

SCOPA BRIEFING NOTE



MFMA audit outcomes of the 2017-18 financial year

Bojanala Platinum District Municipality

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Introduction

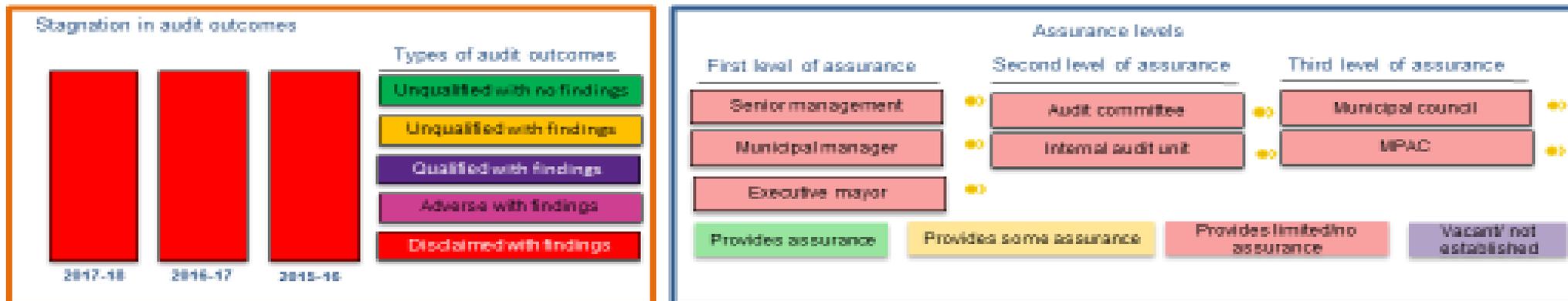
The purpose of this report is to provide the Standing Committee on Public Accounts (SCOPA) with an overview of the audit outcomes and internal control deficiencies that have prevented the municipality from attaining the desired audit outcome, i.e. financially unqualified with no material findings on legislation and predetermined objectives (also known as a 'clean audit outcome'). Below is the summary of the 2017-18 audit outcomes and the status of material findings reported under predetermined objectives and compliance with legislations.

The figure that follows provides a pictorial summary of the audit results and our key messages on how to improve the audit outcomes with the focus on the following:

- Status of the audit outcomes
- Status of the level of assurance provided by key role players
- Status of the drivers of internal controls
- Status of risk areas
- Root causes to be addressed



Overall audit outcome graphic



1 ... the root causes are addressed ...



2 ... the key role players need to assure that ...



3 ... attention is given to the key controls and ...



4 ... the risk areas and ...



5 ... the best practices are maintained.

Root causes should be addressed

Lack by management to address internal control weaknesses identified by external audit

Key officials lack appropriate competences

Consequence management not implemented

Risk areas

- Quality of submitted financial statement
- Quality of submitted performance information
- Supply chain management
- Financial health
- Human resource management
- Information technology

Good | Concerning | Intervention required

Status of drivers of internal controls

- Leadership: Effective leadership culture, Oversight responsibility, HR Management, Policies and procedures, Audit action plans, IT Governance
- Financial and performance management: Proper record keeping, Processing and reconciling control, Regular reporting, Compliance monitoring, IT system controls
- Governance: Risk management, Internal audit, Audit committee

Good | Concerning | Intervention required



Overall Message

1. As in the prior year, material misstatements were identified in the financial statements submitted for audit. The stagnation in the overall audit outcome is due to management not identifying the root causes that resulted in the poor audit outcomes of the prior years and not implementing the required internal control disciplines required to respond to these root causes. This was further hampered by the implementation of MSCOA in the current year which posed additional challenges with regard to integration between the existing systems and MSCOA.
2. Sustainable systems and processes were not introduced and implemented during the year for the recording, reconciling and reporting of transactions and balances due to over reliance on consultants. This weakness in the control environment was mainly due to instability in senior management positions for a substantial part of the financial year, particularly that of the municipal manager and chief financial officer.
3. The overall outcomes for predetermined objectives and the quality of the annual report submitted has also regressed in the current year. As reported in the prior year, the significant root cause emanating from the basis of conclusion reached are due to lack of standard operating procedures for performance indicators as well as inadequate controls relating to the collating and recording of information. The audit action plan was not adequate as it did not address the findings on performance information.
4. Non-compliance with legislation remains a major concern and the municipality is unlikely to improve the audit outcomes if the root causes for material non-compliance findings are not addressed.
5. The municipality is experiencing cash flow challenges. At year end the municipality was in a net liability position. This is due to inadequate monitoring of expenditure compared to the approved budget during the year.
6. The municipality has various governance structures with suitably skilled role players with an understanding of the improvements required to achieve a clean administration. However, the effectiveness of the audit committee as an assurance provider is impacted by the municipality and leadership's inability to act on the recommendations made by the audit committee.



Audit opinion history

| | |
|--|---|
| | Clean audit opinion: Financially unqualified opinion with no findings on PDO and compliance |
| | Financially unqualified opinion with findings on PDO and compliance |
| | Qualified audit opinion (with findings) |
| | Disclaimed/adverse audit opinion |

| DESCRIPTION | Movement | 17-18 | 16-17 | 15-16 |
|---|----------|-------|-------|-------|
| Audit opinions | | | | |
| Disclaimer audit opinion (with findings) | ●➤ | | | |
| Predetermined objectives(PDO's) | | | | |
| Basic service delivery and infrastructure development | ●➤ | | | |



Summary of qualification areas, root causes and recommendations

Financial Statement qualification areas

| Finding | Root cause | Recommendation |
|---|--|--|
| <p><i>All below financial statement items</i></p> | <ul style="list-style-type: none"> • Lack of review of the financial statements • Lack of understanding by finance staff of basic accounting principles • Monthly reconciliations between the financial system and subsidiary ledgers are not performed • Where reconciliations were performed, these reconciliations were not adequate and variances were not investigated • Accounts in the general ledger were adjusted to agree to the supporting registers without identifying specific items that have caused the variances • Basic key controls to detect and prevent errors were not implemented throughout the year as there is an over-reliance on consultants to prepare the financial statements at year end • Implementation of Mscoa in the current year which resulted in transactions which were incorrectly mapped <p>Documentation to support certain transactions were not submitted for audit</p> | <ul style="list-style-type: none"> • Staff within the finance unit to be trained to obtain an understanding on the basic accounting principles • Adequate review and supervision of work performed by staff within the finance unit • Implementation of key basic controls to prevent and detect errors on a timely basis. This includes: <ul style="list-style-type: none"> - Performing monthly reconciliations - Reconciliations to be reviewed and variances followed up - Restrictions to process journals to specific individuals - Monthly exception reports - System validations • Review of the financial statements for completeness and accuracy. |



1) Cash and cash equivalents

| Finding | Root cause | Recommendation |
|---|--|--|
| <p>The amounts disclosed as cash book balances for the periods ended 30 June 2017 and 30 June 2016 were not accurate and did not agree to the actual cash book balances of these years.</p> | <p>Lack of proper monitoring controls during the preparation of the financial statements to ensure that information contained therein is accurate, complete, meets the requirements of the relevant reporting framework and is supported and evidenced by reliable information that is accessible and available to support financial reporting in a timely manner.</p> | <p>Implementation of key basic controls such as monthly reconciliations, systems controls over journal processing and quarterly reviewed financial statements basis. These controls should be executed by the municipality's own officials throughout the course of the financial year to ensure errors are timously detected and addressed prior the submission of the annual financial statements for audit.</p> |

2) Property, plant and equipment

| Finding | Root cause | Recommendation |
|--|--|--|
| <p>Work in progress was not accounted for during the year. Depreciation was not calculated as per accounting policy.</p> | <p>Lack of adequate understanding of the basic accounting principles resulting in incorrect application of the accounting framework.</p> | <p>Implementation of key basic controls such as monthly reconciliations, systems controls over journal processing and quarterly reviewed financial statements basis. These controls should be executed by the municipality's own officials throughout the course of the financial year to ensure errors are timously detected and addressed prior the submission of the annual financial statements for audit.</p> |



3) Payables from exchange transactions

| Finding | Root cause | Recommendation |
|--|--|---|
| <p>Documentation to support payables disclosed at year end could not be provided.</p> <p>In addition, amounts that did not qualify as payables were disclosed as payables at year end.</p> | <ul style="list-style-type: none"> • Lack of an adequate record management system • Regular reconciliations are not prepared and reviewed and there are no supporting documents for journals processed. • Lack of adequate understanding of the basic accounting principles resulting in incorrect application of the accounting framework. | <ul style="list-style-type: none"> • Implement records management processes and systems to ensure that documents are properly filled, controlled and easily retrieved when required. • Implementation of key basic controls such as monthly reconciliations, systems controls over journal processing and quarterly reviewed financial statements basis. These controls should be executed by the municipality's own officials throughout the course of the financial year to ensure errors are timeously detected and addressed prior the submission of the annual financial statements for audit. |

4) Accumulated deficit

| Finding | Root cause | Recommendation |
|---|--|---|
| <p>Variances were identified between the accumulated deficit disclosed in the financial statements and the accumulated deficit as per the financial system / general ledger which could not be substantiated.</p> | <p>Lack of proper monitoring controls during the preparation of the financial statements to ensure that information contained therein is accurate, complete, meets the requirements of the relevant reporting framework and is supported and evidenced by reliable information that is accessible and available to support financial reporting in a timely manner.</p> | <p>Implementation of key basic controls such as monthly reconciliations, systems controls over journal processing and quarterly reviewed financial statements basis. These controls should be executed by the municipality's own officials throughout the course of the financial year to ensure errors are timeously detected and addressed prior the submission of the annual financial statements for audit.</p> |



5) Employee related cost

| Finding | Root cause | Recommendation |
|--|--|--|
| <p>Variations were identified between the employee related cost disclosed in the financial statements and the employee related cost as per the payroll system (PAYDAY) which could not be substantiated.</p> | <p>Lack of proper monitoring controls during the preparation of the financial statements to ensure that information contained therein is accurate, complete, meets the requirements of the relevant reporting framework and is supported and evidenced by reliable information that is accessible and available to support financial reporting in a timely manner.</p> | <p>Implementation of key basic controls such as monthly reconciliations, systems controls over journal processing and quarterly reviewed financial statements basis. These controls should be executed by the municipality's own officials throughout the course of the financial year to ensure errors are timely detected and addressed prior the submission of the annual financial statements for audit.</p> |

6) Depreciation and amortisation

| Finding | Root cause | Recommendation |
|---|---|---|
| <p>Insufficient evidence provided to support the comparative depreciation figure disclosed in the financial statements.</p> | <p>Lack of proper monitoring controls during the preparation of the financial statements to ensure that information contained therein is accurate, complete, meets the requirements of the relevant reporting framework and is supported and evidenced by reliable information that is accessible and available to support financial reporting in a timely manner</p> | <p>Implementation of key basic controls such as monthly reconciliations, systems controls over journal processing and quarterly reviewed financial statements basis. These controls should be executed by the municipality's own officials throughout the course of the financial year to ensure errors are timely detected and addressed prior the submission of the annual financial statements for audit</p> |

7) Contracted services

| Finding | Root cause | Recommendation |
|---|---|---|
| <ul style="list-style-type: none"> Insufficient evidence provided to support the comparative contracted services figure disclosed in the financial statements. | <ul style="list-style-type: none"> Lack of an adequate record management system. Lack of adequate understanding of the basic accounting principles resulting in incorrect | <ul style="list-style-type: none"> Implement records management processes and systems to ensure that documents are properly filled, controlled and easily retrieved when required. Staff within the finance unit to be trained to obtain an |



| Finding | Root cause | Recommendation |
|--|--|--|
| <ul style="list-style-type: none"> In addition, transfers and subsidies were incorrectly classified as contracted services. | application of the accounting framework. | understanding on the basic accounting principle in order to be fully capacitated to properly prepare and review the financial statements prior submitting for audit. |

8) Transfers and subsidies

| Finding | Root cause | Recommendation |
|---|---|---|
| Insufficient evidence provided to support the comparative transfers and subsidies figure disclosed in the financial statements. | Lack of an adequate record management system. | Implement records management processes and systems to ensure that documents are properly filled, controlled and easily retrieved when required. |

9) Loss on disposal of assets and liabilities

| Finding | Root cause | Recommendation |
|--|---|---|
| Insufficient evidence provided to support the comparative loss on disposal of assets and liabilities figure disclosed in the financial statements. | Lack of proper monitoring controls during the preparation of the financial statements to ensure that information contained therein is accurate, complete, meets the requirements of the relevant reporting framework and is supported and evidenced by reliable information that is accessible and available to support financial reporting in a timely manner. | Implementation of key basic controls such as monthly reconciliations, systems controls over journal processing and quarterly reviewed financial statements basis. These controls should be executed by the municipality's own officials throughout the course of the financial year to ensure errors are timely detected and addressed prior the submission of the annual financial statements for audit. |



10) Operational costs

| Finding | Root cause | Recommendation |
|---|--|--|
| <ul style="list-style-type: none"> Insufficient evidence provided to support the comparative operational cost figure disclosed in the financial statements. In addition, expenditure incurred in the prior year was recognised as expenditure for the current year. | <ul style="list-style-type: none"> Lack of an adequate record management system. Lack of adequate understanding of the basic accounting principles resulting in incorrect application of the accounting framework. | <ul style="list-style-type: none"> Implement records management processes and systems to ensure that documents are properly filled, controlled and easily retrieved when required. Staff within the finance unit to be trained to obtain an understanding on the basic accounting principle in order to be fully capacitated to properly prepare and review the financial statements prior submitting for audit. |

11) Cash flow statement

| Finding | Root cause | Recommendation |
|--|---|---|
| <p>Insufficient evidence provided to support the cash flow movements in the cash flow statement.</p> | <p>Inadequate skills within the finance department and lack of adequate review of the financial statements.</p> | <p>Implementation of key basic controls such as monthly reconciliations, systems controls over journal processing and quarterly reviewed financial statements basis. These controls should be executed by the municipality’s own officials throughout the course of the financial year to ensure errors are timeously detected and addressed prior the submission of the annual financial statements for audit.</p> |



12) Statement of comparison of budget and actual amounts

| Finding | Root cause | Recommendation |
|--|--|---|
| <p>The budget amounts included in the statement of comparison of budget and actual amounts did not agree to the final approved budget of council and reasons for variances between budget and actual were not disclosed.</p> | <p>Lack of proper monitoring controls during the preparation of the financial statements to ensure that information contained therein is accurate, complete, meets the requirements of the relevant reporting framework and is supported and evidenced by reliable information that is accessible and available to support financial reporting in a timely manner.</p> | <p>Implementation of key basic controls such as monthly reconciliations, systems controls over journal processing and quarterly reviewed financial statements basis. These controls should be executed by the municipality's own officials throughout the course of the financial year to ensure errors are timeously detected and addressed prior the submission of the annual financial statements for audit.</p> |

13) Prior period errors

| Finding | Root cause | Recommendation |
|---|---|---|
| <p>The municipality did not correctly disclose all of the adjustments made to the prior year balances. The nature and the amount of the corrections were not disclosed.</p> | <p>Inadequate skills within the finance department and lack of adequate review of the financial statements.</p> | <ul style="list-style-type: none"> • Staff within the finance unit to be trained to obtain an understanding on the basic accounting principles • Adequate review and supervision of work performed by staff within the finance unit |



14) Unauthorised expenditure

| Finding | Root cause | Recommendation |
|---|---|--|
| <ul style="list-style-type: none"> The municipality did not account for any unauthorised expenditure for the current year. Due to the state of the accounting records the unauthorised expenditure could not be determined. In addition, additional unauthorised expenditure identified in the 2016 financial year was not accounted for. | <ul style="list-style-type: none"> Inadequate skills within the finance department and lack of adequate review of the financial statements. Lack of proper monitoring controls during the preparation of the financial statements to ensure that information contained therein is accurate, complete, meets the requirements of the relevant reporting framework and is supported and evidenced by reliable information that is accessible and available to support financial reporting in a timely manner. | <ul style="list-style-type: none"> Staff within the finance unit to be trained to obtain an understanding on the basic accounting principles. Implementation of key basic controls such as monthly reconciliations, systems controls over journal processing and quarterly reviewed financial statements basis. These controls should be executed by the municipality’s own officials throughout the course of the financial year to ensure errors are timeously detected and addressed prior the submission of the annual financial statements for audit. |

15) Irregular expenditure

| Finding | Root cause | Recommendation |
|--|---|---|
| <ul style="list-style-type: none"> Documentation to support irregular expenditure disclosed was not provided. Additional irregular expenditure was identified due to non-compliance with supply chain regulations which was not accounted for. | <ul style="list-style-type: none"> Lack of an adequate record management system The increase in irregular expenditure is mainly attributed in the municipality not emphasising the importance of ensuring compliance with laws and regulations. Most of the contracts awarded by the municipality were assessed as irregular. The officials within the SCM department also lacked adequate skills to understand some of the applicable laws and regulations. | <ul style="list-style-type: none"> Implement records management processes and systems to ensure that documents are properly filled, controlled and easily retrieved when required. Implementation of key basic controls such as monthly reconciliations, systems controls over journal processing and quarterly reviewed financial statements basis. These controls should be executed by the municipality’s own officials throughout the course of the financial year to ensure errors are timeously detected and addressed prior the submission of the annual financial statements for audit. |



Predetermined objectives qualification areas

Development priority – Basic service delivery and infrastructure development

| Finding | Root cause | Recommendation |
|---|--|--|
| <p>Reported achievements (targets) not consistent with the planned indicators for the following indicators:</p> <ul style="list-style-type: none"> - Number of roads programmes completed by 30 June 2018 in Letlhakeng Village Moses Kotane Local Municipality - Number of sanitation projects constructed in Mazista and Derby (Kgetlengrivier Local Municipality) by 30 June 2018 - Number of structures constructed in Mmakau Village, Madibeng Local Municipality by 30 June 2018 | <ul style="list-style-type: none"> • Inadequate planning when indicators are developed. Indicators are not relevant to the mandate and function of the municipality. • Lack of standard operating procedures that predetermine how the achievement would be measured, monitored and reported. • Inadequate review of the annual performance report. | <ul style="list-style-type: none"> • Review of the indicators and targets in the SDBIP to ensure this is aligned to the mandate and powers and functions of the district municipality. • Development of standard operating procedures that set out how each indicator would be measured, monitored and reported. • Quarterly reports to be reviewed and targets reported for each quarter to be validated |
| <p>Reported achievement (target) did not agree with evidence provided for the following indicators:</p> <ul style="list-style-type: none"> - Number of public awareness campaigns conducted in BPDM by 30 June 2018 - Number of waste recovery awareness campaigns implemented in 5 local municipalities by 30 June 2018 | | |
| <p>Sufficient appropriate evidence not available to support reported achievement for the following indicator:</p> <ul style="list-style-type: none"> - Procurement of disaster equipment in support of local municipalities | | |



Key focus areas

The table below provides an extract of the municipality’s performance broken down into specific key areas. The colour attached to each area represents the severity of the concerns noted within the key area.

| | |
|---------------------------------------|--|
| ■ | Good – minor issues noted and reported |
| ■ | In progress – resolution of concerning issues raised is in progress |
| ■ | Intervention required – matters raised require urgent attention |

| | |
|--|--|
| <i>Quality of submitted financial statements</i> | <p>Quality of financial statements submitted were poor.</p> <p>Basic accounting errors were identified which could have been prevented had reasonable due care been exercised.</p> |
| <i>Quality of submitted annual performance reports</i> | <p>The quality of the performance report had also deteriorated compared to prior year. The number of material misstatements identified compared to prior years has increased.</p> |



| | |
|--|--|
| <p><i>Supply chain management, and unauthorised, irregular as well as fruitless and wasteful expenditure</i></p> | <p>A number of non-compliance findings were identified on the supply chain management process. This include:</p> <ul style="list-style-type: none"> - Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotation. - Quotations were accepted from bidders who did not submit a declaration on whether they are employed by the state. - Quotations were accepted from bidders whose tax matters had not been declared. - Goods and services of a transaction value above R200 000 were procured without inviting competitive bids. Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids. - The preference point system was not applied in the procurement of goods and services above R30 000. - Persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest. <p>The non-compliance matters identified above have resulted in irregular expenditure of R304 178 972</p> <p>The municipality did not have adequate systems in place to identify and record all unauthorised expenditure throughout the year.</p> |
| <p><i>Financial health</i></p> | <p>The municipality's total liabilities exceed its total assets by R27 133 040.</p> <p>Trade payables disclosed in the financial statements at year end amount to R20 499 567, whereas the cash on hand at 30 June 2018 was R2 339 601. This is an indication that the municipality does not have sufficient cash to settle its short term obligations.</p> |
| <p><i>Vacancies and stability, competencies, management of consultants and consequence management</i></p> | <p>The CFO position was vacant for the major part of the financial year.</p> <p>Finance staff lack the appropriate competencies and do not fully understand the requirements of the financial reporting framework.</p> <p>There is an over-reliance on consultants to prepare the financial statements at year end. As a result, sustainable systems and processes were not introduced and implemented during the year for the recording, reconciling and reporting of transactions and balances.</p> <p>Consequence management was not implemented and poor performance and repeat transgressions were not dealt with.</p> |



Status of records

The Auditor-General of South Africa (AGSA) remains committed to assisting all government institutions in the process of identifying and communicating good practices to improve transparency, accountability and governance in the public sector. The purpose is to build public confidence in government's ability to account for public resources in a transparent manner.

As part of our commitment to continually assist the municipality, we have performed a high level risk assessment process for the period 2018/19, with the aim of:

- Identifying key areas of concern that may derail the department's progress in relation to the preparation of financial and performance reports and complying with the relevant legislation and ultimately result in a negative audit outcome.
- Providing our assessment of the status of the key focus areas that we reviewed.
- Assessing the progress made by the department in implementing action plans/ carrying out commitments to address areas of concern that were communicated in previous engagements with the Accounting Officer (AO).
- Identifying value-add matters that can assist in putting measures/ action plans in place well in advance in order to manage the possible risks that stem from the matters.

Our assessment was in the form of a status of records review which includes follow-up procedures and analysis of available financial and non-financial information. The assessment included a high level review of the records of the department - i.e. inspection of the municipality's internal and external reports/documents and discussions with senior managers.

The following root causes were noted from the review based on the key focus areas:

- Lack of review of the financial statements
- Lack of understanding by finance staff of basic accounting principles
- Monthly reconciliations between the financial system and subsidiary ledgers are not performed
- Where reconciliations were performed, these reconciliations were not adequate and variances were not investigated
- Basic key controls to detect and prevent errors were not implemented throughout the year as there is an over-reliance on consultants to prepare the financial statements at year end

Summary of common root causes to be addressed

1. The appropriate level of management failed to regularly review financial, performance and compliance reporting to ensure credibility of information.



2. Documented procedures relevant to both financial and non-financial information to enable and support the understanding and execution of internal control processes and responsibilities were not developed and implemented.
3. Municipal officials lack an understanding of basic accounting principles.
4. Consequence management was not implemented.

Conclusion

The municipality has structures of governance committees with suitably skilled role players with an understanding of the improvements required to achieve a clean administration. However, the effectiveness of these committee's / role players as an assurance provider is impacted by the municipality and leadership's ability to act on the recommendations made by these committees.

It is therefore critical that the root causes highlighted above are addressed to ensure good governance and an improvement in the overall audit outcomes.

