% (175)	62% (140)
Prevention of unauthorised, irregular and fruitless and wasteful expenditure	►	72% (171)	72% (161)
Effecting consequences	▼	56% (134)	50% (112)

Non-compliance by **78% (186)** *of municipalities* **can potentially lead to a financial loss**

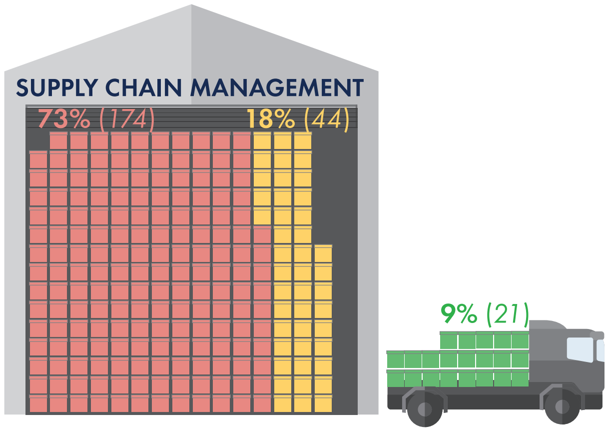
OTHER NOTABLE NON-COMPLIANCE AREAS	2016-17	MOVEMENT	MOST COMMON FINDINGS PER AREA
Expenditure management	55% (132)	▼	*Creditors not paid within 30 days - 51% (121)*
Asset management	39% (94)	▼	*Ineffective system of internal control for assets - 32% (77)*
Strategic planning and performance management	36% (86)	▲	*No performance management system established or adopted - 10% (24)*
Human resource management	33% (79)	▼	*No policies/procedures to measure/evaluate staff performance - 23% (54)*
Revenue management	30% (71)	▼	*Revenue due not recorded - 23% (56)*

PROVINCIAL VIEW

PROVINCE	MUNICIPALITIES WITH NO FINDINGS ON COMPLIANCE	
	Number	Movement from 2015-16
Eastern Cape	2 (5%)	▼
Free State	0 (0%)	▼
Gauteng	1 (9%)	▼
KwaZulu-Natal	6 (11%)	▼
Limpopo	0 (0%)	►
Mpumalanga	2 (10%)	▼
Northern Cape	1 (4%)	▼
North West	0 (0%)	►
Western Cape	21 (75%)	▼
Total	33 (14%)	▼

SUPPLY CHAIN MANAGEMENT (SCM)

▼ More municipalities complied with SCM legislation, but increase in material non-compliance findings from 63% (141) to 73% (174) led to overall regression



▼ Not able to audit procurement of **R1 296 million** due to **missing or incomplete information** at 52 municipalities (22%)

Most common in:
- Gauteng (R830 million)
- North West (R155 million)
- Mpumalanga (R106 million)

🟩 With no findings 🟨 With findings 🟥 With material findings

AWARDS TO EMPLOYEES, COUNCILLORS, CLOSE FAMILY MEMBERS AND OTHER STATE OFFICIALS

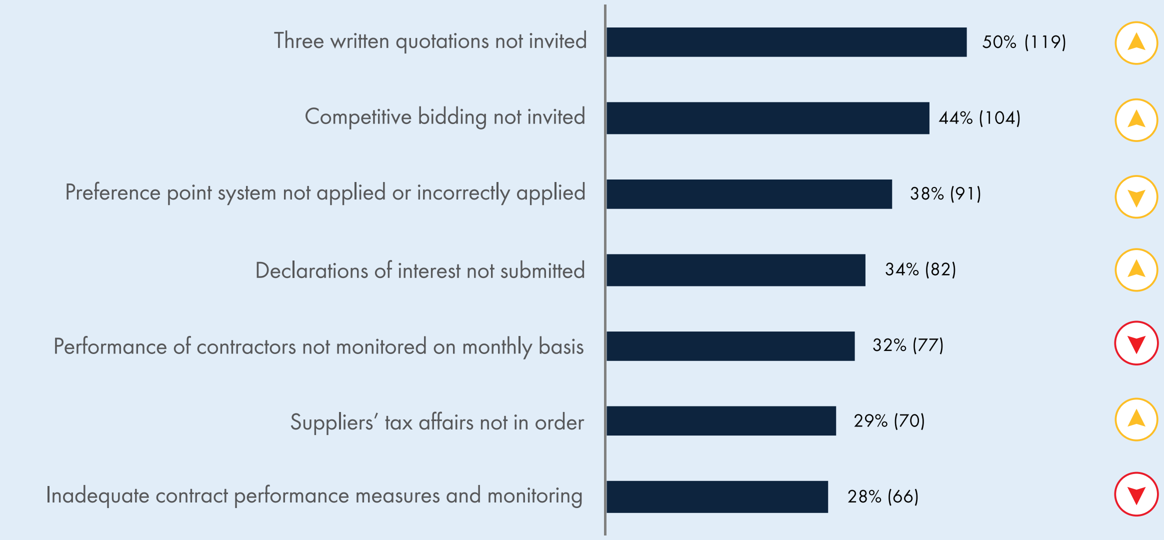
FINDINGS	MOVEMENT	NUMBER OF MUNICIPALITIES WITH AWARDS	AMOUNT (R MILLION)
Prohibited awards to other state officials	▼	64% (153)	R2 075
Prohibited awards to employees and councillors	▲	21% (49)	R15
At 22 municipalities, awards valued at **R7,92 million** were made to councillors, with the values ranging from **R4 200** to **R4,07 million** per councillor			
Awards to close family members of employees	▼	41% (99)	R320
At 26 municipalities (11%), awards to close family members were not disclosed in the financial statements as required			

UNCOMPETITIVE OR UNFAIR PROCUREMENT PROCESSES AND CONTRACT MANAGEMENT

Findings on **uncompetitive and unfair procurement processes** at **81%** of the municipalities, of which 67% was material non-compliance

Findings on **contract management** at **44%** of the municipalities, of which 33% was material non-compliance

Most common findings were the following:



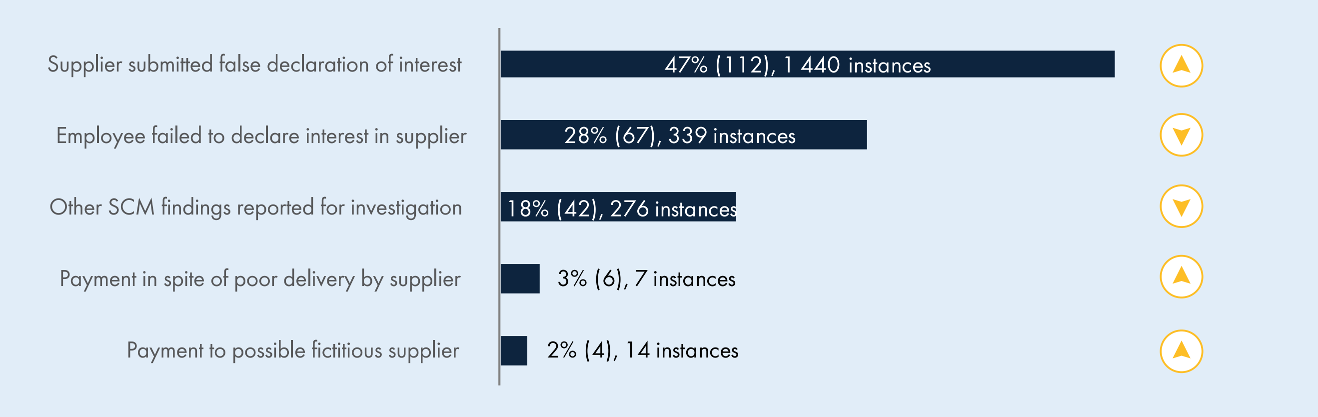
LOCAL PROCUREMENT

Municipalities are required to procure certain commodities from local producers; **58 municipalities** (57%) out of 102 where we audited local procurement failed to comply with regulation on promotion of local producers on awards amounting to **R587 million**

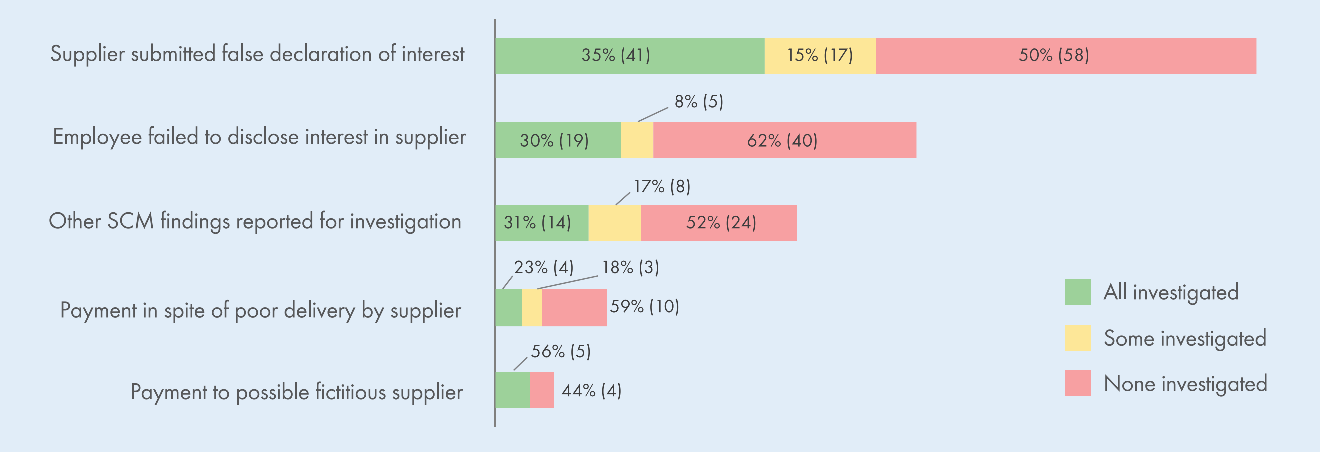
FALSE DECLARATIONS BY SUPPLIERS AND NON-DISCLOSURE BY EMPLOYEES

FINDINGS	MOVEMENT	NUMBER OF MUNICIPALITIES	NUMBER OF SUPPLIERS/EMPLOYEES	AMOUNT (R MILLION)
Suppliers owned or managed by **employees of another state institution** made false declarations	▲	41% (98)	1 232	R1 495
Suppliers owned or managed by **employees and councillors of the municipality** made false declarations	▼	8% (18)	49	R2
Suppliers owned or managed by **close family members of employees** of the municipality made false declarations	▲	10% (23)	173	R24
Employees of the municipality **failed to declare their own interest** either as part of the procurement processes or through annual declarations	▼	12% (29)	77	R9
Employees of the municipality **failed to declare their family members' interest**	▼	19% (46)	254	R88

FINDINGS REPORTED FOR INVESTIGATION DURING THE AUDIT PROCESS IN CURRENT YEAR



FOLLOW-UP OF PREVIOUS YEAR'S SUPPLY CHAIN MANAGEMENT FINDINGS REPORTED FOR INVESTIGATION IN PRIOR YEAR



UNAUTHORISED, IRREGULAR AND FRUITLESS AND WASTEFUL EXPENDITURE (UIFW)

	IRREGULAR *Non-compliance with legislation in process leading to expenditure*	UNAUTHORISED *Expenditure more than budget or not in accordance with grant or budget conditions*	FRUITLESS AND WASTEFUL *Expenditure made in vain – could have been avoided if reasonable care was taken*
How much was disclosed in 2016-17?	**R28,376 billion at 215 municipalities (90%)** 75% increase from R16,212 billion in 2015-16 ▼	**R12,603 billion at 161 municipalities (67%)** 9% decrease from R13,814 billion in 2015-16 ▲	**R1,526 billion at 204 municipalities (85%)** 71% increase from R890 million in 2015-16 ▼
Is all of it 2016-17 expenditure?	**No** R15,026 billion (53%) was expenditure in previous years only uncovered and disclosed in 2016-17 R13,35 billion (47%) was expenses in 2016-17, which included payments on ongoing contracts irregularly awarded in a previous year Based on analysis of top 26 contributors, **16% (± R4,5 billion) represented non-compliance in 2016-17**	**Yes**	**No** R280 million (18%) was expenditure in previous years only uncovered and disclosed in 2016-17 **R1,246 billion (82%) was expenses in 2016-17**
How much of the 2016-17 local government budget does it represent?	4%	4%	< 1%
Is this the total amount?	**No** 80 municipalities (33%) did not know total amount and were still investigating to determine full amount 53 municipalities (22%) were qualified on the **completeness** of their disclosure We could also not audit procurement processes valued at R1,296 billion due to missing or incomplete documentation – it is not known whether any part of this amount might represent irregular expenditure	**No** 17 municipalities (7%) were qualified on the **completeness** of their disclosure	**No** 8 municipalities (3%) were qualified on the **completeness** of their disclosure

	IRREGULAR	UNAUTHORISED	FRUITLESS AND WASTEFUL
What was main cause?	**Non-compliance with supply chain management legislation (99%), related to:** • Procurement without following a competitive bidding or quotation process – R8,322 billion (30%) • Non-compliance with procurement process requirements – R18,092 billion (64%) • Inadequate contract management – R1,738 billion (6%)	**Overspending of budget (99,5%)** Of the R12,54 billion overspent, R5,055 billion (40%) related to actual payments in excess of the budget R7,485 billion (60%) related to non-cash items, representing the poor estimation of, for example, asset impairments	**Penalties and interest on overdue accounts and late payments (74%)** – mostly as a result of municipalities' poor financial health
Did the municipalities detect this expenditure?	**79% identified by municipality and remainder by audit process** Many municipalities implemented processes to fully uncover irregularities of previous years – partly to address prior year qualifications on irregular expenditure (R7,476 billion) but also to correct past irregularities	**79% identified by municipality and remainder by audit process**	**93% identified by municipality and remainder by audit process**
Does it mean this money was wasted?	**Possibly – it can only be determined through a council investigation** Goods and services were received for R23,265 billion (83%) of the expenditure related to supply chain management, but were not received for R12 million (< 1%), while we did not audit the remaining 17% We cannot confirm if value for money was received for all of these goods and services	**No**	**Yes**

PROVINCIAL VIEW

	Irregular (R billion)	Unauthorised (R billion)	Fruitless and wasteful (R billion)
Eastern Cape	R13,558 48% of total 35% of provincial local government budget	R1,446 12% of total 4% of provincial local government budget	R0,179 12% of total < 1% of provincial local government budget
North West	R4,294 15% of total 22% of provincial local government budget	R1,185 9% of total 6% of provincial local government budget	R0,192 13% of total 1% of provincial local government budget
Gauteng	R3,653 13% of total 3% of provincial local government budget	R2,009 16% of total 2% of provincial local government budget	R0,204 13% of total < 1% of provincial local government budget
KwaZulu-Natal	R2,449 9% of total 4% of provincial local government budget	R1,545 12% of total 2% of provincial local government budget	R0,051 3% of total < 1% of provincial local government budget
Mpumalanga	R1,996 7% of total 10% of provincial local government budget	R1,334 11% of total 7% of provincial local government budget	R0,273 18% of total 1% of provincial local government budget
Limpopo	R1,317 5% of total 7% of provincial local government budget	R1,068 8% of total 6% of provincial local government budget	R0,243 16% of total 1% of provincial local government budget
Free State	R0,675 2% of total 5% of provincial local government budget	R2,899 23% of total 21% of provincial local government budget	R0,325 21% of total 2% of provincial local government budget
Northern Cape	R0,261 1% of total 4% of provincial local government budget	R1,034 8% of total 16% of provincial local government budget	R0,055 4% of total 1% of provincial local government budget
Western Cape	R0,173 < 1% of total < 1% of provincial local government budget	R0,083 1% of total < 1% of provincial local government budget	R0,004 < 1% of total < 1% of provincial local government budget

Expenditure of 5% or higher of the provincial local government budget is highlighted in red

TOP 10 CONTRIBUTORS – UNAUTHORISED EXPENDITURE

All of these municipalities have incurred unauthorised expenditure for the past 3 years, except Msunduzi and Enoch Mgijima

MUNICIPALITY	DISCLOSED (R BILLION)	NATURE
Matjhabeng (FS)	R1,031	Overspending of budget R0,474 million (46%) related to non-cash items
Mangaung Metro (FS)	R0,722	Overspending of budget R0,671 million (93%) related to non-cash items
City of Tshwane Metro (GP)	R0,62	Overspending of budget R0,168 million (27%) related to non-cash items
Emfuleni (GP)	R0,595	Overspending of budget R0,217 million (36%) related to non-cash items
City of Johannesburg Metro (GP)	R0,502	Overspending of budget R0,113 billion (22%) related to non-cash items
Nelson Mandela Bay Metro (EC)	R0,432	Overspending of budget R0,432 billion (100%) related to non-cash items
Msunduzi (KZN)	R0,4	Overspending of budget R0,336 billion (84%) related to non-cash items
Vhembe District (LP)	R0,375	Overspending of budget R0,249 billion (66%) related to non-cash items
Gamagara (NC)	R0,374	Overspending of budget R0,364 billion (97%) related to non-cash items
Enoch Mgijima (EC)	R0,323	Overspending of budget R0,323 billion (100%) related to non-cash items
Total for top 10	R5,374	This constitutes 43% of the total unauthorised expenditure R3,347 billion (62%) of top 10 value related to non-cash items

TOP 10 CONTRIBUTORS – IRREGULAR EXPENDITURE

All of these municipalities have incurred irregular expenditure for the past 3 years

Municipality	Disclosed (R billion)	Incurred in 2016-17 (R billion)	Main non-compliance	Key projects affected	Grants affected* (R billion)
Nelson Mandela Bay Metro (EC)	R8,184	R0,045 (0,5%)	99% related to non-compliance with procurement process requirements	Water infrastructure, road infrastructure, and housing	R1,318 (USDG)
OR Tambo District (EC)	R3,082	R0,680 (22%), of which R0,097 (14%) represents non-compliance in 2016-17	99% related to procurement without following competitive bidding or quotation processes	Water infrastructure	R0,713 (MIG/RBIG)
City of Tshwane Metro (GP)	R1,825	R1,211 (66%), of which R0,231 (19%) represents non-compliance in 2016-17	83% related to procurement without following competitive bidding or quotation processes	Smart prepaid contract (R0,699 billion), Wi-Fi contract (R0,079 billion), and fleet management contract (R0,130 billion)	N/A
Rustenburg (NW)	R0,984	R0,540 (55%) The portion that represents non-compliance in 2016-17 could not be determined due to poor document management at municipality	100% related to non-compliance with procurement process requirements	Rustenburg rapid transport (various sub-contracts)	R0,145 (PTNG)
Ngaka Modiri Molema District (NW)	R0,828	R0,164 (20%) The portion that represents non-compliance in 2016-17 could not be determined due to poor document management at municipality	80% related to procurement without following competitive bidding or quotation processes	Water infrastructure and sanitation	R0,015 (MIG)

Municipality	Disclosed (R billion)	Incurred in 2016-17 (R billion)	Main non-compliance	Key projects affected	Grants affected* (R billion)
City of Johannesburg Metro (GP)	R0,706	R0,706 (100%), of which R0,393 (56%) represents non-compliance in 2016-17	100% related to non-compliance with legislation on contracts	ICT - SAP upgrade	N/A
City of Ekurhuleni Metro (GP)	R0,591	R0,367 (62%)	59% related to non-compliance with procurement process requirements	Refuse removal, housing infrastructure (e.g. housing, dwelling and lifts projects), chemical toilets (i.e. sanitation), and road infrastructure	R0,420 (PTNG)
Buffalo City Metro (EC)	R0,584	R0,287 (49%), none of which represents non-compliance in 2016-17	77% related to non-compliance with procurement process requirements	Multi-year contract for road infrastructure	R0,532 (USDG)
Madibeng (NW)	R0,562	R0,562 (100%), of which R0,504 (90%) represents non-compliance in 2016-17	80% related to non-compliance with procurement process requirements	Water infrastructure and sanitation	R0,051 (MIG)
Moretele (NW)	R0,557	R0,139 (25%) The portion that represents non-compliance in 2016-17 could not be determined due to poor document management at municipality	100% related to non-compliance with procurement process requirements	Water infrastructure and sanitation	R0,019 (MIG)
Total for top 10	R17,903	This constitutes 63% of the total irregular expenditure disclosed in 2016-17 R11,265 billion (63%) of top 10 value resulted from non-compliance with procurement process requirements, while R5,617 billion (31%) related to procurement without following competitive bidding or quotation processes			

*MIG: municipal infrastructure grant
PTNG: public transport network grant
RBIG: regional bulk infrastructure grant
USDG: urban settlement development grant

TOP 10 CONTRIBUTORS – FRUITLESS AND WASTEFUL EXPENDITURE

All of these municipalities have incurred fruitless and wasteful expenditure for the past 3 years, except Rand West City (new municipality)

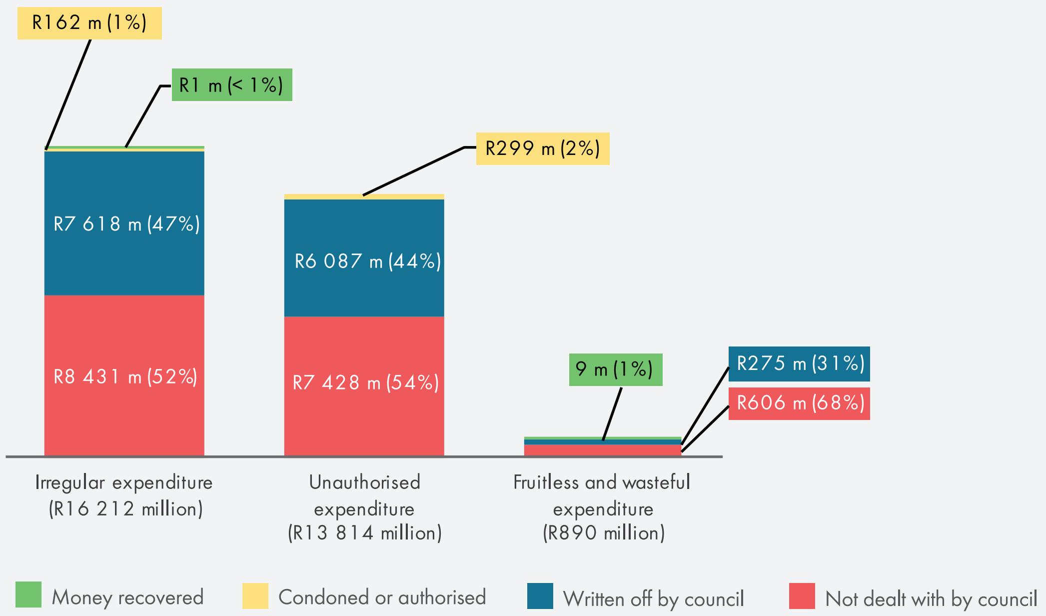
MUNICIPALITY	DISCLOSED (R BILLION)	NATURE
Matjhabeng (FS)	R0,187	Eskom interest of R0,182 billion; remainder relating to penalties and interest – Sars and other creditors
Mopani District (LP)	R0,164	Payment for work that had to be redone due to poor quality
Nelson Mandela Bay Metro (EC)	R0,11	Mostly payments to rectify faulty work and for damages awarded in court
Emalahleni (MP)	R0,079	Eskom interest of R0,078 billion
Emfuleni (GP)	R0,06	Penalties and interest on late payment of accounts
Rand West City (GP)	R0,055	Mostly related to interest: Eskom – R0,02 billion, Sars – R0,01 billion, and Rand Water – R606 807
Lekwa (MP)	R0,043	Eskom interest of R0,04 billion; remainder relating to penalties and interest – Sars, AGSA and Telkom
City of Tshwane Metro (GP)	R0,042	Mostly related to standing time, interest and re-application of licence at Temba water purification plant
Msukaligwa (MP)	R0,041	Eskom interest of R0,02 billion and Department of Water Affairs interest and penalties of R0,021 billion
Ditsobotla (NW)	R0,037	Eskom interest of R0,024 billion; remainder relating to penalties and interest – Sars and AGSA
Total for top 10	R0,818	This constitutes 54% of the total fruitless and wasteful expenditure R0,365 billion (45%) of top 10 value related to interest on late payments to Eskom

INVESTIGATION AND FOLLOW-UP OF PRIOR YEAR UIFW

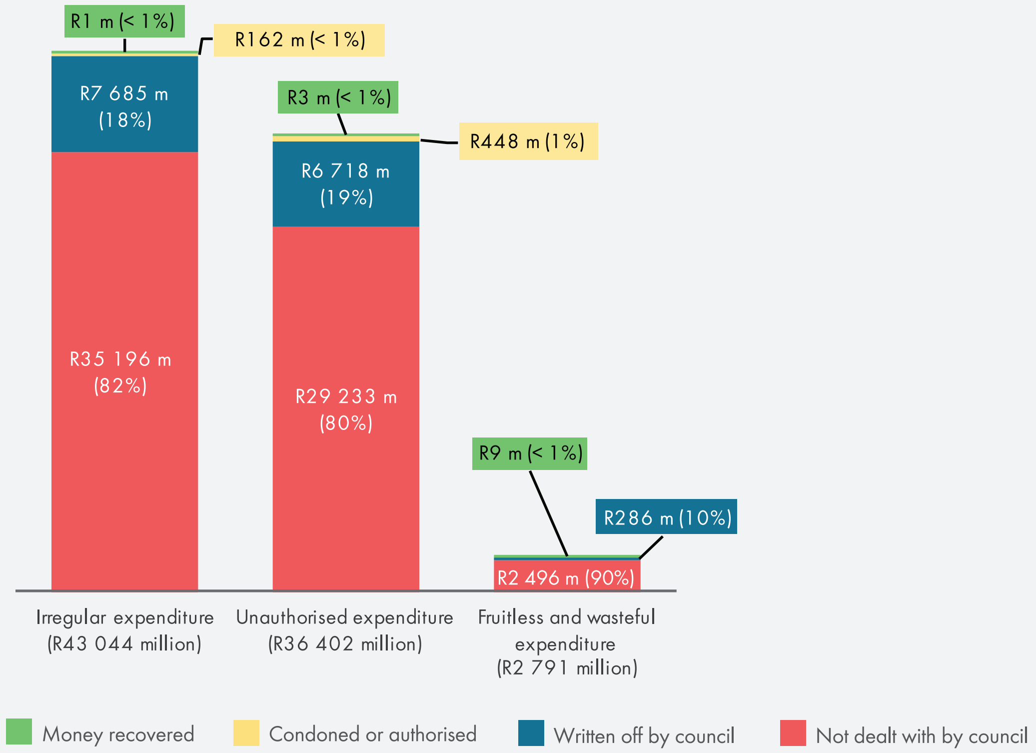
Investigations by municipalities of all prior year instances regressed from 103 (48%) to 84 (39%)

UIFW disclosed must be investigated by the council to determine impact and responsible person/s. Based on the outcome of the investigation, the next steps can include condonement/authorisation, recovery or write-off.

HOW HAS COUNCIL DEALT WITH THE 2015-16 UIFW?



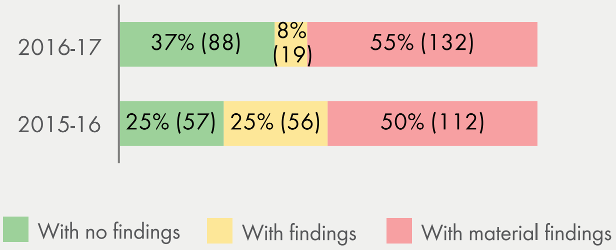
HOW HAS COUNCIL DEALT WITH ALL THE UIFW TO DATE?



FRAUD AND LACK OF CONSEQUENCES

▼ SLIGHT INCREASE IN MATERIAL NON-COMPLIANCE WITH LEGISLATION ON IMPLEMENTING CONSEQUENCES

NON-COMPLIANCE WITH LEGISLATION ON IMPLEMENTING CONSEQUENCES



Most common findings were the following:

- *Irregular expenditure identified in prior year was not investigated at 122 municipalities (51%)*
- *Fruitless and wasteful expenditure identified in prior year was not investigated at 114 municipalities (48%)*
- *Unauthorised expenditure identified in prior year was not investigated at 100 municipalities (42%)*

MECHANISMS TO DEAL WITH LACK OF CONSEQUENCES ▼

Inadequate mechanisms for reporting and investigating transgressions and possible fraud at 82 municipalities (34%)

Most common findings were the following:

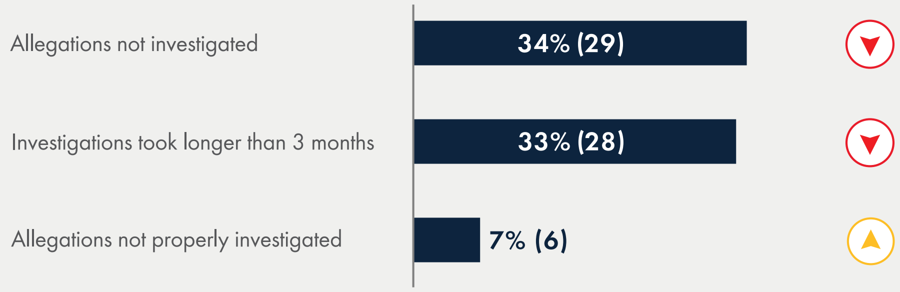
Disciplinary board not established at 56 municipalities (23%)

No policies regarding investigations of allegations and disciplinary procedures at 46 municipalities (19%)

No hotline or other process to report fraud at 32 municipalities (13%)

CONTRIBUTE TO

INADEQUATE FOLLOW-UP OF ALLEGATIONS OF FINANCIAL AND SUPPLY CHAIN MANAGEMENT MISCONDUCT AND FRAUD



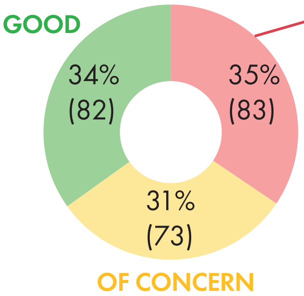
AND

Unauthorised, irregular and fruitless and wasteful expenditure (UIFW) not followed up and dealt with – refer to section on UIFW

Supply chain management (SCM) findings we reported to management for investigation not followed up – refer to section on SCM

FINANCIAL HEALTH

▼ SLIGHT REGRESSION IN FINANCIAL HEALTH



INTERVENTION REQUIRED

This means the municipality:
- is in a vulnerable financial position and might be unable to continue operating and/or
- received a disclaimed or adverse opinion, which means the financial statements were not reliable enough for analysis

VULNERABLE FINANCIAL POSITION

31% (73)
26% (59) ▼

Fruitless and wasteful expenditure of **R1,1 billion** incurred by those in vulnerable financial position

🟦 2016-17 🟦 2015-16

SUSTAINABILITY INDICATORS

NET CURRENT LIABILITY POSITION

43% (90)
40% (83) ▼

BANK IN OVERDRAFT

3% (7)
2% (4) ▼

DEFICIT (expenditure exceeded revenue)

31% (66)
33% (68) ▲

Consolidated deficit of R5,6 billion

Major contributors from:
- *Mpumalanga* - **R1,8 billion (32%)**
- *Free State* - **R1 billion (19%)**
- *Gauteng* - **R1 billion (19%)**

86% (57) *of those with deficits also incurred unauthorised expenditure amounting to* **R5,8 billion**

CREDITOR PAYMENTS

CREDITOR-PAYMENT PERIOD > 30 DAYS

87% (183)
82% (170) ▼

CREDITOR-PAYMENT PERIOD > 90 DAYS

47% (100)
42% (87) ▼

AVERAGE CREDITOR-PAYMENT PERIOD

161 DAYS
140 DAYS ▼

ESKOM ARREARS - R9,4 billion

***71%** of arrears concentrated in Free State (**49%**) and Mpumalanga (**22%**)*

Source – Eskom annual report: March 2017

WATER BOARD ARREARS - R6,5 billion

Free State contributed R2,6 billion (40%) to total

Source – Treasury database: 30 September 2017

REVENUE MANAGEMENT INDICATORS

MORE THAN 10% OF DEBT IRRECOVERABLE

92% (195)
95% (196) ▲

DEBT-COLLECTION PERIOD > 90 DAYS

55% (115)
51% (106) ▼

AVERAGE DEBT-COLLECTION PERIOD

187 DAYS
178 DAYS ▼

PROVINCIAL VIEW

PROVINCE	OVERALL ASSESSMENT*				INDICATORS*							
	GOOD	OF CONCERN	INTERVENTION REQUIRED		VULNERABLE FINANCIAL POSITION		CREDITOR-PAYMENTS > 30 DAYS		MORE THAN 10% OF DEBT IRRECOVERABLE		DEFICIT	
Eastern Cape	32% (12)	42% (16)	26% (10)	▼	24% (9)	▼	86% (30)	▼	94% (33)	▲	26% (9)	▲
Free State	0% (0)	0% (0)	100% (18)	▼	94% (17)	▼	100% (13)	▶	100% (13)	▼	85% (11)	▼
Gauteng	18% (2)	46% (5)	36% (4)	▼	45% (5)	▼	91% (10)	▼	82% (9)	▲	45% (5)	▲
KwaZulu-Natal	47% (25)	30% (16)	23% (12)	▼	19% (10)	▼	86% (43)	▼	100% (50)	▶	10% (5)	▲
Limpopo	39% (9)	39% (9)	22% (5)	▼	9% (2)	▲	89% (17)	▼	89% (17)	▲	21% (4)	▲
Mpumalanga	25% (5)	50% (10)	25% (5)	▲	20% (4)	▼	89% (17)	▼	89% (17)	▼	42% (8)	▼
Northern Cape	8% (2)	36% (9)	56% (14)	▼	56% (14)	▼	96% (22)	▼	87% (20)	▲	65% (15)	▼
North West	14% (3)	27% (6)	59% (13)	▼	45% (10)	▲	86% (12)	▲	86% (12)	▲	50% (7)	▼
Western Cape	86% (24)	7% (2)	7% (2)	▲	7% (2)	▲	70% (19)	▲	89% (24)	▲	7% (2)	▲

*including municipalities with disclaimed/adverse opinions

*excluding municipalities with disclaimed/adverse opinions

INFRASTRUCTURE DEVELOPMENT AND MAINTENANCE

▼ COMPLIANCE WITH DIVISION OF REVENUE ACT REMAINED UNCHANGED AT 87%, BUT PROJECT MANAGEMENT WEAKNESSES REMAINED WIDESPREAD

MANAGEMENT OF INFRASTRUCTURE GRANTS

FUNDING	MUNICIPAL INFRASTRUCTURE GRANT (MIG) *518 projects (209 municipalities)*	PUBLIC TRANSPORT NETWORK GRANT (PTNG) *15 projects (10 municipalities)*	URBAN SETTLEMENT DEVELOPMENT GRANT (USDG) *30 projects (8 municipalities)*
Available to spend *(percentage of funds spent)*	R15,09 billion (94%) ▶	R5,85 billion (93%) ▲	R11,14 billion (96%) ▲
Underspending by more than 10%	46 municipalities (22%) ▼	4 municipalities (40%) ▼	2 municipalities (25%) ▼
Used for intended purpose	198 municipalities (95%) ▲	10 municipalities (100%) ▶	8 municipalities (100%) ▶

FINDINGS *(per project)*	MUNICIPAL INFRASTRUCTURE GRANT (MIG)	PUBLIC TRANSPORT NETWORK GRANT (PTNG)	URBAN SETTLEMENT DEVELOPMENT GRANT (USDG)
Targets not achieved/ not evaluated	38% (199) ▼	47% (7) ▼	23% (7) ▼
Reported achievements not reliable	14% (70) ▼	13% (2) ▼	7% (2) ▼
Supply chain management findings	27% (142) ▶	13% (2) ▼	20% (6) ▼
Not correctly accounted for in financial statements	5% (26) ▲	None ▲	17% (5) ▼

ROAD INFRASTRUCTURE

ROAD INFRASTRUCTURE DELIVERY FINDINGS	2016-17	2015-16
No approved road maintenance plan/priority list for renewal and routine maintenance	55% (107) ▼	50% (89)
No assessment of condition of all infrastructure	27% (53) ▼	18% (32)

43% (84) of the municipalities did not implement corrective action to address all findings raised in the previous year

ROAD PROJECT PLANNING FINDINGS

31% (61) - No standard for infrastructure procurement and delivery management

13% (25) - No needs/cost estimates for road projects

12% (23) - No detailed project plan completed during planning phase

11% (21) - No feasibility study conducted

ROAD PROJECT MANAGEMENT FINDINGS

26% (51) - Road projects exceeded planned completion date

12% (24) - No penalties imposed for projects not completed on time

9% (18) - No processes for project progress reporting

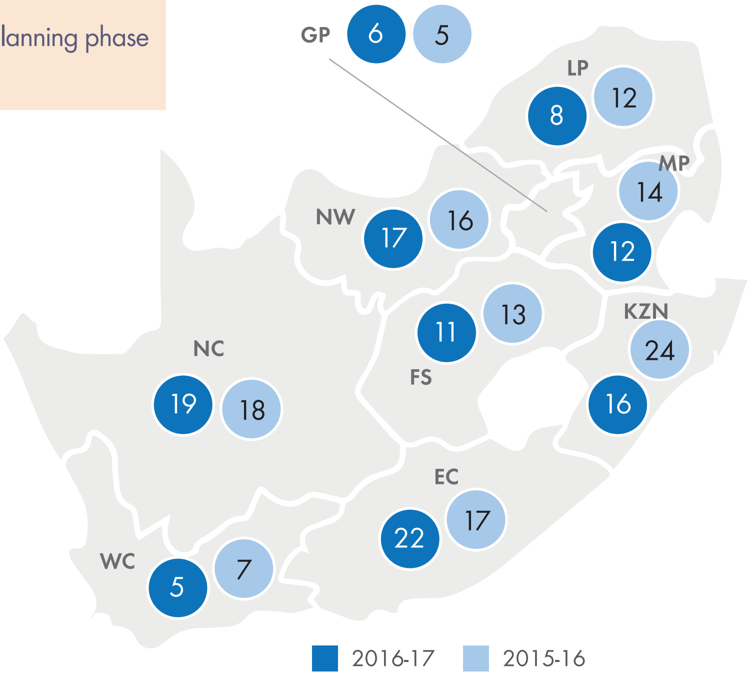
9% (17) - Construction sites not timeously handed over to contractors

8% (16) - Work completed not verified prior to payment

PROVINCIAL VIEW

FINDINGS

AFFECTING DELIVERY OF ROAD INFRASTRUCTURE



PROVISION OF WATER AND SANITATION

PERFORMANCE PLANNING AND REPORTING BY MUNICIPALITIES THAT ARE WATER AUTHORITIES

	WATER	SANITATION
Indicators not planned in SDBIP/IDP*	6% (8) ▲	8% (11) ▲
Indicators and targets not useful	4% (5) ▲	4% (5) ▲
Reported achievements not reliable	9% (13) ▲	10% (14) ►
Targets for indicators not achieved	11% (15) ▲	6% (8) ▲

WATER AND SANITATION INFRASTRUCTURE PROJECTS

KEY FINDINGS ON INFRASTRUCTURE PROJECTS	WATER	SANITATION
Exceeded completion date	26% (36) ▲	22% (30) ▲
With significant supply chain management findings	21% (29) ▲	17% (24) ►
Project did not address cause of backlog	18% (25) ▲	16% (21) ▲

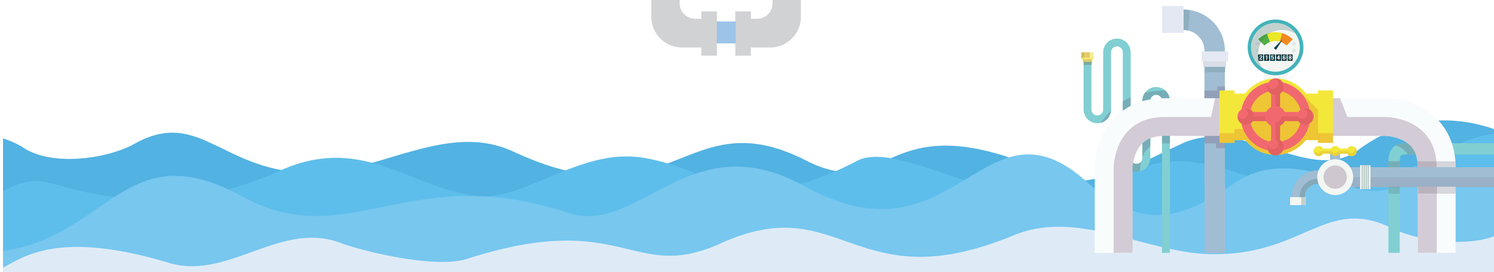
FUNDING	WATER	SANITATION
Used for intended purpose	95% ▼	97% ▼
Not fully utilised	27% ▼	16% ▼
Underspending more than 10%	17% ▼	10% ▲

*SDBIP/IDP: service delivery and budget implementation plan/integrated development plan

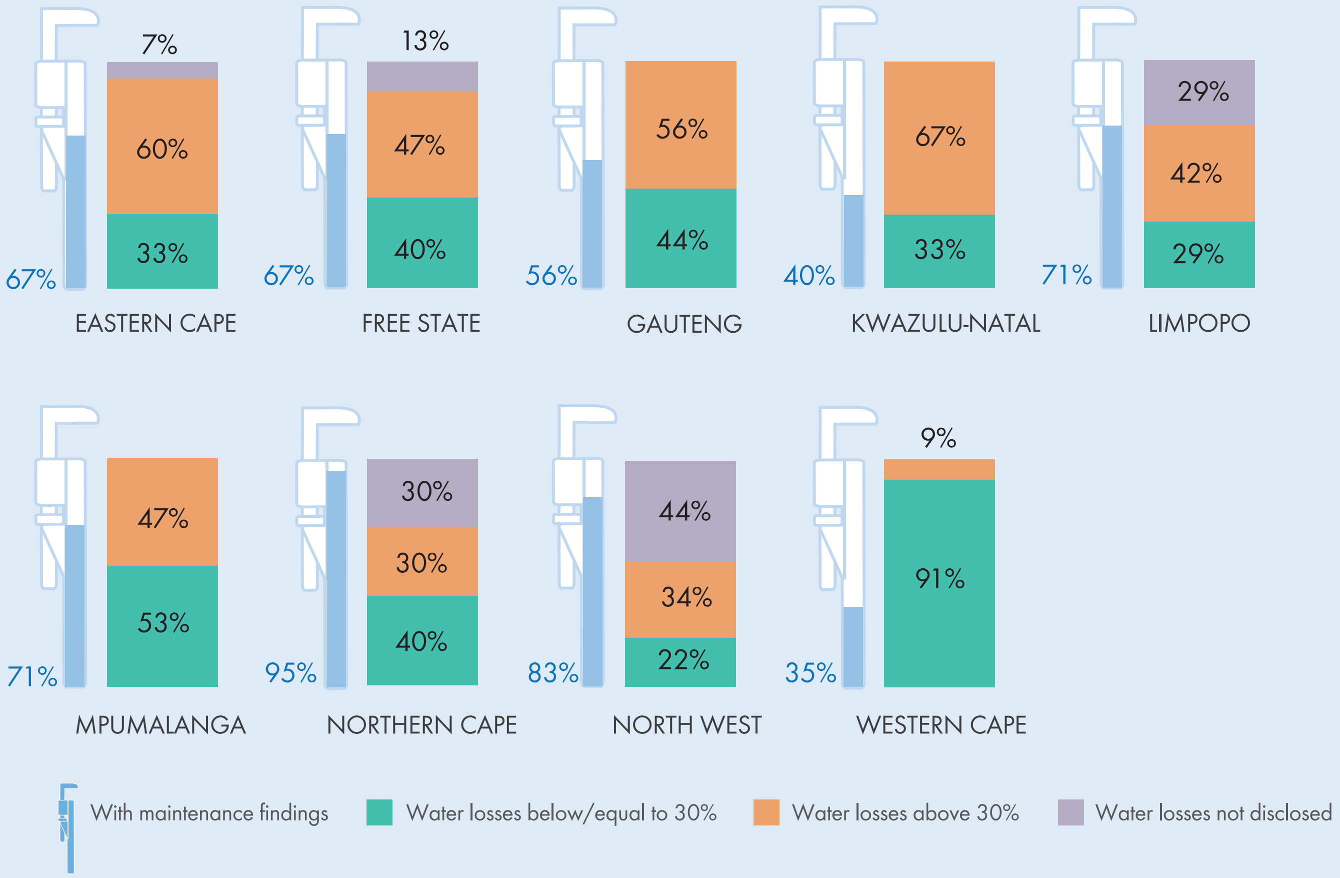
MAINTENANCE OF WATER INFRASTRUCTURE AND EXTENT OF WATER LOSSES

FINDINGS ON MAINTENANCE OF WATER INFRASTRUCTURE

- No policy on maintenance of water infrastructure ▶ 57%
- No maintenance plan ▲ 46%
- No assessment of condition to inform maintenance plan and budget ▼ 35%
- 26% ▼ No steps taken to prevent over-/underspending of routine water infrastructure maintenance budget
- 24% ▼ Targets and time frames for routine maintenance of water infrastructure not achieved
- 22% ▼ Maintenance was not budgeted for



MAINTENANCE WEAKNESSES AND WATER LOSSES



HUMAN RESOURCE (HR) MANAGEMENT

▼ SLIGHT REGRESSION IN GOOD HR MANAGEMENT CONTROLS - FROM 28% (62) TO 24% (58)

AVERAGE VACANCY RATES

OVERALL ▼ **21%**   *SENIOR MANAGEMENT* ▼ **28%**   *FINANCE UNITS* ▼ **18%**

Resourcing of 48% (114) of the finance units assessed as either concerning or requiring intervention

KEY POSITIONS - VACANCIES, STABILITY AND ACHIEVEMENT OF COMPETENCY REQUIREMENTS

MUNICIPAL MANAGER

VACANCIES 27% (65) ▼

VACANT for less than 6 months - **10% (24)**

VACANT for 6 months or more - **17% (41)**

STABILITY 40 months *(Average number of months in position)* ▼

COMPETENCY 10% (17) ▲

Did not meet minimum requirements - **6% (11)**

Minimum competencies not assessed/ limitations - **4% (6)**

CHIEF FINANCIAL OFFICER

VACANCIES 28% (68) ▼

VACANT for less than 6 months - **7% (17)**

VACANT for 6 months or more - **21% (51)**

STABILITY 44 months *(Average number of months in position)* ▼

COMPETENCY 11% (19) ▲

Did not meet minimum requirements - **8% (14)**

Minimum competencies not assessed/ limitations - **3% (5)**

STABILITY* IN KEY POSITIONS PRODUCED BETTER AUDIT OUTCOMES

MUNICIPAL MANAGER

**Average number of months in position*

🟩 66 🟨 40 🟪 29 🟥 19

CHIEF FINANCIAL OFFICER

**Average number of months in position*

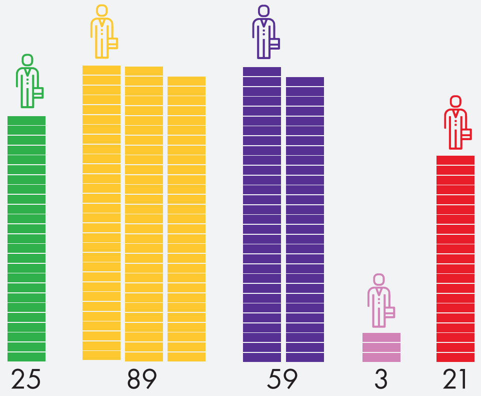
🟩 58 🟨 48 🟪 32 🟥 32

🟩 *Unqualified with no findings* 🟨 *Unqualified with findings* 🟪 *Qualified with findings* 🟥 *Adverse and disclaimed with findings*

EFFECTIVE USE OF CONSULTANTS

Local government spent an estimated **R2 772 million** on consultancy services in **2016-17**

CONSULTANTS USED FOR FINANCIAL REPORTING SERVICES - R757 million (2015-16: R752 million)



AUDIT OUTCOMES WHERE CONSULTANTS WERE USED **15 ∧** **34 ∨**

- 🟩 Unqualified with no findings
- 🟨 Unqualified with findings
- 🟪 Qualified with findings
- ■ Adverse with findings
- 🟥 Disclaimed with findings

__42% (101)__ of the financial statements submitted for auditing included material misstatements in the areas in which **consultants did work**

This means the **misstatements were identified and corrected by the audit process and not by the consultants,** *prior to submission of the financial statements for audit purposes*

REASONS WHY **FINANCIAL REPORTING** CONSULTANTS WERE INEFFECTIVE

AUDITEE INEFFECTIVENESS
27% (54)

POOR PROJECT MANAGEMENT
12% (23)

CONSULTANT DID NOT DELIVER
12% (23)

LACK OF RECORDS AND DOCUMENTS
9% (17)

CONSULTANT APPOINTED TOO LATE
9% (17)

MANAGEMENT OF CONSULTANTS - ALL SERVICES

At __69%__ of the __227__ municipalities that used consultancy services, significant weaknesses were identified in the following areas:

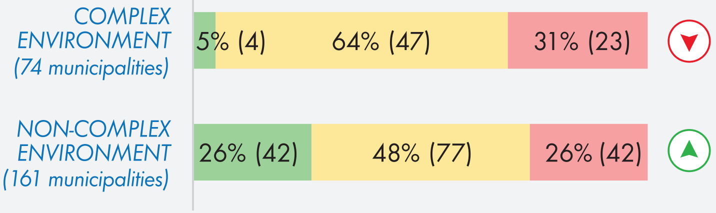
- ▲ **54%** Performance management and monitoring
- ▼ **48%** Transfer of skills
- ▲ **31%** Planning and appointment process

INFORMATION TECHNOLOGY (IT) CONTROLS

Slight improvement in IT controls

An inherent part of the control environment at 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.

OVERALL STATUS

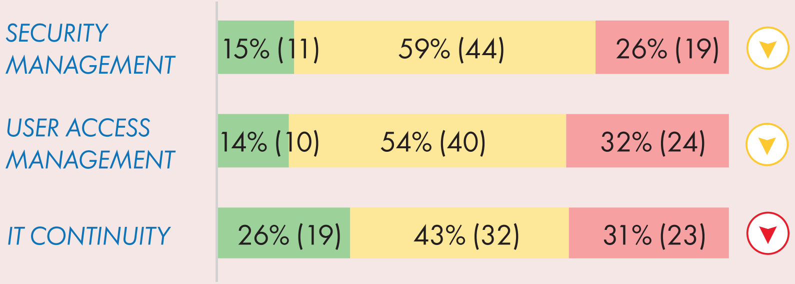


Municipalities with a **complex IT environment** have sophisticated hardware (e.g. more than one server and operating system) and software (e.g. customised applications); employ advanced technologies and transact online; and rely heavily on IT controls for financial and performance information.

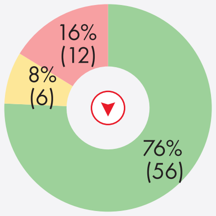
Municipalities with a **non-complex IT environment** use less sophisticated hardware and software (i.e. commercial off-the-shelf infrastructure and applications), while key controls over financial and performance information do not overly rely on IT.

COMPLEX ENVIRONMENT

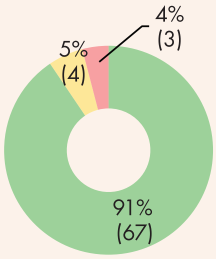
INFORMATION TECHNOLOGY FOCUS AREAS



QUALIFICATIONS AND EXPERIENCE – chief information officers or IT managers



USE OF IT CONSULTANTS



🟩 Good 🟨 Of concern 🟥 Intervention required

At the 74 municipalities with complex IT environments, only 9% appointed IT consultants due to a shortage of skills or to fill vacant positions. Although the other 91% did not appoint IT consultants to fill vacant positions, they were still using IT consultants to support them. The total approximate cost for IT consultants at these municipalities was R540 million.

PROGRESS TOWARDS IMPLEMENTATION OF SUB-OUTCOMES OF REVISED MEDIUM-TERM STRATEGIC FRAMEWORK INITIATIVES

SUB-OUTCOME 1: MEMBERS OF SOCIETY HAVE SUSTAINABLE AND RELIABLE ACCESS TO BASIC SERVICES

Programme management office and municipal asset management

Municipalities not utilising municipal asset management system

15 (6%)

Municipalities not receiving related assistance from Department of Cooperative Governance (DCoG)

8 (3%)

PROVINCE	EASTERN CAPE	FREE STATE	GAUTENG	KWAZULU-NATAL	LIMPOPO	MPUMALANGA	NORTHERN CAPE	NORTH WEST	WESTERN CAPE
Municipalities not utilising municipal asset management system	5% (2)	28% (5)	0% (0)	0% (0)	0% (0)	5% (1)	16% (4)	14% (3)	0% (0)
Municipalities not receiving related assistance from DCoG	3% (1)	6% (1)	0% (0)	0% (0)	0% (0)	0% (0)	20% (5)	5% (1)	0% (0)

53% (8) of those not utilising Municipal Infrastructure Support Agent's asset management system or similar were also qualified on assets

SUB-OUTCOME 3: DEMOCRATIC, WELL-GOVERNED AND EFFECTIVE MUNICIPAL INSTITUTIONS CAPABLE OF CARRYING OUT THEIR DEVELOPMENTAL MANDATE AS PER THE CONSTITUTION

Public participation

PROVINCE	EASTERN CAPE	FREE STATE	GAUTENG	KWAZULU-NATAL	LIMPOPO	MPUMALANGA	NORTHERN CAPE	NORTH WEST	WESTERN CAPE	TOTAL
Ward-level improvement plans not submitted for auditing	3	1	0	1	0	0	2	1	0	8
Ward-level improvement plans not developed	9	5	0	0	0	5	11	5	3	38
Ward-level improvement plans did not address basic concerns	0	1	0	0	0	2	1	2	0	6
Ward committees not established for each ward	7	0	2	1	0	0	3	2	1	16

SUB-OUTCOME 4: SOUND FINANCIAL AND ADMINISTRATION MANAGEMENT

Implementation of back-to-basics (B2B) programme

▼ SLIGHT REGRESSION IN NUMBER OF MUNICIPALITIES NOT REPORTING ON A MONTHLY BASIS

No monthly reporting on B2B

2016-17 15% (37)

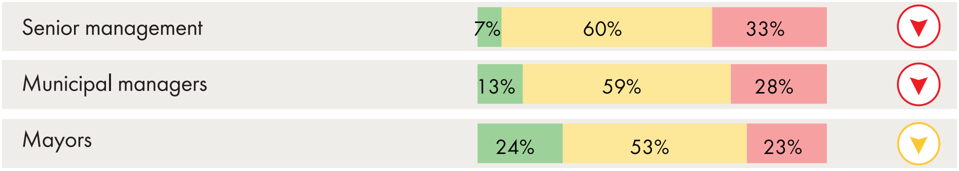
2015-16 14% (32)

PROVINCE		EASTERN CAPE	FREE STATE	GAUTENG	KWAZULU-NATAL	LIMPOPO	MPUMALANGA	NORTHERN CAPE	NORTH WEST	WESTERN CAPE
No monthly reporting on B2B	2016-17	41% (16)	22% (4)	0% (0)	6% (3)	0% (0)	10% (2)	12% (3)	32% (7)	7% (2)
	2015-16	23% (8)	39% (7)	0% (0)	0% (0)	5% (1)	21% (4)	33% (8)	19% (4)	0% (0)
	Movement	▼	▲	►	▼	▲	▲	▲	▼	▼

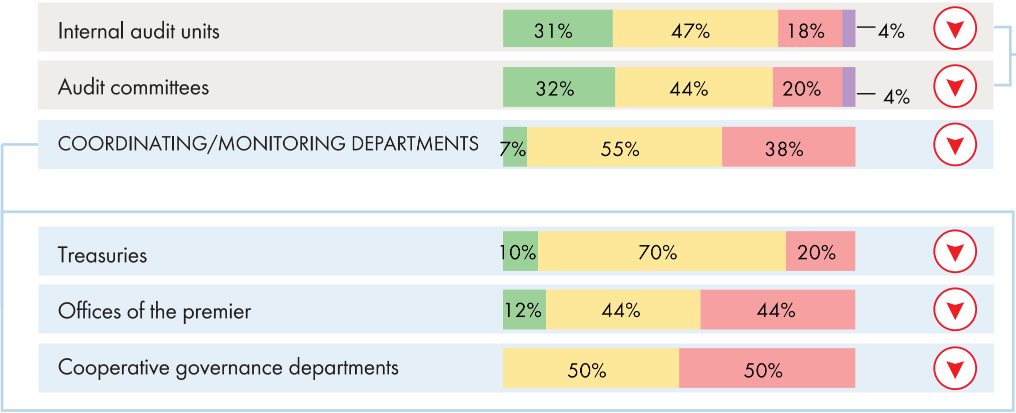
ASSURANCE PROVIDERS

▼ OVERALL REGRESSION IN ASSURANCE PROVIDED BY ROLE PLAYERS

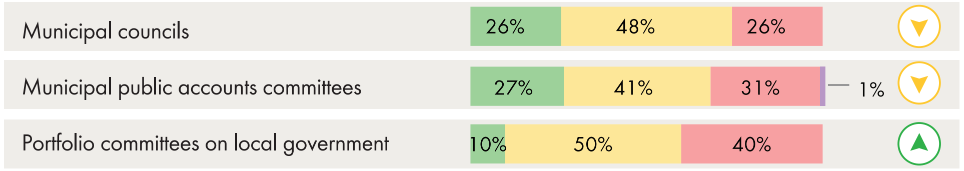
ASSURANCE PROVIDED BY MANAGEMENT / LEADERSHIP



INTERNAL INDEPENDENT ASSURANCE AND OVERSIGHT



EXTERNAL INDEPENDENT ASSURANCE AND OVERSIGHT

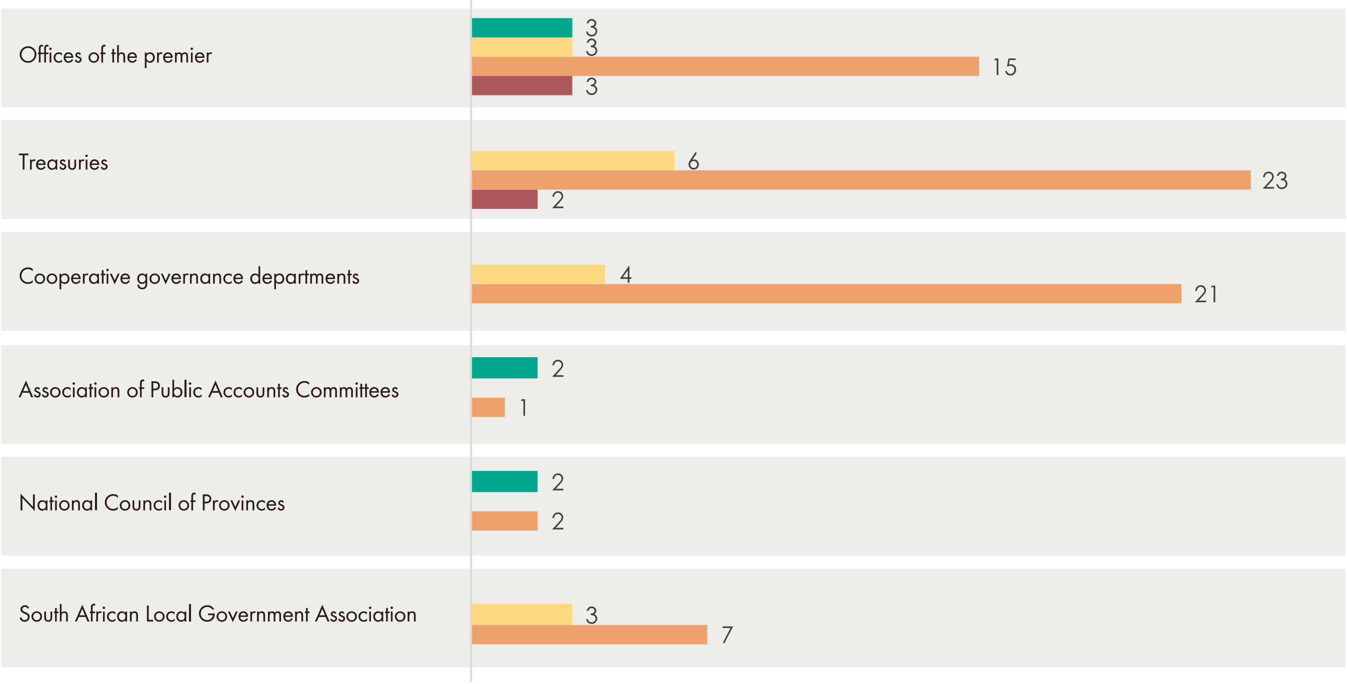


🟩 Provides assurance 🟨 Provides some assurance 🟥 Provides limited/no assurance 🟪 Not established

Low levels of assurance show 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

FINDINGS	INTERNAL AUDIT UNITS	AUDIT COMMITTEES
Fully compliant with legislation	83% (190) ▼	82% (188) ▼
Positive impact on audit outcomes	39% (89) ▼	53% (121) ▼
Evaluates reliability of financial information	87% (200) ▲	89% (204) ▲
Evaluates reliability of performance information	84% (194) ▲	86% (198) ▲
Evaluates compliance with key legislation	89% (205) ▲	88% (203) ▲
Interacts with executive authority	N/A	90% (207) ▶

STATUS OF COMMITMENTS MADE IN PREVIOUS YEARS BY NATIONAL AND PROVINCIAL ROLE PLAYERS TO SUPPORT LOCAL GOVERNMENT



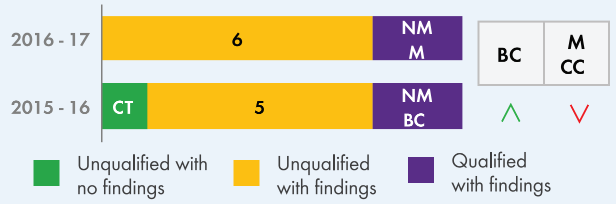
🟩 Completed - significant impact 🟨 Completed - limited impact 🟧 In progress 🟥 Not implemented

STATUS OF METROS

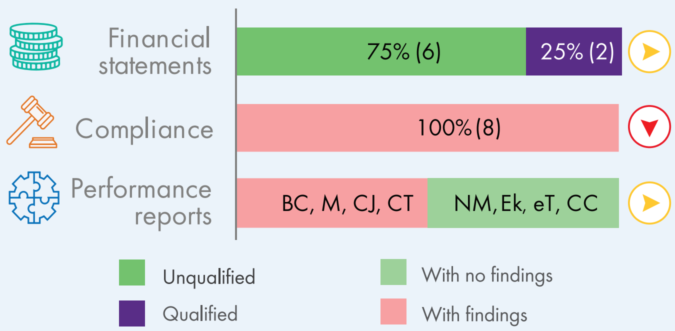
▼ OVERALL REGRESSION IN AUDIT OUTCOMES

AUDIT OUTCOMES

Almost 55% (R195 billion) of the total municipal expenditure budget of R362 billion was managed by metros



AUDIT OUTCOMES ON THREE KEY AREAS



eThekwini and City of Cape Town submitted their financial statements and performance reports with no material misstatements

FINANCIAL HEALTH ▼

INTERVENTION REQUIRED

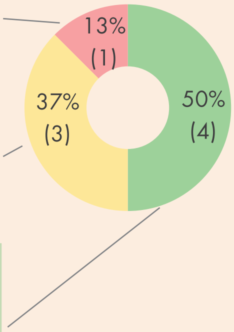
- Mangaung (M)

OF CONCERN

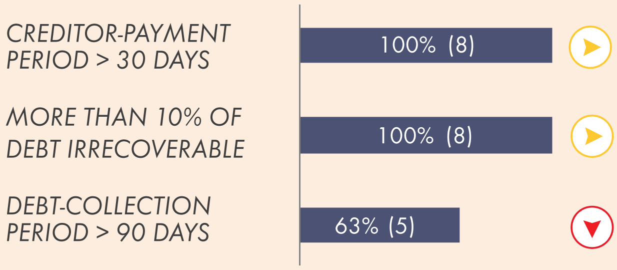
- City of Johannesburg (CJ)
- City of Tshwane (CT)
- Nelson Mandela Bay (NM)

GOOD

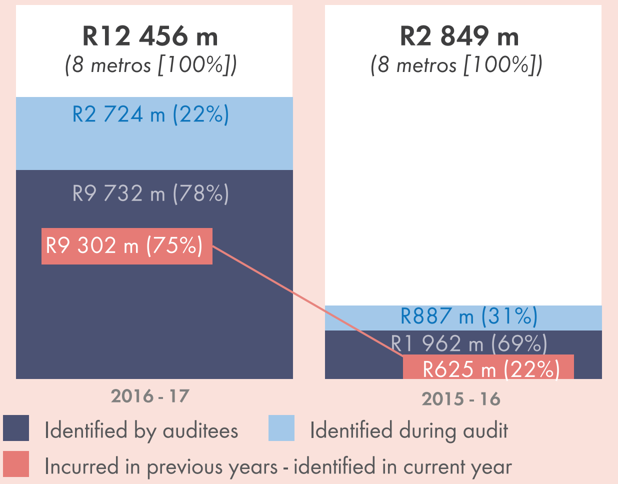
- Buffalo City (BC)
- City of Cape Town (CC)
- City of Ekurhuleni (Ek)
- eThekwini (eT)



FINANCIAL HEALTH INDICATORS



IRREGULAR EXPENDITURE ▼



FINDINGS ON SUPPLY CHAIN MANAGEMENT

METROS	UNCOMPETITIVE PROCESS	INADEQUATE CONTRACT MANAGEMENT	AWARDS TO CLOSE FAMILY MEMBERS	LIMITATION	AWARDS TO EMPLOYEES
Buffalo City Metro	🟨	🟩	🟨	🟩	🟩
City of Johannesburg Metro	🟥	🟥	🟥	🟩	🟨
City of Tshwane Metro	🟥	🟩	🟨	🟥	🟩
City of Ekurhuleni Metro	🟥	🟩	🟨	🟥	🟨
eThekwini Metro	🟨	🟩	🟨	🟩	🟨
Mangaung Metro	🟨	🟥	🟩	🟨	🟩
Nelson Mandela Bay Metro	🟥	🟥	🟥	🟩	🟩
City of Cape Town Metro	🟥	🟨	🟩	🟩	🟩

🟩 With no findings 🟨 With findings 🟥 With material findings

VACANCIES AND STABILITY

	MUNICIPAL MANAGER	CHIEF FINANCIAL OFFICER
Vacancies at year-end	None ▲	CJ* ►
Stability *(Average number of months in position)*	23 ▼	63 ▼

*Vacant for less than 6 months

SECTION 5

Provincial overviews

5.1 EASTERN CAPE

PROVINCIAL SNAPSHOT

▼ **Clean audits: 5%** (2015-16: 20%)

▼ **Quality financial statements: 62%** (2015-16: 63%)

▼ **Quality performance report: 31%** (2015-16: 40%)

▼ **No findings on compliance with legislation:5%** (2015-16: 20%)

▼ **Irregular expenditure: R13 558 m** (2015-16: R5 428 m)

The Eastern Cape local government consists of 49 auditees, made up of 39 municipalities and 10 municipal entities. Ten municipalities reported on in the previous year were merged into four new municipalities at the beginning of the year under review. The 2015-16 percentages in the graphic above therefore exclude the 10 municipalities that were disestablished to ensure greater comparability of the information. In addition, the outcomes of the 10 municipal entities are excluded from this analysis, as they did not have a significant impact on the overall outcomes of local government in the province.

At the start of their term, we informed the political leadership of their roles and responsibilities in ensuring a responsive, accountable, effective and efficient local government that is characterised by robust and transparent financial and performance management systems and by resilient oversight and accountability mechanisms. During our engagements on the status of records review, we provided early warning signals on the need to maintain stability in the administrative leadership, fill vacancies timeously, and improve the status of records management and basic internal controls. In addition, we emphasised the need to be diligent and decisive in dealing with irregularities. The engagements were consistent and done in advance to assist in improving the audit outcomes (and sustaining the good outcomes) as well as to avoid a collapse in governance that could lead to accountability failures.

The municipal leadership did not heed our numerous warnings about the impact that changes at an administrative level and the failure to fill vacancies timeously would have on accountability. As a result, the improvements in audit outcomes seen over the past few years stalled. The overall outcomes reflect a net regression of one, made up of six improved and seven regressed audit outcomes. The seven regressions include five municipalities that had unqualified opinions with no findings in the prior year. The disregard for our messages and warning signals was most noticeable at Mnquma where there was a collapse in oversight and governance accompanied by a breakdown in internal controls, caused by leadership that was in conflict with itself, unrest and strikes. These accountability failures caused the municipality's outcome to regress from an unqualified opinion with findings to a disclaimed opinion as a result of it not being able to account for its financial affairs.

During previous years, we continuously warned the provincial leadership that the mergers were complex and needed leadership to drive the changes and manage the process. This would entail making sure that systems were tested for integration and alignment, that there were adequate resources including skilled and competent people to support the implementation of plans, and ensuring that core staff members were retained. Our warnings were ignored, resulting in three of the four merged municipalities not being able to account for their current year's financial affairs – as reflected by their disclaimed audit opinions.

The municipalities that received modified opinions were similar to last year at 39%. The most common qualification areas requiring attention to improve transparency included the disclosure of irregular expenditure; property, infrastructure and equipment; and receivables. During the year under review, we saw a reduction in the use of consultants to prepare financial statements. This reduction in both the number of municipalities using consultants and their associated cost is a positive response to our previous recommendations relating to building in-house capacity and reducing the reliance placed on external consultants to prepare financial statements. However, this resulted in a 21% regression in the quality of the financial statements submitted for auditing, as 90% of the municipalities required material adjustments to their financial statements in 2016-17.

It is encouraging to note that the provincial treasury capacitated its municipal finance unit and regularly engaged with municipalities on matters affecting their financial management. The provincial cooperative governance department supported municipalities in the key areas of action plans, back to basics, public participation, revenue enhancement strategies, human resource planning, and capacity building. Municipalities in the province are in the early stages of implementing the Municipal Standard Chart of Accounts, with the aim of improving financial reporting. Five municipalities adopted this early and we raised findings at three of them. We are worried about the province's readiness to implement the Municipal Standard Chart of Accounts, as we assessed the readiness of 28% of the municipalities as concerning and that of a further 8% as requiring intervention. We have raised these concerns with the provincial treasury.

The 9% increase in the number of performance reports with findings and 15% regression in the quality of the performance reports submitted for auditing were due to poor planning as well as a lack of systems to track performance and to collect, collate and record information about actual performance. The lack of improvement in this area by 69% of the municipalities, despite our reporting thereon for a number of years, ultimately affects the process that helps to improve performance and achieve positive results.

The 15% regression in compliance with legislation and overall high levels of non-compliance were due to a culture where leadership tolerated compliance deviations instead of taking appropriate action against those responsible for transgressions. When a municipality or its entities enter into contracts for goods and services, they must do so in a manner that is transparent, competitive, equitable, fair and cost-effective. For a number of years, we have expressed concern over the disregard for the requirements of our country's constitution in procuring goods and services. The culture of non-compliance and lack of consequences for legislative transgressions resulted in cumulative irregular expenditure of R22,9 billion at the end of the financial year under review. An amount of R9,4 billion in irregular expenditure brought forward from the prior period was neither written off after investigation nor recovered as required by legislation. Furthermore, we could not find evidence that 49% of the municipalities had investigated and followed up the irregular expenditure incurred by them in previous years.

Irregular expenditure increased due to instability, disregard for laws and regulations, and the absence of solid internal controls

An amount of R13,6 billion in irregular expenditure was incurred and disclosed during the year under review. This irregular expenditure may not be the full amount incurred, as 12 municipalities were qualified on the irregular expenditure disclosed by them. This amount included R7,2 billion identified as a result of the diligence applied by the new leadership in identifying payments made on contracts and quotations in the previous year that had been awarded irregularly and reclassified as irregular. A further R4,6 billion related to open contracts that were awarded irregularly in contravention of supply chain management legislation in previous years. There was very little evidence that councils had investigated the validity of these awards that continue to be paid despite having been deemed irregular. The remaining R1,8 billion related to contracts and quotations awarded irregularly in the year under review and not prevented by the accounting officers.

Most of the irregular expenditure disclosed was caused by supply chain management transgressions. One such common transgression was participating in contracts secured by other organs of state (in terms of supply chain management regulation 32) without ensuring that all of the conditions for participation were met. For example, one municipality used a contract secured by another municipality to appoint consultants to assist with financial reporting at a cost of R62 million over three years. The original contract stipulated a contract value of R7 million over 10 months, which the second municipality exceeded by R55 million and 26 months. Thus, this municipality did not comply with the requirements of regulation 32, as it was not participating in an existing contract but rather entered into a new contract with the supplier. Therefore, this contract was irregular and should have gone out on open tender.

The provincial cooperative governance department should assist municipalities to investigate prior year irregular expenditure and to deal with the large number of investigations required. Councillors should receive training on how to conduct investigations into irregular expenditure appropriately, which will ensure that oversight bodies take a strong stance against irregular expenditure and that transgressors face adequate consequences.

A municipality must strive, within its financial and administrative capacity, to achieve the objectives set out in our country's constitution. We are concerned about the financial sustainability of 24 municipalities in the province. They include five municipalities whose net current liabilities plus commitments and contingencies exceeded their entire budgets for 2017-18 and a further 19 municipalities where a large percentage of their 2017-18 budgets would be required to settle their current liabilities, commitments and contingencies. Four of the mentioned 24 municipalities had Eskom debts totalling R303 million that were significantly in arrears. The financial difficulties faced by these municipalities are an accumulation of various factors over a number of years. These include low revenue bases, inadequate cash-flow management, weak internal controls, poor governance, and accountability failures.

One of the key objectives of local government contained in the constitution is to promote social and local development – municipalities can do this by supporting small, medium and micro-sized enterprises. In order for such enterprises to flourish, they should be paid for the goods and services delivered by them within 30 days. However, 21 municipalities did not pay their suppliers within this stipulated period. This was due to 77% of the municipalities not including this requirement as a performance target and accounting officers not being held accountable.

South Africa needs to maintain and expand its electricity, water, transport and telecommunications infrastructure to support economic growth and social development goals. Our audits focused on the use of grants for their intended purposes and the effective implementation of road, water and sanitation infrastructure in local government. We found that the municipal infrastructure grant was used for its intended purposes, but that 22% of the municipalities underspent on their allocations by more than 10% and key milestones were not achieved on 36% of the projects.

Effective project management of infrastructure includes adequate planning that focuses on the needs of the community, clear scoping to allocate the right amount of work to successfully complete the project, and the use of competent service providers for the implementation of the project. An example where the needs of the community were not assessed is a municipality that provided two toilets (instead of one) to each household in a village while there was a backlog of 14 983 households that did not have access to sanitation services in other areas of the municipality.

We also noted poor project planning and implementation pointing to poor monitoring and evaluation practices throughout the project life cycle. For example, a contractor was appointed on a project valued at R54 million, and subsequently abandoned the site due to cash-flow problems and poor workmanship after he had been paid R15 million. As a result, a new contractor was appointed to carry out remedial work and to complete the project at a cost of R84 million. The completion of this project was delayed significantly, as it had a planned completion date of 30 June 2015 but was only 78% complete at 31 August 2017. This trend of delays was noted throughout the province as the work in progress balance increased from R10,8 billion to R12,5 billion during the year under review – R1,7 billion more than the previous year's balance.

Management was generally slow in implementing our recommendations to improve the control environment, including the controls in the information technology environment. This resulted in ineffective, slow and complicated manual processes, poor risk management, and ineffective governance. Very few municipalities had well-established and effective internal controls relating to the areas of leadership, financial and performance management, and governance. As a result, the required daily, weekly, monthly and annual disciplines were not embedded in the systems and processes at most municipalities. Furthermore, monitoring and oversight of the internal controls by all assurance providers were not effective and had a limited impact on the overall performance in the province.

At our numerous interactions with key role players in the province, we provided insights for them to take action on the issues reported relating to governance, financial management, performance management and oversight. We also conducted status of records reviews to provide the accounting officers with early warning signals on internal controls, irregular expenditure, the proactive auditing of service delivery and budget implementation plans, and financial viability. Despite these engagements being well received, the accounting officers were slow to act on our recommendations.

The amendments to the Public Audit Act could result in a shift in behaviour, culture, public trust and confidence. This will ultimately lead to local government institutions that are robust in providing basic municipal services, political leadership that does not interfere in operations (specifically relating to supply chain management and human resource appointment processes), municipalities being attractive to professionals thus retaining skills in the province, and transparent finances represented by good audit outcomes.

5.2 FREE STATE

PROVINCIAL SNAPSHOT

Clean audits: 0% ▼
(2015-16: 4%)

Quality financial statements: 56% ▼
(2015-16: 83%)

Quality performance report: 17% ▼
(2015-16: 44%)

No findings on compliance with legislation: 0% ▼
(2015-16: 6%)

Irregular expenditure: R675 m ▲
(2015-16: R813 m)

The fundamental principles needed to improve prior year audit outcomes, break the cycle of impunity and ensure accountability, include proper planning, execution and supervision of internal controls as well as consequences for poor performance. Without these fundamental principles and leadership setting the right tone, the audit outcomes did not improve to the desired level, as the leadership did not address the root causes of audit findings, strengthen internal controls, or improve monitoring.

Continued lack of accountability and leadership failures were the main causes of government failures, which led to a significant regression in audit outcomes

During 2015-16, we urged the political and administrative leadership to take accountability for, and address control weaknesses to improve, the audit outcomes. Notwithstanding the provincial leadership's continued commitments every year to implement basic key controls to ensure a sound control environment and implement consequences for poor performance and transgressions, these commitments have not yet been realised. Assurance providers did not prioritise the need to get the basics right, nor did they implement fundamental key controls such as monitoring compliance with legislation, adequate records management, daily and monthly processing and reconciling controls as well as accurate and regular financial and performance reporting.

This continued lack of accountability and leadership failures were the main causes of governance failures, which led to a significant regression in audit outcomes from the prior year. Seven municipalities regressed while no auditees were able to improve. Fezile Dabi District regressed from a clean audit to an adverse opinion. Kopanong and Mangaung Metro regressed from an unqualified audit opinion with findings to a qualified audit opinion. Mohokare and Tokologo regressed from unqualified audit opinions with findings to disclaimed opinions. Letsemeng and Nketoana regressed from qualified audit opinions to disclaimed opinions. Furthermore, five outstanding audits had not been finalised by the cut-off date for inclusion in this report due to the municipalities' late or non-submission of financial statements in an attempt to improve or sustain their previous year's audit outcome, namely Lejweleputswa District (consolidated financial statements), Mafube, Maluti-A-Phofung, Masilonyana, and Ngwathe.

If we had not allowed any audit adjustments, only Thabo Mofutsanyana District would have received a financially unqualified audit opinion. Municipalities relied on the audit process and consultants to identify shortcomings and to produce credible financial statements, despite most chief financial officers meeting the minimum competency requirements. This points to a lack of leadership and supervision, as chief financial officers did not review the financial statements and the relevant supporting information before submission for auditing. Inadequate skills and/or vacancies in finance departments contributed to the poor implementation of internal controls, thus creating a continued over-reliance on consultants in the province. The 12% increase in the senior management vacancy rate also contributed to the regression in audit outcomes. Despite us raising concerns during quarterly engagements with the political and administrative leadership about municipal manager contracts expiring shortly after the local government elections, as well as the vacancies and instability in senior management positions and the staff supporting them, very limited action was taken.

The slow response by the political and administrative leadership to address the weak control environment, a lack of consequences, and the continued disregard for legislative prescripts resulted in findings on compliance with legislation at all 18 municipalities. The main findings related to material adjustments to the financial statements, the inadequate management of expenditure as well as unauthorised, irregular and fruitless and wasteful expenditure not being prevented. Additionally, there was a noticeable regression in the quality of the reported performance information, as 15 municipalities had material findings, compared to 10 in the previous year. If we had not allowed audit adjustments, all municipalities would have had findings on their performance information. Performance reporting did not receive the necessary attention to enable accountability for, and transparency on, the performance against the political leadership's promises to citizens.

Despite information systems being critical to the integrity and availability of financial and performance information to enable reliable reporting, the information technology environment remained weak at most of the municipalities. There were also no dedicated strategies at any of the municipalities to implement an information technology platform to assist in reporting on performance information. At Mohokare and Tokologo, the weak information technology environment contributed to us raising material findings in their audit reports. Mohokare migrated to a new financial system without a proper system changeover process; while the system at Tokologo was breached by a virus and adequate backups were not available to restore reliable data. Most municipalities have not yet finalised their migration and mapping to the Municipal Standard Chart of Accounts; and where it had been done, challenges are still being experienced. The general information technology control environment, including the full implementation of the Municipal Standard Chart of Accounts, should be prioritised to ensure that complete and accurate financial information is available for the 2017-18 audit of the financial statements.

Irregular expenditure disclosed in the financial statements decreased from R813 million to R675 million. The decrease was due to Matjhabeng reporting irregular expenditure of R534 million in 2015-16, of which R228 million related to prior years, to address a qualification. The main contributors to irregular expenditure were Matjhabeng (R327 million), Tokologo (R57 million), and Letsemeng (R56 million). The most common instances of irregular expenditure related to competitive bids not being invited, bid adjudication committees not being composed properly, and the use of contracts secured by other organs of state without meeting the requirements of supply chain management regulation 32. It is concerning that R227 million of the irregular expenditure incurred related to multi-year contracts entered into in previous years that had not yet been dealt with appropriately, with Matjhabeng contributing R164 million. In 2016-17, the newly elected administration incurred R413 million of the total irregular expenditure. The closing balance of irregular expenditure stood at R2,5 billion for the province, which indicated that irregular expenditure was not always adequately investigated to identify the officials to be held accountable for the possible recovery of losses, resulting in the year-on-year increase in the balance.
A culture of no consequences has been created through leadership's involvement in the decision-making that led to transgressions. As a result, where irregular expenditure was investigated, officials were seldom found liable and amounts were written off. The continued disregard for procurement processes by the administrative and political leadership that resulted in irregular expenditure, coupled with limited consequences for these transgressions, is creating an environment open to misappropriation, wastage and the abuse of state funds.

The Medium-Term Strategic Framework calls for the establishment of an accountable, effective and efficient local government that promotes accountability for government spending in a manner that will have a positive impact on people's lives. In spite of this, unauthorised expenditure of R2,9 billion (2015-16: R2,5 billion) was incurred. At Letsemeng, Mohokare and Tswelopele, the municipal infrastructure grant was not used for its intended purpose. Spending on key projects relating to water and sanitation was riddled with shortcomings, as the municipalities did not always apply the principles of sound project planning and management, resulting in poor quality workmanship and delays in the completion of projects. Consequently, key performance targets were not always achieved or were not accurately reported.

An example of poor project planning and management was the construction of the Thabong T16 waterborne sanitation project of 1 300 stands in Matjhabeng, which started in 2014-15 at a budgeted amount of R62 million. The municipality prioritised the construction of the toilet structures, plumbing and internal sewers ahead of the bulk network at the pump station, while the sewer pipeline was also not connected to the pump station. This resulted in sewage overflow around the area of construction, which caused pollution and which could potentially compromise the health and safety of the Thabong residents. The appointment of the contractors was irregular and the project was still in progress. To date, R54 million had been spent on this contract. The municipality also entered into an agreement for the upgrading of the Nyakallong wastewater treatment works in 2012 for R52 million. A contractor was appointed in 2012, but a new contractor had to be appointed in 2016 – the municipality did not provide the reason for the change in contactor. This was done without following competitive bidding processes, which resulted in irregular expenditure. To date, R30 million had been spent on this contract. The significant delays in completing the project resulted in an unbearable odour for residents due to sewage overflowing in the street.

At Mangaung Metro, there were delays in various projects where significant amounts had been spent on planning and feasibility studies in previous years. For example, since the start of a project in 2012-13 for the planning and establishment of the airport development (N8) node with the purpose of establishing a new township development area, the municipality had spent R141 million on planning and establishment costs. However, no further progress had been made on this project and approval for the township establishment had not been obtained from the relevant planning tribunal.

Leadership's lack of accountability for sound financial management had a negative impact on municipalities' financial sustainability. Municipalities' financial health deteriorated from a net current liability position (where current liabilities exceed current assets) of R2,9 billion in the prior year to R4 billion in the current year. Municipalities faced significant cash-flow constraints, as they did not maximise the revenue from service charges and rates nor the collection of amounts outstanding from consumers. Municipalities also incurred significant electricity and water distribution losses of R1 billion (2015-16: R851 million) due to theft, illegal connections, poor monitoring of indigents' consumption, and poorly maintained infrastructure. Given these cash-flow constraints, municipalities fell behind with their payments for bulk purchases of electricity and water to Eskom by R2,5 billion (2016: R1,6 billion) and water boards by R2,5 billion (2015-16: R1,8 billion), which were outstanding at 30 June 2017. These late payments contributed to most of the fruitless and wasteful expenditure of R324 million (2015-16: R275 million), due to penalties and interest. The deterioration in municipalities' financial health was due to leadership not considering the budget when committing to strategic projects, not always paying the best price for goods and services, and wastage caused by poor planning. Without improved fiscal disciplines for the more effective, efficient and economical use of resources, municipalities' financial health and service delivery will continue to deteriorate.

Effective monitoring and oversight by all assurance providers are essential to break the cycle of impunity and to improve internal controls. The administrative and political leadership should create a culture that will result in a responsive, accountable, effective and efficient local government as envisaged in the Medium-Term Strategic Framework. Mechanisms to promote accountability typically include proper planning and budgeting; basic daily and monthly checks and balances on compliance as well as financial and performance information; ensuring stability in key positions; managing the performance of staff; and implementing consequences for poor performance and transgressions. Mayors and councillors should critically assess information, such as procurement deviations, before making decisions. 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.

We remain committed in our efforts to be a value-adding assurance provider through continuous engagements with the political and administrative leadership. We have reported the weaknesses in internal control and the risks that required attention in our management, audit and general reports. We provided root causes for audit findings and recommendations to address those root causes. We ensured that our messages were heard through quarterly engagements with all assurance providers. These actions have not had the desired impact and management was not always open and honest about key challenges. We have now extended our engagements to status of records reviews. These include an analysis of financial and non-financial information to identify key areas that may derail progress in the compliance with legislation and in the preparation of financial and performance reports. This could assist management to implement measures and action plans well in advance to lessen risks and the consequential regression in audit outcomes.

There has been an increased call for greater accountability in local government in the Free State. Our audits have consistently identified instances where accountability mechanisms in local government have failed. We trust that the proposed amendments to the Public Audit Act, once approved, will have a positive impact on implementing consequences. These amendments would deal with issues of recovery where losses have been suffered and enforcing accountability against officials responsible for such losses.

The fundamental principles needed to improve the audit outcomes require a commitment by leadership. They should therefore instil a culture of accountability and enforce adequate consequences where accountability failures occurred.

5.3 GAUTENG

PROVINCIAL SNAPSHOT

▶ **Clean audits: 9%**
(2015-16: 10%)

▶ **Quality financial statements: 100%**
(2015-16: 100%)

▼ **Quality performance report: 36%**
(2015-16: 60%)

▼ **No findings on compliance with legislation: 9%**
(2015-16: 20%)

▼ **Irregular expenditure: R3 653 m**
(2015-16: R1 291 m)

The Gauteng local government sustained its audit outcomes in 2016-17 with one municipality (9%) obtaining a clean audit. These outcomes are based on a reduced number of 11 municipalities due to the establishment of Rand West City, following the merger of Randfontein and Westonaria after the local government elections in 2016. We commend Midvaal for sustaining a clean audit outcome for the last four years. This was as a result of the municipality institutionalising a number of best practices (which should be replicated across the province), such as timeously monitoring the implementation of action plans to ensure that internal control deficiencies are addressed, maintaining stability in key positions, and effectively applying consequences.

In the previous year, we commended the province on the significant milestone of all municipalities obtaining an unqualified opinion and emphasised the importance of Rand West City maintaining this achievement following the merger. While the sustainability of this achievement in the current year was encouraging, the quality of the financial statements submitted for auditing regressed as only 36% of the municipalities (2015-16: 50%), namely Midvaal, Sedibeng District, Merafong City and Mogale City, submitted financial statements without material misstatements. The continued poor quality of financial statements at some municipalities was the result of a lack of accountability by chief financial officers and finance officials who did not adequately review financial information during the year. We continue to highlight that reliance on auditors to identify errors in the financial statements, which are then corrected by municipalities to avoid qualifications, is not a sustainable practice.

Auditees should enhance measures to address control deficiencies, as these pose a risk to the sustainability of positive audit outcomes

The audit outcomes on reported performance information regressed, as only 36% of the municipalities (2015-16: 60%), namely Midvaal, City of Ekurhuleni Metro, Merafong City and West Rand District, did not have findings on the usefulness and reliability of their performance reports. However, only Midvaal achieved this without reliance on the audit process and submitted a performance report without material misstatements. The poor quality of performance reports is concerning and indicates that previous actions to address internal control deficiencies were not implemented in a sustainable manner. The political and administrative leadership should hold heads of monitoring and evaluation units accountable for the accurate reporting of performance information. This, in turn, will allow 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 only Midvaal did not have material findings on compliance with legislation. The most common finding related to procurement and contract management at 82% of the municipalities. We continue to highlight that non-compliance with legislation remains the major obstacle preventing most municipalities in the province from attaining a clean audit.

Encouragingly, unauthorised expenditure in the province decreased from R3,2 billion to R2 billion due to improved budget controls and monitoring, particularly at the City of Tshwane Metro, where unauthorised expenditure decreased by R1,3 billion. However, irregular expenditure increased significantly to R3,7 billion (2015-16: R1,3 billion) due to increased supply chain management non-compliance, as well as irregular expenditure on contracts awarded in previous years (so-called legacy contracts). The majority of the irregular expenditure (R2,4 billion: 66%) related to expenditure on legacy contracts, which were still under investigation. The City of Tshwane Metro was the largest contributor with irregular expenditure of R1,8 billion (50%), of which R1,6 billion (87%) was due to legacy contracts (including R1,3 billion on the smart prepaid meter contract). The City of Johannesburg Metro incurred R706 million of the irregular expenditure, of which R313 million related to legacy contracts. The City of Ekurhuleni Metro incurred R591 million of the irregular expenditure, of which R224 million related to legacy contracts (including R209 million relating to the bus rapid transport project). The majority of municipal investigations relating to these contracts were still ongoing and should therefore be prioritised.

The province's high levels of non-compliance with legislation and resultant irregular expenditure, increase the risk of possible losses of public resources. The proposed amendments to the Public Audit Act are well timed, as some municipalities in the province have already started implementing stringent consequences. In the context of these amendments, we therefore encourage all municipalities to take a strong stance against the abuse of public funds by ensuring that oversight structures, such as municipal public accounts committees, appropriately investigate transgressions.

The slow response by the administrative leadership, as reflected in the regression in the level of assurance provided by senior management, was largely due to senior officials not prioritising the timeous implementation of the action plans they had committed to. This included senior management's failure to perform credible reviews of financial and performance information and a failure to set a strong tone against acts of non-compliance. Municipal managers should hold senior management accountable for the timely and diligent implementation of action plans. In addition, at large metros with many municipal entities, management in the different departments and entities within the municipal group should work in an integrated manner to resolve audit findings and take joint accountability to improve the control environment.

Instability and vacancies in key positions were root causes that hindered an improvement in audit outcomes. At some municipalities, the contracts of senior managers, who are typically appointed for five years coinciding with local government elections, had recently expired. The resulting vacuum was filled by acting officials, which created an environment that did not support effective performance management and the enforcement of consequences. Instability in the political environment also contributed to the slow response by the administrative leadership; for example, Mogale City had four mayors in the previous financial year, which hindered the appointment of the municipal manager and the chief financial officer. At the City of Tshwane Metro, City of Ekurhuleni Metro and Mogale City, chief financial officers were appointed towards the end of the financial year, while the chief financial officer position was filled by an acting official at the City of Johannesburg Metro, Emfuleni and Rand West City. Three municipalities, namely Emfuleni, Lesedi and Merafong City, did not have a permanent municipal manager at year-end, while all other municipalities except Midvaal and West Rand District appointed new municipal managers during the financial year. This instability at municipal level resulted in a loss of institutional knowledge and good practices already implemented due to key controls being more closely linked to individuals than to established municipal processes.

In the context of the current economic climate, characterised by low economic growth, municipalities' financial sustainability remained constrained, as they continued to experience difficulty in collecting debt from municipal consumers for basic services. This was especially the case for local municipalities in the West Rand and Sedibeng regions, which had a negative impact on these municipalities' ability to pay providers for basic services. In a province characterised by an expanding population with resultant increased infrastructure development and maintenance needs, this also placed a strain on capital expenditure spending. Municipalities should therefore intensify debt-collection processes and embrace prudent and efficient financial spending to ensure that they are still able to provide essential services to their citizens.

The status of the information technology environment regressed, as most municipalities did not adequately implement basic information technology security and user access policies and procedures, and did not enforce monitoring and evaluation mechanisms. At most municipalities, user functions were not adequately segregated, which compromised the integrity of revenue systems. At the City of Johannesburg Metro, service level agreements with some information technology service providers were not adequately managed while some information technology contracts were irregularly awarded. The implementation of the Municipal Standard Chart of Accounts remained a concern, as most municipalities continued to experience delays and challenges. Vacancies at chief information officer and information technology manager level contributed to the instability and lack of accountability within the information technology environment. To address these recurring findings, consequences should be applied where information technology commitments are not met.

Gauteng municipalities and their entities, primarily through the province's three metros, were responsible for R145 billion (36%) of South Africa's local government expenditure budget. This included R21 billion in capital expenditure (30% of the total local government capital expenditure). These funds were allocated to, amongst others, water and sanitation, electricity, road and housing infrastructure projects; all of which are critical enablers to delivering essential services to communities. Our analysis of municipal grants and key infrastructure projects indicated that, encouragingly, 95% of the total municipal infrastructure grant funding of R464 million was used and planned targets were achieved at 94% of the 17 projects funded by this grant. A total of 94% of the R2,5 billion public transport network grant funding was spent at the three metros; similarly, the metros spent 95% of the R5,3 billion urban settlement development grant funding and achieved the planned targets at 40% of the five projects funded. This demonstrates that while grant funding is generally used adequately in the province, the municipalities need to pay greater attention to achieving the planned targets, especially relating to the urban settlement development grant.

Our analysis of water infrastructure projects found, amongst others, that the planned completion dates of projects were not achieved at three municipalities (City of Ekurhuleni Metro, City of Johannesburg Metro, and Lesedi), while the planned targets for the maintenance of water infrastructure were not achieved at two municipalities (City of Tshwane Metro and Lesedi). At the City of Johannesburg Metro, a number of infrastructure projects are implemented through its municipal entities, including Johannesburg Water, City Power Johannesburg, and Johannesburg Roads Agency. At Johannesburg Water, the R25 million Doornkop West / Protea Glen water infrastructure upgrade project was six months behind schedule at year-end, which contributed to the underspending of the urban settlement development grant as highlighted above. However, penalties were instituted against the contractor, which is a good example of how to implement consequences. The City of Tshwane Metro's R516 million Temba water purification plant project experienced major delays and is a few years behind schedule due to poor project planning, including delays in obtaining authorisation from the relevant authorities such as the national Department of Water Affairs. These project management deficiencies resulted in late payments to the contractor, which contributed to an expenditure management non-compliance finding, losses due to idle time and interest paid, and resultant fruitless and wasteful expenditure of R42 million.

Our analysis of housing projects in the province indicated similar examples of delays due to poor project management. At the City of Johannesburg Metro, the R221 million Elias Motsoaledi mixed development housing project funded by the urban settlement development grant was due to be completed in March 2016, but one phase of the work was found to be only 55% complete at year-end as the contractor had abandoned the site. Further, a contractor was paid R22 million in excess of the original contract amount due to additional scope of work, for which no evidence or approval could be provided. These concerns contributed to delays in the completion and handover of houses, which subsequently resulted in service delivery protests. At the City of Ekurhuleni Metro, the R85 million phase 3 Palm Ridge X9 housing infrastructure project was delayed by six months due to design deficiencies that required certain structures to be rebuilt. These shortcomings indicate that there is significant room for improvement in the provisioning of housing infrastructure.

The condition of roads has an impact on all citizens and, as such, remains a key focus area for local government. At the Johannesburg Roads Agency, poor performance by the contractor on the M1/M2 road upgrade resulted in delays and the termination of the supplier's contract. The appointment of a new contractor was estimated to result in increased project costs of R43 million, which highlights the negative impact of poor performance.

However, we also found good project planning and management at some projects, which should be embraced at all municipalities. This includes City Power Johannesburg, where progress on the Sebenza power station was found to be on schedule. This was attributable to the appointment of contractors with the required competencies and experience and adhering to sound project disciplines such as holding regular project meetings.

Considering the specific examples of poor project management at various key projects audited, which contributed to delays and in some instances resulted in financial loss, there is a great opportunity for the province to prioritise the implementation of sound project management principles to ensure the efficient, effective and economical delivery of key basic services. This includes proper planning, regular monitoring and, as mentioned above, effectively enforcing consequences. By getting the basics right, municipalities will be better placed to avoid financial losses, improve financial sustainability, reduce related non-compliance with legislation, and ultimately improve audit outcomes.

As part of our contribution to improve accountability, we interacted regularly with stakeholders to discuss our management and audit reports and to highlight key areas requiring attention. We also performed status of records reviews as part of the 2016-17 financial year audit. These engagements assisted auditees to identify areas requiring attention early on, including the disclosure of contracts on which irregular expenditure was incurred. At Rand West City, this also assisted the municipality to sustain an unqualified opinion after the merger. The initiative was received positively by auditees and will be rolled out to all municipalities during the 2017-18 financial year audit.

Further improvement in clean administration remains achievable for the province as was demonstrated in 2014-15 when four municipalities (40%) obtained clean audits. We continue to encourage key role players such as the provincial cooperative governance department and the provincial treasury to intensify the level of support provided to municipalities going forward, especially in the areas of compliance and procurement. This will translate into improved audit outcomes across the province. We will continue to monitor the impact and progress of commitments made, as they are critical enablers to improving the overall audit outcomes in the province.

5.4 KWAZULU-NATAL

PROVINCIAL SNAPSHOT

Clean audits: 11% ▼
(2015-16: 20%)

Quality financial statements: 74% ▼
(2015-16: 88%)

Quality performance report: 47% ▼
(2015-16: 71%)

No findings on compliance with legislation: 11% ▼
(2015-16: 20%)

Irregular expenditure: R2 449 m ▼
(2015-16: R2 071 m)

We continued to highlight the importance of accountability in our messages to leadership following the August 2016 local government elections. We emphasised that the newly elected councils should implement specific actions to improve audit outcomes as well as that the leadership should regularly monitor these actions to increase accountability and consequences for transgressions at all levels, and to instil a culture of financial discipline and prudence. The audit outcomes again demonstrated complacency and a lack of commitment by leadership to decisively address key matters of concern and to follow through on undertakings made by former accounting officers and councils. The results of these accountability failures are described in the paragraphs below.

The regression in the 2016-17 audit outcomes confirms that leadership did not embrace accountability for key internal controls and monitoring of action plans with vigour and diligence to achieve credible and reliable reporting. A concerning regression was Msunduzi, which moved from a clean audit in 2014-15 to a disclaimed opinion in 2016-17. This municipality was characterised by a leadership and senior management team that paid little attention to the importance of key internal controls as well as the timely resolution of important audit matters. Another regression from a clean audit, in this case to a qualified audit opinion, was that of the consolidated audit of King Cetshwayo District, resulting from material misstatements due to a lack of sufficient evidence to support assets and expenditure at its municipal entity, Uthungulu Fresh Produce Market.

The outcomes are based on 54 municipalities (49 existing and five newly established municipalities) following the re-determination of municipal boundaries, which decreased the number of municipalities from the previous year's 61. The audit of one newly formed municipality, Inkosi Langalibalele, was not finalised by the cut-off date for inclusion in this report, as their financial statements were late and only received on 15 December 2017. Insofar as the other new municipalities are concerned, Alfred Duma received a qualified audit opinion, both Dr Nkosazana Dlamini-Zuma and Big Five Hlabisa received unqualified audit opinions with findings, and Ray Nkonyeni received an unqualified audit opinion with no findings (clean audit).

We do not include the outcomes of any of the municipal entities in this report, but they are published in the annexures available on our website. Although the number of clean audits would have increased from 11% to 19% by these inclusions, the overall results for the province would still have reflected a regression.

Our messages during leadership and senior management engagements at municipalities that regressed focused on basic internal controls. These controls were compromised by ineffective operational policies and procedures as well as instability and vacancies in accounting and chief financial officer positions. Moreover, we experienced challenges as municipalities obtained their own legal opinions that did not agree with our accounting and legal interpretations. This delayed audit responses, as there was provincial leadership pressure to improve outcomes. The time taken by senior management to adequately implement action plans and recommendations to allow for remedial steps to be instituted swiftly, continued to hamper progress and caused the majority of the regressions.

The continued reliance on auditors to identify errors in the financial statements remains a concern. A total of 24 municipalities (45%) avoided qualifications only because they corrected the material misstatements that we identified during the audit process. The nature of the misstatements in financial reporting demonstrated a lack of understanding by key officials and support staff on what they needed to do. In addition, daily and monthly activities undertaken by key support staff were not closely supervised and reviewed. Many municipalities remained reliant on consultants at a cost of R93,9 million (2015-16: R132,9 million) for financial reporting, mainly as a result of a lack of skills. Of the 39 municipalities that made use of consultants, 17 still required material corrections in areas that were within the consultants' scope of work. The recurring appointment of consultants indicates that skills are not transferred to officials due to inadequate monitoring and also contributes to lower levels of accountability in the financial reporting cycle.

There was a lapse in the reporting of performance information, as 28 municipalities (53%) had material findings in the year under review compared to 14 municipalities (29%) in the previous year. There was also a significant regression of 24% in the quality of performance reports produced. Weak records management, inadequate standard operating procedures and a poor understanding of the required documents to support reported performance resulted in performance reports not being useful and reliable.

Material findings on compliance increased in the year under review. In addition to the poor quality of submitted financial statements, the prevention of unauthorised, irregular and fruitless and wasteful expenditure as well as non-compliance with procurement processes remained as key areas of non-compliance.

Accountability failures continued to be reflected in the high levels of irregular expenditure and the lack of effectively enforcing consequences

The levels of irregular expenditure continued to balloon despite the warning signals we raised with accounting officers to implement appropriate preventive and detection measures. eThekwini Metro, KwaDukuza and Umzinyathi District were responsible for R1 billion (41%) of the total irregular expenditure incurred in 2016-17. Of the total irregular expenditure of R513 million incurred by eThekwini Metro, R386 million was due to the awarding of a contract for the construction of housing units that was not adjudicated by the bid adjudication committee. We identified that R379 million (38%) of the irregular expenditure at the above three municipalities related to mainly multi-year construction contracts. The new councils at these municipalities made little effort to prevent repetitive multi-year irregular expenditure.

Municipalities continued to abuse supply chain management regulation 36, as deviations from competitive bidding and quotation processes were not supported and the emergency criteria were incorrectly applied. In addition, suppliers were awarded contracts without providing tax clearance and broad-based black economic empowerment certificates, while local content thresholds were also not applied. The province had a cumulative closing balance of R7 billion in irregular expenditure, which had not yet been dealt with or was in the process of being dealt with by municipal councils. Where councils did not investigate non-compliance related to unauthorised, irregular and fruitless and wasteful expenditure, it could result in possible financial losses through excessive expenditure (uneconomical use of funds). This trend will persist if not vigorously addressed.

Most grant funding was used with no significant underspending, with the exception of Msunduzi that materially underspent the public transport development grant by R165 million (45%) due to delays in appointing contractors. Although most of the municipalities achieved their planned targets for the municipal infrastructure grant, nine did not achieve targets although they had spent most of the grant funding. These included Umkhanyakude, Harry Gwala and Uthukela district municipalities that are responsible for the provision of water and sanitation to underdeveloped rural areas. These district municipalities were plagued by budget constraints and poor project management, which included the late appointment and poor monitoring of contractors. Delays in the maintenance and development of water and sanitation infrastructure contributed to service delivery protests by citizens in these districts.

Although road infrastructure was being developed, we identified two instances at Alfred Duma and Umngeni where payments were made to contractors for incomplete roads. This was due to management not adequately monitoring these projects. In addition, many local municipalities struggled with the implementation of effective road asset management practices. In this regard, policies and project plans for road renewal and maintenance were not applied due to poor budgeting and project management disciplines, resulting in deteriorating road infrastructure.

eThekwini Metro – with a R36,7 billion budget, being the largest share of the total local government budget – had no material findings on their performance report. Projects with a total value of R5,8 billion for the western and northern aqueduct, ablution in-situ upgrade and integrated rapid public transport infrastructure system were progressing well and should significantly improve the lives of citizens when completed. Good practices implemented by the metro included regular monitoring of projects and monthly inspections of sites. Necessary action was taken for inferior work and payments were withheld and/or contracts were terminated when contractors defaulted.

Financial health remained a challenge, with material going concern uncertainties reported at 10 municipalities (19%). Key factors affecting financial health were poor debt-collection practices and reduced revenue flows due to water restrictions at municipalities affected by the severe drought conditions. The extended debt-collection periods placed the cash flow of municipalities under strain and many failed to pay money owed within 30 days, as required by legislation. This contributed to R20 million of the fruitless and wasteful expenditure incurred due to interest and penalties. In most cases, however, municipalities did pay Eskom debts on time to ensure the continued supply of essential services to communities.

A major obstacle to municipalities improving their information technology management was a lack of technically skilled individuals to support the information technology systems and infrastructure in use. Municipalities continued to experience challenges with vacancies in information technology positions, system functionality limitations, adherence to established information technology controls, and resolving prior year information technology audit findings. Although most municipalities made use of the National Treasury's transversal tender, we are concerned about the 30 municipalities (57%) that had control weaknesses as well as the three municipalities (6%) that did not demonstrate readiness for the implementation of the Municipal Standard Chart of Accounts. This was despite R64 million having been spent on consultants at 28 municipalities to manage the Municipal Standard Chart of Accounts migration process.

The provincial treasury and the provincial cooperative governance department continued to support municipalities with the implementation of the municipal support and back-to-basics programme.

However, the premier's coordinating forum and the provincial cooperative governance department's operation clean audit meetings need to be more effective to support municipalities. A new director-general was appointed on 1 August 2017, after a two year vacancy, which should further assist in the coordination of the planned support initiatives to promote intergovernmental relations and good governance. Although some progress was made in honouring the commitments by the coordinating departments, their efforts did not have the desired impact. This was mainly due to poor planning and inadequate support provided by these departments to facilitate a smooth transition between the former and new councils.

We had several interactions with stakeholders to improve accountability, which included discussing our management reports and audit reports with accounting and chief financial officers, speakers, municipal public accounts committees and councils. Our engagements also included an in-depth review of the status of municipal records to identify challenges and warning signals. These engagements were well received by accounting officers for purposes of risk identification and rigorous monitoring of action plans with a view to respond proactively to key areas of concern.

Accountability failures had a major impact on the local government outcomes in the province and will continue indefinitely if not addressed by leadership and those charged with governance. Where material irregularities occur, such as the bypassing of the supply chain management process leading to financial losses, the extension of our mandate to refer such matters will assist in restoring public confidence and solidifying accountability and ethical behaviour.

The political leadership and senior management need to own the business of local government and be accountable for their actions and those delegated to their subordinates to curb the regressions and address the root causes of unfavourable audit outcomes. Consequences must be enforced for officials who fail to comply with applicable legislation and strict corrective action must be taken against transgressors. The understanding and application of policies and procedures need to be entrenched in daily and monthly activities through appropriate reviews, monitoring, corrective action and credible reporting by designated officials. The adequate transfer of skills and succession planning are also vital because it can be expected that officials change over time. Risk management and internal control are integral parts of a financial, performance management and compliance system and crucial to the achievement of favourable outcomes. A strong system with combined assurances from internal audit units and municipal public accounts committees is essential to ensure the implementation of government policies and the achievement of intended outcomes. This will enforce financial discipline, strategic allocation of resources, efficient service delivery, and accountability.

5.5 LIMPOPO

PROVINCIAL SNAPSHOT

Clean audits: 0% ►
(2015-16: 0%)

Quality financial statements: 39% ▼
(2015-16: 57%)

Quality performance report: 13% ▼
(2015-16: 14%)

No findings on compliance with legislation: 0% ►
(2015-16: 0%)

Irregular expenditure: R1 317 m ▲
(2015-16: R1 324 m)

The province's audit outcomes regressed with no single auditee being able to improve their audit outcome. Auditees with unqualified audit opinions decreased, while disclaimed opinions increased and adverse opinions remained the same. We reported in the 2015-16 general report that the premier had made a number of commitments to deal with poor-performing municipalities in his state of the province address and in our engagements with him. Unfortunately, these were not followed by the required actions to turn around the declining state of good governance in the province.

At the cut-off date of 15 January 2018 for inclusion of outcomes in this report, there were four outstanding audits, namely those of Greater Giyani, Mogalakwena, Thabazimbi, and Modimolle-Mookgophong. The financial statements of Greater Giyani were received by the legislated date but the audit could not be finalised by the reporting date of 30 November due to poor data-migration controls when the municipality was implementing the Municipal Standard Chart of Accounts, which had a significant impact on the quality of the financial statements. We received the financial statements of Mogalakwena after the legislated deadline. We subsequently completed these audits with both auditees obtaining adverse audit opinions. Thabazimbi and Modimolle-Mookgophong had not yet submitted their financial statements at the cut-off date for inclusion in this report.

The 2016-17 audit outcomes represent the results of the first cycle of the newly elected councils following the local government elections in August 2016. The boundary re-determinations saw a new municipality being established (Collins Chabane) as well as the mergers of Fetakgomo and Tubatse, and Modimolle and Mookgophong. Aganang and Mutale were disestablished, with Aganang being incorporated into Polokwane and Blouberg, and Mutale into Collins Chabane, Thulamela and Makhado. The overall impact was a reduction in the number of municipalities from 30 to 27, made up of five district municipalities and 22 local municipalities.

We gave a presentation on our role as well as the importance of the new deliverables in the accountability cycle during the councillor induction programme of the South African Local Government Association. Our message to the new councillors focused on the importance of instilling good governance practices that would ensure accountability at municipalities. We shared the poor state of financial management practices in local government, which had resulted in the province not achieving a clean audit outcome since 2011-12. We further emphasised concerns over the high dependency on consultants for financial reporting; the failure to fill critical vacancies timeously leading to a lack of ownership by those appointed in acting positions; and the high levels of unauthorised, irregular as well as fruitless and wasteful expenditure without adequate consequences. We recommended to the new leadership that they should hold officials accountable through the development of sound and robust internal controls to ensure that there is an improvement in the province's overall audit outcomes and ultimately in the service delivery to communities.

The municipalities did not take our repeated recommendations and warnings seriously, resulting in the province reporting five regressions, with no improvement in the audit outcomes. These outcomes were as a result of the failure by the first-level assurance providers (senior management, municipal managers and mayors) to develop strategies to address deficiencies in the internal control environment, implement effective action plans to address the root causes of poor audit outcomes, and use effective cash-management practices. This was made even worse by the failure of the second and third level of assurance providers to rigorously review the information submitted through the effective use of internal audit units, audit committees and municipal public accounts committees; and to ensure that there were consequences for those officials responsible for transgressions and poor performance.

The provincial outcomes can be categorised into three classes:

1. Complacent auditees consistently receiving unqualified opinions with findings, without any improvement in internal controls to address shortcomings in the areas of performance reporting and compliance. These municipalities lacked the will to move to a clean audit status.

2. Underperformers that continue to receive qualified audit outcomes because of their failure to deal with repeat qualifications.

3. Consistent poor performers with high levels of transgressions and no consequences.

None of the auditees could submit financial statements that were free of material misstatements. The province spent R96 million (2015-16: R93 million) on consultants for the preparation of financial statements, but the quality thereof remained consistently poor. Seven of the nine auditees that obtained unqualified audit opinions made use of consultants at a total cost of R25 million, with Sekhukhune District incurring the highest consultant cost at R15 million (60%). Auditees that obtained qualified audit opinions spent R52 million on consultants in total, with Polokwane contributing the most with R19 million (37%); while municipalities with adverse or disclaimed opinions spent R19 million, with Vhembe District being responsible for most of this amount at R13 million (68%). It is encouraging that Makhudutamaga and Musina obtained unqualified opinions with findings without making use of a consultant. This proves that basic financial reporting disciplines that lead to reliable financial reporting can be developed and sustained. The return on investment of expenditure on consultants in the form of reliable reporting and a reduction in the number of qualified municipalities is concerning, while the use of consultants has also not led to an improvement in the basic internal controls. The cumulative amount spent on consultants to assist with financial reporting over the past three years exceeded R290 million.

Only three of the 23 auditees, namely Waterberg District, Maruleng and Molemole, had no findings on either the usefulness or the reliability of their reported performance information. Of these three, only Maruleng did not require adjustments to their performance report to achieve this. Until standardised key performance indicators for basic service delivery are developed, and the collation and record keeping of information for performance reporting are improved, municipalities will continue to have findings on performance information. Generally, the level of service delivery in the province needs to be improved, as evidenced by the various service delivery protests that took place during the year under review.

The level of unauthorised, irregular as well as fruitless and wasteful expenditure remained very high at R1,1 billion, R1,3 billion and R243 million, respectively. Poor planning, budgeting and expenditure controls were at the root of the continuous incurrence of unauthorised expenditure – of which more than 50% related to non-cash items such as depreciation and the impairment of receivables. This was the result of municipalities not considering the actual costs reported in previous years when budgeting, as well as a lack of a deeper understanding and analysis of cost drivers. Vhembe District incurred the highest amount at R375 million, of which R250 million related to non-cash items. The unauthorised expenditure on cash items amounted to R125 million – most of which was incurred on water-related expenditure that had not been adequately budgeted for.

As a result of accountability failures, irregular expenditure on supply chain management transactions remained high at R1,3 billion (95%) of the total irregular expenditure incurred. The highest contributors to the irregular expenditure were Sekhukhune District, Vhembe District and Polokwane, which incurred R333 million, R226 million and R199 million, respectively, totalling R758 million. Of this amount, R326 million was from multi-year contracts and R432 million was incurred under the new administration. The nature of the transgressions remained the same as in previous years. Mopani District and Vhembe District – the consistent poor performers with repeat adverse or disclaimed audit opinions – had an accumulated irregular expenditure closing balance of R186 million and R882 million, respectively. These two district municipalities did not appropriately investigate the irregular spending, resulting in none of the money being recovered from the liable persons or written off by the council. In this regard, the underlying root cause was the lack of corrective action by the first level of assurance providers and the failure by third-level assurance providers to implement a culture of accountability and consequences through investigating transgressions, particularly relating to the procurement of goods and services. Furthermore, all auditees had findings on compliance with laws and regulations. Both the political and the administrative leadership need to have action plans that deal directly with non-compliance to move municipalities out of this state of lawlessness.

Municipalities also did not consistently apply the principles of sound project management, as evident by the fact that we raised 34 findings on 54 key projects selected for testing relating to the municipal infrastructure grant. Shortcomings included planned targets for projects not being achieved (13), incorrect performance reporting (seven), performance of the project not being evaluated (six), non-compliance with supply chain management prescripts (six), and misstatements relating to the incorrect reporting of achievements (two).

There is no use in having action plans without them being implemented, validated and monitored – the current trend is taking the province backwards

The financial health of municipalities slightly regressed from the previous year and continued to be a concern. The inability of municipalities to collect money owed for services rendered is an ongoing challenge. Twelve auditees could not collect debts owed to them within 90 days. Seventeen auditees had to significantly impair their receivables balance due to doubt over the recoverability of these amounts. Municipalities struggled to effectively manage their working capital, with four municipalities being in a net current liability position and eight municipalities having creditors balances greater than the actual cash on hand. At Musina, the creditors balance as a percentage of cash and cash equivalents was a staggering 16 021%. The provincial treasury had to intervene and provided additional funding to settle debt owed to creditors at Musina (R10 million to Eskom) and Thabazimbi (R25 million, including Eskom debt) as at 30 June 2017.

The information technology audit outcomes improved due to the inclusion of information technology matters in the action plans. The province saw an improvement in the four information technology focus areas of governance, security management, user access management, and service continuity. The key information technology initiative carried out by municipalities was system upgrades and/or replacements in preparation of financial systems that would comply with the Municipal Standard Chart of Accounts, with the aim of quality data on which to base budgets and financial statements. However, most municipalities did not follow the project implementation guidelines, resulting in poor change management processes. This was quite evident at Greater Giyani where we were unable to complete the audit in time as mentioned earlier, due to the poor quality of the financial statements. Failure by municipalities to urgently and effectively manage this transition could result in their audit outcomes regressing in the next financial year.

We noted a number of new initiatives being implemented by the coordinating departments and the South African Local Government Association to improve financial and performance reporting as well as the compliance levels at municipalities. We are pleased to note the launch of a provincial municipal public accounts committee forum by the provincial cooperative governance department. This forum aims to promote capacity building for municipal public accounts committee members to better equip committees in improving service delivery and municipal performance, and – more importantly – holding municipalities accountable for the use of municipal funds. The initiatives previously developed had limited or no impact due to a lack of commitment to rigorously implement these initiatives and develop sound monitoring mechanisms to evaluate the progress made. Both the political and the administrative leadership should commit to taking part in developing, managing and monitoring such initiatives to bring them into fruition.

Our office is implementing status of records reviews at all municipalities. These reviews will replace the previous quarterly key control discussions and are aimed at providing municipal managers and mayors with tools to proactively address significant risks. Through these reviews, we will be able to identify key risks that may derail the auditee towards achieving improved audit outcomes, assess progress made on the implementation of action plans, and follow up on leadership commitments.

There has been a general call for greater accountability to deal with the recurring findings we report, which could come about through amendments to the Public Audit Act. We believe that these amendments, once approved, will have a positive impact on dealing with issues of recovery where losses have been suffered and on enforcing consequences and accountability against officials responsible for such losses. We encourage leadership in the province to ensure that a culture of accountability is cultivated that will ensure that all levels of management and leadership accept responsibility for improving audit outcomes. We are also of the belief that once better audit outcomes are achieved, it will lead to better service delivery in the province.

5.6 MPUMALANGA

PROVINCIAL SNAPSHOT

▼ **Clean audits: 10%** (2015-16: 16%)

▲ **Quality financial statements: 65%** (2015-16: 47%)

▲ **Quality performance report: 40%** (2015-16: 37%)

▼ **No findings on compliance with legislation: 10%** (2015-16: 16%)

▼ **Irregular expenditure: R1 996 m** (2015-16: R1 467 m)

In its first year, the new administration of the Mpumalanga local government saw an improvement in the 2016-17 audit outcomes. There has been a notable improvement in the reduction of disclaimed audit opinions over the past three years from four municipalities to only one; as well as a reduction in the number of qualified audit opinions in 2016-17.

Notwithstanding this good progress, improvements in audit outcomes as well as in the quality of financial statements were often as a result of over-reliance on the audit process to identify misstatements and thereafter make corrections to the submitted financial statements. This is an indication that daily accounting disciplines have still not been institutionalised. Over the past years, we have highlighted the following indicators of accountability failures and urged management, leadership and oversight to take actions that would stimulate sustainable good governance:

- Weakening internal controls around basic financial, performance and project management due to the slow response by management to implement sustainable long-term solutions.

- Reliance on consultants with little or no monitoring and transfer of skills, instead of stabilising the municipalities by filling key positions and investing in training programmes to enhance skills and competencies of staff.

- Lack of commitment to prevent, or deal with the accumulated balances of, unauthorised, irregular and fruitless and wasteful expenditure as well as management failure to implement recommendations and resolutions of the various assurance providers, such as internal audit units, audit committees and municipal public accounts committees, due to leadership not implementing consequences for poor performance and transgressions.

These indicators of accountability failures continued to prevail in the year under review. Even the envisaged benefits one would have expected from the amalgamation of Mbombela and Umjindi, being the improvement of managerial effectiveness to improve service delivery, had not yet been realised. The new City of Mbombela retained the same unqualified audit outcome with findings on service delivery reporting against predetermined objectives. Furthermore, we saw the regression of Steve Tshwete from a clean audit status to an unqualified opinion with findings on compliance with legislation.

As a result of these accountability failures, only two municipalities (10%) – which managed 4% of the local government budget in the province – produced credible financial and performance reports and complied with key legislation, while municipalities entrusted with 96% of the budget failed to achieve clean audits. Furthermore, only eight (40%) of the municipalities had quality performance reports. However, the usefulness of the information in these reports slightly improved from nine (47%) to 11 (55%) municipalities, while 12 municipalities (60%) still struggled to report reliably on service delivery. This indicates that municipalities prepared performance reports merely to comply with legislation rather than to use these reports as tools to measure performance, ensure clear accountability, and continually improve reporting on service delivery. There is also a risk that the in-year monitoring, oversight and decision-making processes might have been based on information that was not credible, which might explain the negative impact on service delivery in some areas of the province.

In addition, municipalities reported underperformance on their planned projects. Of the R1,9 billion municipal infrastructure grant allocation, R128 million (7%) was not spent – mainly due to delays in procurement processes and disputes with contractors. A total of 17 municipalities were responsible for the delivery of water, sanitation and road services in the province. We selected 46 key projects at these municipalities for auditing, of which 15 (33%) were not awarded in accordance with supply chain management regulations and prescripts; and 20 (43%) were behind schedule and did not meet their planned target dates. We also noted poor quality workmanship at some of the projects, which is an indication of potential fruitless and wasteful expenditure.

The upgrading of the Embalenhle X18 sewer reticulation network project in Govan Mbeki costing R25 million, is an example of the delays and poor workmanship highlighted above. The project was abandoned for two years due to the contractor's inability to perform the work, yet the contract with the contractor was not terminated. This meant that the municipality could not appoint another contractor to rectify the defects and complete the project. The effect of these delays was that the infrastructure already installed did not function properly, resulting in sewage flowing in the streets and between houses in the township.

The province still struggled to improve the management of procurement and contracts; and to prevent unauthorised, irregular and fruitless and wasteful expenditure. The irregular expenditure for the current year increased to R1 996 million (of which R1 989 million related to non-compliance with supply chain management legislation) from R1 467 million in the previous year. We noted numerous examples of the inappropriate exercise of management's discretion to deviate from the normal procurement processes and to allow multiple extensions of contracts without following the legislated processes, which are meant to ensure fair, equitable and transparent procurement. There was also an increasing trend of not properly applying local content requirements to source a certain percentage of intermediate goods used in the production processes from domestic manufacturers.

Daily financial disciplines had still not been institutionalised

Bushbuckridge and City of Mbombela continued to be the highest contributors to irregular expenditure in the province with R493 million and R348 million, respectively, joined in 2016-17 by Mkhondo with R236 million. A total of 70% of the irregular expenditure for the current year related to multi-year contracts, which were awarded irregularly in previous years. Despite our efforts to proactively engage with municipal managers and mayors during our quarterly interactions on the process to deal with the irregular expenditure balance, they have been slow in investigating such irregular expenditure. In addition, R523 million of the 2016-17 closing balance (R6 459 million) of irregular expenditure was as a result of the use of the provincial supplier database with Rand Water as the implementing agent, three years ago, to fast-track the construction of water infrastructure. This R523 million has not yet been investigated even though it has been at the centre of our engagements with the provincial leadership.

The information technology environment improved, with four municipalities implementing sound information technology controls as compared to none in 2015-16. While we welcome this improvement, shortcomings in the information technology environment at 16 municipalities (80%) in 2016-17 should not be ignored, as poor information technology controls increase the risk of fraud and data manipulation, which can affect the credibility of information used for decision-making. In addition to the information technology challenges identified, the implementation of the Municipal Standard Chart of Accounts on 1 July 2017 will have an impact on how information is recorded and classified if this project is not properly executed. Only Nkangala District and City of Mbombela were ready for full implementation; 13 municipalities experienced challenges with implementation specifically relating to the payroll function, assets and inventory management; and five municipalities were not ready for implementation by 1 July 2017 as they had major challenges, most notably with billing. Six municipalities (30%) used consultants at a cost of R8,8 million for information technology services, including Municipal Standard Chart of Accounts implementation.

We advised the provincial treasury to remind the leadership to direct concerted effort and attention to addressing all Municipal Standard Chart of Accounts implementation risks (including the monitoring of the consultants who are assisting with the project) so as not to jeopardise the credibility of the financial records.

The financial health of the municipalities in the province keeps deteriorating each year. To illustrate, 15 (75%) of the local municipalities were unable to settle their liabilities when they fell due. Nine municipalities continued to spend more than their available resources, thus incurring a net deficit. The financial situation of five of the municipalities became severe, as they continued to owe significant amounts to their creditors, including R2,3 billion to Eskom as at 30 June 2017. The province already had to intervene to prevent disconnection by major suppliers such as Eskom and the national Department of Water and Sanitation. This led to some municipalities (for instance, Emalahleni and City of Mbombela) entering into payment plans with the suppliers to enable the continued delivery of basic services.

This poor state of financial health also has a negative impact on the province meeting its socio-economic goals. As a consequence, the province experienced excessive water and electricity distribution losses of over R1 258 million due to aging infrastructure assets, unmetered sites, and illegal connections. As we have been doing over the past few years, we again warned leadership to take immediate actions to address this situation.

The effects of financial constraints were particularly visible at City of Mbombela and Govan Mbeki where delays in payments to service providers resulted in delays in the finalisation of projects. This caused major damage to existing municipal property through violent service delivery protests. Linked to the state of financial health indicated above, is municipalities' inability to budget properly – which led to unauthorised expenditure of R1 333 million in 2016-17. Non-cash items such as depreciation and impairment continued to contribute to the unauthorised expenditure. Despite the fact that unauthorised expenditure slightly decreased from R1 650 million in 2015-16, this will continue to put pressure on the province's severely constrained cash flow.

We continue to urge the political leadership of the province to focus on instilling stability at local government level. Municipal managers and chief financial officers were often rotated among municipalities, some even during the audit. Together with political tensions in some cases, this disrupted the effectiveness of municipal administration – including the audit process. During our interactions, some of the mayors expressed concern that the deployment system delayed appointment processes. Most municipal public accounts committees, which are tasked with oversight responsibilities, still did not have adequate capacity and resources to fulfil these responsibilities. This has been at the centre of discussions at meetings of the speakers' forum; however, municipal councils have been very slow to address this matter. This negatively affected the effectiveness of the oversight these committees provide.

While we acknowledge the efforts by the provincial treasury to assist municipalities, this support is mainly reactional in response to errors we identify during the audits. Going forward, the provincial treasury needs to consider proactive mechanisms to make sure that their support to municipalities is effective. The portfolio committee responsible for cooperative governance and traditional affairs in the province should evaluate the impact of its oversight visits to the three districts to conduct hearings on underperforming municipalities and follow up on the implementation of the resolutions taken at those hearings.

We take note that the provincial leadership consistently expressed their intolerance for poor audit outcomes, especially the disclaimed audit outcomes. However, this must include setting the right tone for solid ethical behaviour that will support a responsible, accountable, effective and efficient local government system. The unintended consequences of the said intolerance coupled with accountability failures were dire during the 2016-17 financial year, as they led to unethical behaviour by some municipal officials. All these instances, which we reported to the leadership of the respective municipalities, put pressure on the audit process.

As part of our continuous contribution to accountability and good governance in the public sector, we introduced the status of records review and implemented this project at three municipalities in the province. Our efforts produced positive results at Emalahleni, where the municipality has already started implementing our recommendations in preparation for the 2017-18 year. Although progress may be slow, we are hopeful that as we continue engaging with all municipalities, this initiative will translate into even more positive audit outcomes in 2017-18 – provided that our recommendations are implemented. Furthermore, if the proposed amendments to the Public Audit Act are approved, we will be able to refer cases for further investigation when accounting officers do not deal with some of the issues we raise during our audits, such as unauthorised, irregular and fruitless and wasteful expenditure. Had the Public Audit Act amendments already been effected in 2016-17, at least three municipalities could possibly have been referred, as the accountability mechanisms at these municipalities had failed. We continue to urge the collective leadership in the province to deal decisively with the accountability failures by stabilising local government and implementing consequences. This will not only improve audit outcomes but will have a positive impact on service delivery in the province.

5.7 NORTHERN CAPE

PROVINCIAL SNAPSHOT

▼ **Clean audits: 3%**
(2015-16: 7%)

▲ **Quality financial statements: 48%**
(2015-16: 46%)

▲ **Quality performance report: 24%**
(2015-16: 17%)

▼ **No findings on compliance with legislation: 4%**
(2015-16: 8%)

▲ **Irregular expenditure: R261 m**
(2015-16: R457 m)

The stagnated audit outcomes of local government in 2016-17 confirm that the previous year's commitments by the provincial oversight to ensure the clearing of prior year findings, promote a culture of oversight and increase the level of oversight with a focus on supply chain management, were not sufficiently implemented. The stagnation also confirms that our previous year's message that mayors, municipal managers and senior management need to hold each other and their subordinates accountable, was not taken seriously, resulting in many instances where similar findings were raised during the audit process.

The key root causes that contributed to these failures were inadequate consequences for poor performance and transgressions (80% [2015-16: 83%]), the slow response by management (80% [2015-16: 75%]), and the slow response by the political leadership (72% [2015-16: 71%]). The results of these accountability failures are outlined below.

A number of municipalities submitted their financial statements after the legislative deadline. This does not only have a knock-on effect on the completion of the audits of these municipalities, but also on the work of the various oversight bodies that rely on the audit reports to perform their duties. The late submission of financial statements by six municipalities (Kai !Garib, Kgatelopele, Phokwane, Renosterberg, Tsantsabane, and Ubuntu) resulted in their audits not being finalised in time for inclusion in this report.

Despite previously raising concerns about the quality of the financial statements, only ZF Mgcawu District (4% [2015-16: 25%]) was able to submit quality financial statements in the year under review. We had also previously highlighted the fact that most municipalities relied heavily on the external auditors to identify misstatements in their financial statements. The regression in 2016-17 confirms that leadership did not respond to the matters we had raised in 2015-16, and that municipalities had still not implemented controls that were supposed to ensure the quality of financial statements submitted for auditing. Municipalities spent R70 million on consultants for financial reporting (excluding consultants paid by other institutions), compared to R36 million in 2015-16. Worryingly, the financial statements of 54% of the 24 municipalities that used consultants for financial reporting were still disclaimed or qualified.

Predetermined objectives remained an area where progress was lacking, with 76% of the municipalities (2015-16: 83%) being unable to produce performance reports that were useful and reliable, indicating that there was a lack of capacity and understanding of the performance reporting process. These constraints were further evidenced by the fact that none of the municipalities were able to submit quality performance reports for audit purposes, as all the municipalities were left with material misstatements or made amendments to avoid material findings.

We remain extremely concerned about the status of compliance with legislation by municipalities in the province. A total of 96% of the municipalities (2015-16: 92%) had material findings due to non-compliance with legislation. This was the one audit area that had been in a dire position for a long time and leadership continued to ignore the need to hold staff accountable. Municipal managers need to prioritise the enforcement of accountability where officials allow non-compliance, as they are currently not dealing decisively with offenders. The most common compliance findings related to the quality of financial statements submitted for auditing (96%); preventing unauthorised, irregular and fruitless and wasteful expenditure (88%); and the management of procurement and contracts (80%).

Irregular expenditure decreased from R457 million in the previous year to R261 million in the year under review. Of the R261 million, R105 million (40%) related to multi-year contracts that were reported as irregular expenditure in 2015-16 as well. A total of 97% of the irregular expenditure in 2016-17 resulted from instances of non-compliance with supply chain management regulations. The most common supply chain management areas on which we raised findings related to procurement without competitive bidding or quotation process (56%) and non-compliance with the procurement process (42%). Despite the decrease in the amount of irregular expenditure, the number of municipalities incurring such expenditure remained high at 80% (2015-16: 83%). Fourteen municipalities were still investigating the full extent of their irregular expenditure, meaning that the R261 million disclosed as irregular expenditure in 2016-17 was in all likelihood understated. It is probable that a large portion of irregular expenditure may be uncovered and still be disclosed in future years.

During the year under review, municipalities wrote off or condoned irregular expenditure amounting to only R110 million. The fact that there was only one insignificant instance where irregular expenditure was recovered from the liable person indicates that investigations either are not taking place or are not rigorous enough to resolve the significant balance of irregular expenditure recorded by the province. This lack of accountability and consequences was consistently reported in previous years, but no progress had been made in this regard.

The level of unauthorised expenditure increased since the previous year and amounted to R1 034 million (2015-16: R713 million) – all of which was due to budget overspending, with 70% relating to non-cash items that had not been budgeted for. Gamagara again incurred the most unauthorised expenditure in the province, amounting to R374 million (2015-16: R179 million). In addition, the level of fruitless and wasteful expenditure again increased and amounted to R54 million (2015-16: R33 million). Of the R54 million, 94% related to interest and penalties mainly due to the late payment of suppliers, including Eskom, water service providers and the South African Revenue Service.

The financial well-being of the province remained a concern, with a material uncertainty regarding the financial health of 56% of the municipalities (2015-16: 50%). The cash-flow difficulties experienced by many municipalities were evident from the fact that 13 municipalities (65%) struggled to pay Eskom, while six (30%) were struggling to pay water service providers. The electricity was cut at four municipalities (20%) during the year and three of them subsequently entered into payment arrangements with Eskom to avoid further cuts, while seven (35%) avoided electricity cuts by making payment arrangements with Eskom from the start.

The audit outcomes are a reflection of the poor state of internal controls, with only 4% of municipalities (2015-16: 8%) being assessed as having good leadership and good financial and performance management controls. Improved audit outcomes that are sustainable will only be possible if they are based on a strong internal control environment characterised by regular monitoring and review as well as leadership holding staff accountable for their actions. It is worrying that the first level of assurance (made up of senior managers, the municipal manager and the mayor) of only one municipality (4%) provided the necessary assurance. Overall, the level of assurance provided by all three levels of assurance providers showed little movement, with internal audit units being the only assurance provider that regressed. Municipal managers and senior managers need to monitor the effectiveness of internal controls as well as consider the status, functioning and capacity of internal audit units and ensure that their findings are responded to.

As part of our audits, we assessed progress on infrastructure projects as well as infrastructure maintenance.
This assessment focused on key municipal infrastructure projects currently underway, and highlighted the following concerns:

- Water losses were not disclosed (85%) or resulted in a qualification (10%).

- 75% of the municipalities did not have a plan for the maintenance of water infrastructure that set specific time frames and targets.

- Planned targets or key milestones were not achieved at 50% of the municipal infrastructure grant projects.

- 50% of the municipalities did not perform an assessment of the condition of water infrastructure.

- 45% of the road projects were completed later than planned.

The above findings confirm the need for better budget management, project planning and progress monitoring to ensure the timely delivery of quality municipal services.

The implementation of the Municipal Standard Chart of Accounts, aimed at improving financial reporting, was set to be finalised by 1 July 2017. Municipalities made use of external service providers to implement systems that would comply with this chart of accounts. Overall, 16 municipalities (64%) implemented the Municipal Standard Chart of Accounts by the deadline, with another two (8%) subsequently implementing it. However, we are worried about the seven municipalities (28%) that had not implemented it to date. This concern is made even worse by the fact that five (20%) of these municipalities were unable to confirm their planned implementation date.

As an office, we have been influencing improved audit outcomes by preparing management reports that clearly highlight the various weaknesses at municipalities. Our reports are not limited to findings, but include root causes as well as recommendations. During the audits, we invest time on explaining the various findings to our auditees, thereby ensuring that all findings are properly understood and that management has a clear view on what needs to be done to address the findings.

Leadership's inaction created a culture of 'no consequences'

The provincial treasury assisted by seconding staff to struggling municipalities, and helping with Municipal Standard Chart of Accounts readiness assessments and data cleansing. These efforts assisted some municipalities in improving in specific areas, but the initiatives of the other oversight departments did not have a meaningful impact on the audit outcomes. The premier's office drove the process to ensure that a memorandum of agreement to coordinate the efforts of the provincial treasury and the provincial cooperative governance department was developed, but the late implementation of this agreement meant that little progress was made on previous commitments made by provincial role players.

We briefed the oversight departments on the outcomes of the audits after the completion of the audit cycle so that they could respond effectively to the issues raised. In addition, the municipal leadership gets the opportunity to interact with the auditor-general and senior leadership in the province during the annual Municipal Finance Management Act roadshow. During these sessions, municipal oversight and leadership also get the opportunity to raise any concerns they may have relating to the audit process. The above initiatives have not resulted in an improvement in the audit outcomes due to implementation delays at the various levels.

To improve audit outcomes and strengthen accountability in the province, the following should happen:

- The tone has to be set from the top (by senior managers, the municipal manager and the mayor) that there is zero tolerance for poor performance and transgressions.
- Municipal councils have to be fully capacitated to effectively exercise their oversight role.
- Municipalities should strive towards sound records management.
- The vigorous implementation and execution of action plans need to be at the forefront of all initiatives.

To further contribute to accountability in the province, we are phasing in status of records reviews at certain municipalities. This initiative identifies key areas of concern and serves as an early warning system to both management and the political leadership. Management has welcomed this initiative and was willing to engage with the auditors, but it is too early to measure the impact thereof. We will expand these reviews to all municipalities in our 2018-19 financial year.

The proposed amendments to the Public Audit Act will lead to stricter consequences where we identify instances that are likely to result in financial losses. The area that would be affected the most in the province is irregular expenditure, due to the substantial amount being reported every year without necessary and rigorous investigations taking place. Once accountability has been established, it will lead to improved audit outcomes that would hopefully have a positive effect on service delivery in the province.

5.8 NORTH WEST

PROVINCIAL SNAPSHOT

Clean audits: 0% ►
(2015-16: 0%)

Quality financial statements: 9% ▼
(2015-16: 19%)

Quality performance report: 9% ▼
(2015-16: 24%)

No findings on compliance with legislation: 0% ►
(2015-16: 0%)

Irregular expenditure: R4 294 m ▼
(2015-16: R3 186 m)

The North West province consists of 22 municipalities and three municipal entities. The number of municipalities changed from 23 to 22 due to the merger of Tlokwe City Council and Ventersdorp after the local government elections in August 2016. The overall 2016-17 audit outcomes for the province regressed, with the number of municipalities with financially unqualified opinions decreasing from four (19%) to two (9%) and the number with disclaimed opinions increasing from six (29%) to eight (36%). 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 who are 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 actions to hold officials accountable and implement consequences for poor performance.

Our audit environment has become more hostile, with increased contestations of audit findings, pushbacks and subtle threats by auditees where they would question the auditors' integrity. It is acceptable for auditees to question and challenge the outcome of audits based on evidence and solid accounting interpretations or legal grounds, but this trend pointed to the lack of accountability and was often a tactic to divert attention away from the fact that there were no grounds for factual disagreement with our findings. There were also two instances where community protests and strikes prevented our auditors from accessing the municipal premises for extended periods, which delayed our audits. The lack of accountability and consequences for the undesirable audit outcomes should have been a priority of the provincial executive leadership, as highlighted in the previous year's general report. Despite the continued reinforcement of our messages during the year through quarterly interactions with the leadership of municipalities and the province, there were no interventions to minimise key risks identified or to implement our recommendations. Most audit findings were repetitive in nature and no actions were taken to address the internal control deficiencies that resulted in these findings.

The vacancies and instability in key positions, which we identified as a root cause in previous years, were also not addressed. Twelve municipalities (55%) did not have a permanently appointed municipal manager and 14 (64%) did not have a permanent chief financial officer. The average overall vacancy rate at senior management level was 60%, with 16 municipalities having a senior management vacancy rate of 50% or more. The environment created by this high vacancy rate did not enable accountability, as the officials in an acting capacity lacked the authority to take the necessary actions. As highlighted in previous years, the province needs to invest urgently in building and retaining capacity in these key positions over the long term.

The poor quality of submitted financial statements remains one of our foremost concerns. All municipalities continued to rely on consultants to assist with the preparation of financial statements at a cost of R96,2 million (2015-16: R118,7 million), yet all the financial statements submitted for auditing still contained material misstatements. None of the municipalities in the province would have obtained an unqualified opinion, if we had not given them an opportunity to correct the misstatements identified during the audit process. Key controls that enable reliable and timeous financial reporting, such as proper record keeping and daily and monthly reconciliations, need to be institutionalised through effective training and ongoing monitoring to avoid relying on the auditors to identify misstatements after year-end. However, this will only be possible once vacancies in key positions have been filled.

There was a notable regression in the quality of the reported performance information, as 20 municipalities had material findings, compared to 18 in the previous year. If we had not allowed audit adjustments, 21 municipalities would have had findings on their performance information. Most municipalities were unable to provide supporting documents for their reported results, due to poor records management and a lack of institutionalised controls to timeously and reliably report on their performance.

Of the grant allocation of R2,3 billion to municipalities for infrastructure development, R194,8 million (8%) was not spent. Cash-flow constraints contributed to underspending, as in some cases the grant allocations were used to fund operational expenditure. Due to underspending in previous years, the National Treasury withheld an additional R296,1 million (2015-16: R466,1 million) in grant funding for the year under review. We audited 56 grant-funded projects in terms of the municipalities' key service delivery objectives and most of them were characterised by poor project management. Of these 56 projects, 28 (50%) were behind schedule or completed late. In 22 cases (39%), the reported achievement in the performance reports of the municipalities did not reflect the actual progress at year-end. One such project was the Rustenburg rapid transport system, with an estimated cost of R3 billion. Construction started in 2012 and the first phase of the project was expected to be completed by December 2016. However, phase 1C of the project was still only about 40% complete by June 2017. Records management for the project was a major concern and as a result we could not reliably measure the costs incurred to date. Another example is the upgrade of the wastewater treatment works at Tlhabologang in the Ngaka Modiri Molema region. The project started in 2011-12 and was initially expected to be completed in May 2014. As at June 2017, the budget had been increased to R106,4 million (from the original R67,8 million) but the upgrade was still not complete due to the service provider not having been paid, which led to the contractor suspending work.

All municipalities still had findings on compliance with legislation, specifically in the areas of unauthorised, irregular as well as fruitless and wasteful expenditure; procurement; and contract management. A further R4,29 billion (2015-16: R3,19 billion) in irregular expenditure was disclosed in the financial statements of the 22 municipalities for the year under review, bringing the total unresolved balance of irregular expenditure to R12,2 billion as at 30 June 2017. The three municipalities that contributed 55% in this regard were Rustenburg (R983,5 million), Ngaka Modiri Molema District (R827,8 million), and Madibeng (R561,9 million). In addition, 17 municipalities were qualified due to the disclosed irregular expenditure either being misstated or incomplete. At 20 municipalities, the irregular expenditure of prior years was not investigated at all or not properly investigated. This lack of investigations and consequences was the main driver of the increase in irregular expenditure, which then heightened the culture of non-compliance; in turn creating an environment susceptible to fraud and corruption.

We are concerned about instances where supply chain management regulations were deliberately contravened. For example, 11 municipalities (50%) participated in contracts arranged by other organs of state without complying with the requirements of supply chain management regulation 32 (we identified 48 such contracts amounting to R414,4 million during 2016-17). Fifteen municipalities (68%) did also not submit tender documents for auditing. Furthermore, fraudulent credit cards were opened in the name of the municipality at Madibeng and unauthorised monthly deductions were made from the municipality's bank account. These transactions were not identified by the municipality's system of internal control, such as the monthly bank reconciliations.

The proposed amendments to the Public Audit Act would allow us to refer – for investigation – any acts or omissions causing a loss of public resources or resulting in public resources not being used for its lawful purpose. Our audits identified instances where the accountability mechanisms in local government had failed. In the context of these amendments, we encourage all municipalities to take a strong stance against the abuse of public funds by ensuring that oversight structures, such as municipal public accounts committees, appropriately investigate transgressions.
The lack of accountability for sound financial management by the leadership had a negative impact on municipalities' financial viability. At eight (35%), the financial information was not reliable enough to analyse financial viability (as they had disclaimed opinions), while a further 20% were in a vulnerable financial position. Given the already vulnerable position of local government, we are very concerned about the overspending of budgets by 16 municipalities, resulting in unauthorised expenditure of R1,19 billion. The unauthorised expenditure was as a result of inadequate budget processes and a lack of in-year monitoring of the actual spending. In addition, of the gross outstanding consumer debtors balance of R12,9 billion for the province as at 30 June 2017, R10,5 billion (82%) was unlikely to be recovered. The inability to collect money from consumers resulted in the net current liability position of 12 municipalities (55%) deteriorating. This means that the current liabilities exceeded the current assets by R1,9 billion in the province. The total outstanding payables for the province increased by 23% to R5,4 billion from the previous year. Included in this amount was R1,1 billion owed to Eskom and R1,3 billion to bulk water service providers. The strain on cash resources was evidenced by municipalities taking an average of 240 days to pay outstanding payables (in other words, the persons or companies they owe money to), despite the Municipal Finance Management Act requiring payment within 30 days, which then resulted in further penalties and interest of R187,2 million. The financial viability of municipalities needs to be urgently addressed as it has a direct impact on their ability to continue rendering services.

Consequences, accountability and action by the provincial leadership are the key to turning around poor governance in local government

We continued to focus on environmental management at municipalities, specifically focusing on the management of solid waste landfill sites, the quality and availability of water as well as sewage treatment and effluent disposal. Despite the improved awareness and understanding of environmental management and sustainability, most municipalities had not made much progress in combating non-compliance with environmental laws and related requirements. Some of our key findings included illegal waste disposal and raw or untreated sewage being improperly discharged into the immediate environment and water resources, which may potentially affect the health and well-being of citizens. This was mostly as a result of overloaded or run-down infrastructure due to a lack of maintenance. Based on the National Treasury's budget guidelines, repairs and maintenance cost must be 8% of the carrying value of infrastructure assets. There was a shortfall of approximately R1,6 billion in actual repairs and maintenance at municipalities during 2016-17. This poorly maintained infrastructure also resulted in water losses in excess of R561,1 million or 65 627 906 kilolitres for the year. With the current water scarcity and drought in South Africa, such losses are unacceptable and need to be addressed urgently to prevent a possible disaster in future.

Slow progress in addressing information technology findings remains a concern, as little or no actions were taken to address these concerns. We are specifically concerned about the required implementation of the Municipal Standard Chart of Accounts by 1 July 2017 with the aim to strengthen accountability, facilitate budget reporting, and add value to the budget process to ultimately improve service delivery. Our readiness assessment indicated that the Municipal Standard Chart of Accounts was fully implemented at only four municipalities, while the implementation had not yet started at two municipalities, notwithstanding consultants being paid R71,9 million to assist with its implementation during 2016-17. There was a lack of data migration plans and in most cases mapping had not yet been completed. After year-end, implementation problems with the Municipal Standard Chart of Accounts became more evident at some municipalities. For example, Matlosana had to revert back to the previous system and consumer accounts had not been sent out due to problems with the new system.

The provincial coordinating departments, which include the premier's office, provincial treasury and provincial local government department, did not adequately assist municipalities to address root causes and internal control deficiencies previously identified. The provincial treasury in some instances deployed staff to certain municipalities or appointed consultants to assist with the preparation of financial statements. However, these appointments were not appropriately monitored to ensure that they had the desired impact. During March 2017, the premier committed to develop a 10-point plan to address root causes and key control weaknesses. This plan was to include mechanisms to enforce consequences and policies on investigations and disciplinary procedures. Despite the plan having been developed, it had not been implemented or rolled out to the intended users. No progress had been made in implementing consequences either. Until such time as there is political will at provincial executive level to lead by example and enforce compliance, this is unlikely to change.

The province's downward spiral will further continue until the vacancies in key positions are addressed and individuals in these positions all step up and accept accountability to address the root causes of poor audit outcomes. The province needs to build on the few individuals with personal commitment to perform well in their jobs, coupled with effective political leadership, to turn around the current situation so that officials feel motivated to do well in their jobs and take accountability for their performance. We are committed to continue providing further recommendations for improvement to management through our reporting messages and status of records reviews, and by tracking and providing feedback to the political leadership on the progress made.

5.9 WESTERN CAPE

PROVINCIAL SNAPSHOT

▼ **Clean audits: 70%**
(2015-16: 80%)

▼ **Quality financial statements: 89%**
(2015-16: 96%)

▼ **Quality performance report: 93%**
(2015-16: 96%)

▼ **No findings on compliance with legislation: 75%**
(2015-16: 82%)

▲ **Irregular expenditure: R173 m**
(2015-16: R174 m)

There was a significant regression in the audit outcomes of local government in the province when compared to 2015-16. This can be attributed to some municipalities not taking our messages and recommendations seriously as well as not demonstrating the required levels of accountability and governance. Three municipalities lost their clean audit status, namely Bitou, Eden District and – of serious concern due its significance in the province – the City of Cape Town Metro. This was due to material non-compliance with supply chain management regulations at all three municipalities, irregular expenditure not being prevented at Bitou, and weaknesses in the implementation of consequences and revenue management at the City of Cape Town Metro. Accountability at both the political and administrative level is a core principle for municipalities where they are answerable to the public and responsible for decisions, actions and policies. If effectively demonstrated, this may have a positive impact on audit outcomes. Continued improvements in the levels of accountability and governance contributed to the ability of auditees to sustain their clean audit outcomes and assisted Cederberg and Prince Albert to achieve a clean audit opinion for the first time. These levels of accountability also contributed to Knysna and Kannaland receiving an unqualified opinion with findings and a qualified opinion, respectively. Their outcomes are excluded from our analysis, however, as their audits were finalised after the cut-off date for inclusion in this report due to the late submission of their financial statements.

The overall quality of submitted financial statements regressed slightly with four sets of financial statements (14%) requiring material adjustments to avoid qualifications, compared to three (11%) in the previous year. Only one of the four auditees was able to successfully correct their misstatements and attain an unqualified opinion on their financial statements. As a result, two auditees regressed from financially unqualified opinions with findings to a disclaimed opinion (Beaufort West) and a qualified opinion (Laingsburg), while Oudtshoorn again received a qualified opinion.

We remain concerned that the municipalities relied on the audit process to identify adjustments needed to their performance reports, with 18 performance reports (64%) requiring material corrections in 2016-17 compared to 17 (63%) in 2015-16. 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 (with indicators that are specific, measurable, attainable, realistic and time bound) and processes are in place to report on actual achievements, except for Beaufort West where the performance information did not meet the usefulness criteria. For the first time in years, Oudtshoorn submitted a performance report, but a lack of supporting documents led to material findings on the reliability of their performance information.

Accountability failures resulted in regression

Non-compliance with the Municipal Finance Management Act, in particular supply chain management regulations, continued to be one of the main obstacles to increasing the number of clean audit opinions in the province. Seven auditees (25%) had material findings on compliance with procurement processes, compared to five (18%) in 2015-16. It is concerning that the Central Karoo district continued to be plagued by material findings on compliance with supply chain management regulations, with three of the four municipalities in the district attracting such findings.

A lack of understanding of supply chain management prescripts, vacancies at supply chain management practitioner level, instability as well as the absence of appropriate supply chain management processes and procedures contributed to non-compliance with procurement processes. The total irregular expenditure incurred in the Western Cape was R173 million (2015-16: R174 million), of which R163 million related to non-compliance with supply chain management regulations. A total of 98% of the irregular expenditure related to supply chain management involved current year transgressions; and these transgressions can be isolated to unjustifiable deviations in terms of supply chain management regulation 36, the extension of contracts without the necessary approvals, and non-compliance with local content prescripts. At Oudtshoorn, a multi-year contract relating to consultancy services resulted in irregular expenditure of R4 million (2016: R1,3 million), which was not appropriately dealt with due to a lack of proper contract management systems. At Eden District, a multi-year contract was awarded in the year under review and resulted in irregular expenditure of R24 million, as the contract was not advertised for the minimum stipulated period. As this was the first year the contract was active, we will now have to assess whether any actions are taken in the following years to mitigate the irregular expenditure incurred. Supply chain management officials require further training on the application of local content prescripts.

Generally, allegations of misconduct and unauthorised, irregular and fruitless and wasteful expenditure were investigated by the council and the related expenditure was written off as irrecoverable if no one was found to be liable. At three municipalities (11%), however, investigations were not performed to determine whether any person was liable for such expenditure. Consequences must be implemented to deal with all instances of non-compliance with legislation as required.

The overall assessment of the information technology control environment remained unchanged at municipalities where our information systems auditors performed audit work. One municipality, Swartland, have had no significant information technology audit findings for the past two years. Eight municipalities still experienced challenges in implementing controls relating to all three focus areas, namely user access management, security management, and service continuity management. This was due to information technology operations being prioritised over the implementation of information technology controls, limitations in system functionality, and municipalities' continued focus on the implementation of the Municipal Standard Chart of Accounts. The majority of municipalities had implementation plans in place for the Municipal Standard Chart of Accounts. Formal post-implementation reviews had not yet been performed, but issues were being identified, reported and resolved on an ongoing basis. However, municipalities continued to rely on vendors for support. Some municipalities indicated that the service providers had not written all the modules and as a result they could not print certain reports, while some municipalities were running two systems concurrently. Two municipalities migrated to a new financial system due to vendors no longer providing support on their existing systems.

Municipalities also continued to rely on consultants for financial and performance reporting. The number of municipalities using consultants for performance information decreased slightly from 12 (43%) in 2015-16 to 11 (26%) in 2016-17. There was also a slight decrease in the number of municipalities using consultants for financial reporting from 23 (82%) in 2015-16 to 22 (79%) in 2016-17, which can be attributed to the filling of vacancies at municipalities. However, measures to monitor contract performance and delivery were not defined and/or implemented, and measures to monitor the transfer of skills were not in place, which we raised as findings at six and five municipalities, respectively. The total amount spent on consultants decreased from R37 million in 2015-16 to R30 million in 2016-17. Municipalities should continue with their efforts to ensure the transfer of skills from consultants to municipal officials to further reduce reliance on the consultants where possible.

The number of municipalities with an unfavourable financial health assessment decreased from seven (25%) in 2015-16 to four (14%) in 2016-17. Some municipalities' financial recovery plans included entering into agreements with suppliers, such as Eskom, according to which they agreed to pay off outstanding amounts over a specified period. The suppliers would then write off the interest if the municipalities honoured the agreements, which would improve municipalities' cash flow and help to avoid fruitless and wasteful expenditure. This initiative led to some municipalities successfully settling their overdue Eskom accounts. The concerning financial position of municipalities resulted from difficulty in collecting debt from consumers and weak financial management.

Considering the water crisis that the Western Cape is experiencing, it is concerning that six municipalities (21%) did not have approved policies for the routine maintenance of water infrastructure. Four municipalities (14%) also did not have a plan with specific time frames and targets for the maintenance of water infrastructure. The lack of policies and plans in this regard could pose a serious challenge in overcoming the water crisis. Two municipalities (7%), namely Beaufort West and Laingsburg, reported water losses above the acceptable norm of 30%.

Overall, the status of financial and performance key controls remained mostly unchanged. Further improvements in controls at municipalities that maintained their clean audit opinions from the previous year were unfortunately offset by municipalities where outcomes regressed. To improve the audit outcomes, leadership should take audit findings seriously (including management report findings) and develop detailed action plans to address recurring findings relating to financial statements, performance reports and compliance with key legislation (including supply chain management prescripts).

The accountability failures we noted can be attributed to, among others, political instability, instability in municipal manager and chief financial officer positions, and a failure to sufficiently monitor and implement action plans to address prior year findings. The August 2016 municipal elections brought about a significant change in the political landscape in the Western Cape, resulting in an intake of new mayors and speakers as well as an overall change of municipal councils at most municipalities. In addition, two new municipal managers (7%) and two new chief financial officers (7%) took up positions at municipalities as a result of the elections. Due to these changes, the focus of municipalities was largely on training, attempts to bring about stability, the appointment of municipal and senior managers, and the filling of other critical posts occupied by staff in an acting capacity. Focus on good governance, sound financial practices and the implementation and monitoring of audit action plans was not always evident, despite our warnings in this regard in the previous year's general report. Instability at political and senior management level often led to overall accountability failures at individual auditees, resulting in findings in all three our audit areas (financial statements, performance reports, and compliance with key legislation).

Of concern is the regression in the assurance provided by senior management overall, as they are the custodians of the day-to-day financial activities at municipalities. We rated senior management at various auditees with clean audit opinions as providing only some assurance. This was due to compliance findings reported in the management report (although these findings were not material in 2016-17, they could become so in future if not appropriately dealt with by senior management). Additionally, material corrections to the performance report as well as misstatements in the financial statements corrected during the audit process contributed to us assessing senior management as providing only some assurance.

The City of Cape Town Metro illustrates perfectly what happens when audit findings and messages are not acted upon with the necessary rigour. The metro lost its clean audit status mainly as they did not report all allegations against senior management to the council as well as ineffective controls over the revenue cycle that we had previously reported as an emerging risk.

Staff from our provincial office attended various forums, including the premier's coordinating forum, municipal manager forum, chief financial officer forum and supply chain management forum, to communicate messages related to the outcomes of prior years, the causes of undesired outcomes, emerging risks, and possible responses to the risks identified. We also embarked on a status of records review process at various municipalities. The results of the engagements were mixed and can also be linked to the overall root causes. At auditees where there was instability at leadership level, engagements took place but management did not respond to the issues raised. At the two auditees that improved to clean audit opinions, we noted signs of steady improvement over the past two or three years, including stability and competence at senior levels. These auditees also took our recommendations and discussions seriously, as was the case for the entire audit process.

The proposed amendments to the Public Audit Act would allow the enforcement of consequences in certain circumstances, such as investigations into undesirable audit outcomes. Municipalities are encouraged to implement action plans to address repeat supply chain management non-compliance that results in irregular expenditure.

Key role players continued to be committed to improve the level of support to municipalities and to intensify such support, as was evidenced by the back-to-basics and governance programmes at Cederberg and Prince Albert that obtained clean audits for the first time. Going forward, we encourage all key role players to intensify their support to the municipalities in the Central Karoo district as well as to renew their focus at municipalities whose audit outcomes had regressed. This enhanced level of support could translate into improved audit outcomes across the province. We will continue to monitor the impact and progress of commitments made, as they are critical enablers to improving the overall audit outcomes in the province. In addition, the municipal leadership is encouraged to embrace the status of records reviews, as this initiative provides for a system of early warning and identification of key areas of concern that may compromise financial and performance management and compliance with legislation.

All municipalities should keep striving to improve levels of accountability, good governance and consequences to attain or maintain clean administration.

SECTION 6

Need to know

6.1 OUR AUDIT PROCESS 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 further assess the root cause of any error or non-compliance, based on the internal control that has 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 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 report is published, we share the outcomes and root causes with the national and provincial leadership, Parliament and the legislatures, as well as other 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, regularly assessing these, and sharing the results of the assessment with mayors, municipal managers, chief executive officers as well as audit committees.

During the audit process, we work closely with the municipal managers, chief executive officers, senior management, audit committees and internal audit units, as they are **key role players** in providing assurance on the credibility of the auditees' financial statements and performance reports as well as on their compliance with legislation.

We also continue to strengthen our relationship with the mayors, ministers and members of the executive council responsible for cooperative governance, coordinating and monitoring departments (such as the treasuries, premier's offices and 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 governance. 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 receive a **financially unqualified opinion with no findings** are those that are 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 receive a **financially unqualified opinion with findings** are those that are able to produce financial statements without material misstatements, but are struggling to:

   - align their performance reports to the predetermined objectives to which they have 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 have 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 receive a **financially qualified opinion with findings** face the same challenges as those that are financially unqualified with findings in the areas of reporting on performance and compliance with key legislation. In addition, they are unable to produce credible and reliable financial statements. Their financial statements contain misstatements that they cannot correct before the financial statements are published.

4. The financial statements of auditees that receive an **adverse opinion with findings** include so many material misstatements that we disagree with virtually all the amounts and disclosures in the financial statements.

5. Those auditees with a **disclaimed opinion with findings** cannot provide us with evidence for most of the amounts and disclosures in the financial statements. We are therefore 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 reporting 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 Municipal Finance Management Act. The finding is only reported for auditees that are subject to this act and if the financial statements we receive for auditing include 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 focus on the following areas in our compliance audits if they apply to the particular auditee: ■ the quality of 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, supply chain management) ■ human resource management and compensation.

In our audit reports, we report findings that are 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 have been followed** to ensure that all suppliers are given equal opportunity to compete and that some suppliers are not favoured above others. The principles of a fair, equitable, transparent, competitive and cost-effective supply chain management process are fundamental to the procurement practices of the public sector, as enshrined in the country's constitution and prescribed in the Municipal Finance Management Act and its regulations. The act and its 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:

- Supply chain management 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 supply chain management 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 non-compliance in the process that needs to be investigated by management to determine whether it was an unintended error, negligence or done with the intention to work against the requirements of legislation (which, for example, require that procurement should be fair, equitable, transparent, competitive and cost-effective).

Through such **investigation**, it is also determined who is responsible and what the impact of the non-compliance is. 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, the recovery of any losses from the implicated officials or even cancelling a contract or reporting the matter to the police or an investigating authority.

The Municipal Finance Management Act is clear that **municipal managers are responsible for preventing irregular expenditure** as well as on what process to follow if it has been incurred. Irregular expenditure is reported when it is identified – even if the expenditure was incurred in a previous year.

In order to promote transparency and accountability, auditees **should disclose all irregular expenditure identified (whether by the auditee or through the audit process)** in their financial statements with detail on how it had been resolved; in other words, how much had been investigated, recovered or condoned.

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 used or goods not received.

The Municipal Finance Management Act requires municipal managers to take all **reasonable steps to prevent fruitless and wasteful expenditure**. Auditees should have processes 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 act 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 approved budget by the council or that does not meet the conditions of a grant.

The Municipal Finance Management Act requires municipal managers to take all **reasonable steps to prevent unauthorised expenditure.** Auditees should have processes to identify any unauthorised expenditure and disclose the amounts in the financial statements. The act 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 allocated 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 grant allocations are approved each year through the Division of Revenue Act. This act indicates the approved allocation per auditee for that particular year, together with a forward estimate 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 the act:

- 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 Department of Cooperative Governance introduced the **municipal infrastructure grant** in 2004-05 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.

To achieve this outcome, annual targets must be set in respect of the following expected outputs derived from the municipal infrastructure grant 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 Department of Cooperative Governance. The grant uses the registration requirements of the municipal infrastructure grant 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 **urban settlement development grant** 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 **public transport network grant** 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 that are material enough to be brought to the attention of these users.

As part of the annual audits, we audit the **usefulness of the reported performance information** to determine whether it is presented in the annual report in the prescribed manner and is consistent with the auditee's planned objectives as defined in the integrated development plan and/or service delivery and budget implementation plan. We also assess whether the performance indicators set to measure the achievement of the objectives are:

- well defined (the indicator needs to have a clear, unambiguous definition so that data can be collected consistently, and is easy to understand and use)
- verifiable (it must be possible to validate the processes and systems that produce the indicator)
- specific (so that the nature and the required level of performance can be clearly identified)
- time bound (the time period or deadline for delivery must be specific)
- measurable (so that the required performance can be measured)
- consistent (with the objective, measures and/or targets)
- relevant (so that the required performance can be linked to the achievement of a goal).

We further audit the **reliability of the reported information** to determine whether it can be traced back to the source data or documentation and whether it is accurate, complete and valid.

WHEN IS HUMAN RESOURCE MANAGEMENT EFFECTIVE?

Human resource management refers to the **management of auditees' employees** (in other words, their human resources). Human resource management is effective if adequate and sufficiently skilled staff members are in place and if their performance and productivity are properly managed.

Our audits include an assessment of human resource management, focusing on the following areas: ■ human resource planning and organisation ■ management of vacancies ■ appointment processes ■ performance management ■ acting positions ■ management of leave and overtime.

Our audits further look at vacancies and stability in key positions, the competencies of key officials, 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 assess the status of auditees' human resource management controls.

WHEN ARE INTERNAL CONTROLS EFFECTIVE AND EFFICIENT?

A key responsibility of municipal managers, chief executive officers, 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 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 auditees should focus on are outlined below.

Providing effective leadership

In order to improve and sustain audit outcomes, auditees require **effective leadership** that is based on a culture of honesty, ethical business practices and good governance to protect and enhance 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 key elements of internal control.

The Medium-Term Strategic Framework 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 Department of Cooperative Governance's back-to-basics 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:

- Establishing 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.
- Implementing policies, procedures and monitoring mechanisms to manage records, and making staff members aware of their responsibilities in this regard.

Implementing controls over daily and monthly processing and reconciling of transactions

Controls should be in place to ensure that **transactions are processed accurately, completely and timeously**, 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.

Reviewing and monitoring 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?

Information technology refers to the computer systems used for recording, processing and reporting financial and non-financial transactions. Information technology controls ensure the confidentiality, integrity and availability of state information, enable service delivery, and promote national security. Good information technology governance, effective information technology management and a secure information technology infrastructure are therefore essential.

Non-complex and complex information technology environments

As per our new audit methodology, we differentiate between **non-complex** and **complex** information technology environments, as follows:

Non-complex environment – level 1 (low risk)

This is the lower end of the spectrum for information technology sophistication and relevance. The auditee uses one server associated with financial reporting and/or performance information, a limited number of workstations, no remote locations, commercial off-the-shelf applications and infrastructure, vendors to perform updates and maintenance on the system, little emerging or advanced technology, and a few or no online and e-commerce transactions.

Key controls over financial reporting and/or performance information are not overly reliant on information technology, are embedded in the commercial off-the-shelf applications, or are limited to very few manual processes and controls. Many small to medium-sized entities fall into this category.

Complex environment – levels 2 and 3 (medium and high risk)

This is the middle to high end of the spectrum. These auditees have the following characteristics:

- Use more than one server associated with financial reporting and/or performance information.
- Have remote locations.
- Employ one or more network operating system or non-standard ones.
- Have more workstations in total.
- Use some customisation of application software or have a relatively complex configuration of commercial off-the-shelf applications.
- Use enterprise resource planning systems and/or write their own custom software.
- Perform updates and maintenance on the system centrally onsite or through vendors, or perform centralised updates and maintenance on the system and distribute these to decentralised sites or through onsite vendors.
- Employ a few to moderate or a large number of emerging or advanced technologies.
- Enter into either a few or large number of online and e-commerce transactions.
- Rely heavily on information technology key controls over financial and/or performance information.

An entity running transversal systems would also fall into this category. Information systems for which certain information technology processes are managed centrally, but which are used by various auditees who have limited responsibility regarding the design and enhancement of the system, will also be classified as high risk at a national level.

Which information technology controls do we audit?

During our audits, we assess the information technology controls that focus on governance, security management, user access management and service continuity – as discussed further down. To evaluate the status of the information technology controls in the areas we audit, we group them into the following three categories, with reference to the control measures that should be in place:

1. **Where information technology controls are being designed**, management should ensure that the controls would reduce risks and threats to information technology systems.
2. **Where information technology controls are being implemented**, management should ensure that the designed controls are implemented and embedded in information technology processes and systems. Particular attention should be paid to ensuring that staff members are aware of and understand the information technology controls being implemented, as well as their roles and responsibilities in this regard.
3. **Where information technology controls have been embedded and are functioning effectively**, management should ensure that the controls that have been designed and implemented are functioning effectively at all times. Management should sustain these controls through disciplined and consistent daily, monthly and quarterly information technology operational practices.

Information technology governance

This refers to the leadership, organisational structures and processes which ensure that the auditee's information technology resources will sustain its business strategies and objectives. Effective information technology governance is essential for the overall well-being of an auditee's information technology function and ensures that the auditee's information technology control environment functions well and enables service delivery.

Security management

This refers to the controls preventing unauthorised access to the computer networks, computer operating systems and application systems that generate and prepare financial and performance information.

User access management

These 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

These 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 to 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 include an **assessment of the root causes of audit findings**, based on the identification of internal controls that have failed to prevent or detect the error in the financial statements and performance reports or that have led to non-compliance with legislation. These root causes are confirmed with management and shared in the management report with the municipal managers or chief executive officers and the mayors. We also include 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 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:

- Those directly involved in the management of the auditee (management or leadership assurance).
- 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).
- 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 auditees' internal controls 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 chief financial officer, chief information officer and head of the supply chain management 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 information technology systems.

Municipal managers and municipal entities' chief executive officers

While we recognise that municipal managers and the chief executive officers 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 human resource 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 information technology 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 information technology 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 Municipal Finance Management Act 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 supply chain management 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 Municipal Finance Management Act and the Municipal Systems Act, 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 chief executive officers 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 chief executive officer, 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 Municipal Finance Management Act further requires national and provincial government to assist municipalities in building capacity to support efficient, effective and transparent financial management. Both the Municipal Finance Management Act and the Municipal Systems Act 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 Municipal Finance Management Act and the Municipal Systems Act 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 municipal public accounts committee 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 committee 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 cooperative governance. This executive authority includes the minister and members of the executive council for cooperative governance and other executives involved in local government, such as the minister and members of the executive council for finance. The mechanism used to conduct oversight is the portfolio committees on local government.

6.2 GLOSSARY OF KEY TERMINOLOGY USED IN THIS REPORT

Accountability (plan+do+check+act) **cycle**	The 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.
Asset (in financial statements)	Any item belonging to the auditee, including property, infrastructure, equipment, cash, and debt due to the auditee.
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	The most senior official of the auditee who is accountable for aligning information technology and business strategies, and planning, resourcing and managing the delivery of information technology services and information as well as for the deployment of associated human resources. The chief information officers 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 (information technology)	The complete technical description required to build, test, accept, install, operate, maintain and support a system.
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.
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.
Governance (as one of the drivers of internal control)	The governance structures (audit committees) and processes (internal audit and risk management) of an auditee.
Information technology infrastructure	The hardware, software, computer-related communications, documentation and skills that are required to support the provision of information technology 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.
Medium-Term Strategic Framework	Government's strategic plan for the 2014-19 electoral term. It reflects the commitments made in the election manifesto of the governing party, including the commitment to implement the National Development Plan. Its aim is to ensure policy coherence, alignment and coordination across government plans as well as alignment with budgeting processes.
Misstatement (in financial statements or performance reports)	Incorrect or omitted information in the financial statements or performance report.
Municipal Standard Chart of Accounts	This provides a multi-dimensional, uniform and standardised financial transaction classification framework. Essentially this means that the framework prescribes the method (the how) and format (the look) that municipalities and their entities should use to record and classify all capital and operating expenditure, revenue, assets, liabilities, equity, policy outcomes, and legislative reporting.
Non-cash item (in financial statements)	An entry in the financial statements correlating to expenses that are essentially just accounting entries rather than actual movements of cash. Depreciation and amortisation are the two most common examples of non-cash items.
Platform (information technology)	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.
Public Audit Act (Act No. 25 of 2004)	This is the Auditor-General of South Africa's enabling legislation. The objective of the act is to give effect to the provisions of our country's constitution by establishing and assigning functions to an auditor-general and by providing for the auditing of institutions in the public sector.
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.
Status of records review	A process whereby the auditor performs basic review procedures to identify risks and areas of concern for discussion with the accounting officer or mayor. The purpose of the status of records review is to: • ensure that there is a system of early warning to the accounting officer or mayor on challenges that may compromise good financial and performance management and compliance with legislation • demonstrate to the accounting officer or mayor a deepened level of understanding of the business of the auditee and the value added by the auditor • contribute to capacitating the accounting officer or mayor and senior management in instilling good practices of regular reporting, review and oversight • identify risks early and throughout the audit cycle to respond to these timeously and correctly.
Vulnerable financial position (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.

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