

REPORT OF THE AUDITOR-GENERAL TO PARLIAMENT ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF VOTE NO. 34 - DEPARTMENT OF WATER AFFAIRS AND FORESTRY FOR THE YEAR ENDED 31 MARCH 2007

REPORT ON THE FINANCIAL STATEMENTS

INTRODUCTION

1. I have audited the accompanying financial statements of the Department of Water Affairs and Forestry (DWAF) which comprise the statement of financial position as at 31 March 2007, appropriation statement, statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages 119 to 187.

RESPONSIBILITY OF THE ACCOUNTING OFFICER FOR THE FINANCIAL STATEMENTS

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the modified cash basis of accounting and in the manner required by the Public Finance Management Act, 1999 (Act No. 1 of 1999) (PFMA). This responsibility includes:
 - designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
 - selecting and applying appropriate accounting policies
 - making accounting estimates that are reasonable in the circumstances.

RESPONSIBILITY OF THE AUDITOR-GENERAL

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) and section 40(2) of Public Finance Management Act, 1999 (Act No. 1 of 1999), as amended by Act 29 of 1999, my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with the International Standards

on Auditing and General Notices 646 and 647 of 2007, issued in Government Gazette No. 29919 of 25 May 2007. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls.
6. An audit also includes evaluating the:
 - appropriateness of accounting policies used
 - reasonableness of accounting estimates made by management
 - overall presentation of the financial statements.
7. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

BASIS OF ACCOUNTING

8. The department's policy is to prepare financial statements on the modified cash basis of accounting determined by the National Treasury as set out in accounting policy note 1.1.

BASIS FOR QUALIFIED OPINION

Property, plant and equipment

9. The department embarked on an exercise to compile a fixed asset register. Due to the extensive asset base and complexities facing the department, this exercise had not been completed adequately by the time of the audit. In addition, the physical verification of assets to the register could not be performed and in certain cases assets procured during the financial year could not be traced to the asset register.

Accordingly, the amounts of R2.189 billion disclosed as property, plant and equipment in note 28 and R53.276 million disclosed as intangible capital assets in note 29 to the annual financial statements could not be substantiated with an adequate fixed asset register. I have therefore

been unable to obtain adequate assurance regarding the validity, completeness and accuracy of the amounts disclosed in the financial statements.

Loans, receivables and capitalisation reserve

10. An amount of R41.309 million was included in the loans, receivables and capitalisation reserve balances in the statement of financial position. This amount could not be substantiated. As a result loans, receivables and/or the capitalisation reserve could be misstated. This was due to an inadequate monitoring of the take-on balances from the previous manual system.

Cash and cash equivalents

11. The Bank Exception Account, which is a suspense account used by the department for recording unidentified deposits, amounted to R13.064 million at year-end and was included as part of cash and cash equivalents in the statement of financial position. Not all deposits could be identified timeously by the department as a result of inadequate information. As a result, cash and cash equivalents, receivables and revenue could be misstated.

Disclosure and other matters

12. Due to a lack of supporting systems in the department to facilitate recording of the necessary information, the following was noted:

- **Accruals**
The amount of R18.890 million disclosed as accruals in note 22 to the annual financial statements was not complete and accurate, as a material number of invoices relating to services received before year-end were not included. Furthermore, there were instances where invoices paid before year-end were included in the accrual listing. The amount of the misstatement could not be determined.
- **Commitments**
The amount of R277.920 million disclosed as commitments in note 21 to the annual financial statements was not complete and accurate, as material amounts for contracts awarded and orders placed were not included. Moreover, there were instances where amounts relating to contracts that had expired were included as part of commitments and amounts included could not be substantiated.

Furthermore, commitments for periods longer than one year were not disclosed correctly and in other instances the accumulative expenditure was not deducted from the amounts disclosed.

- **Related parties**
The department has no proper system or controls in place to quantify or record related party transactions. Accordingly, no disclosure of related party relationships and transactions was made in the notes to the financial statements as required by the framework prescribed by National Treasury.

Trust – financial information

13. The financial information of the National Forest Recreation and Access Trust for the 2005-06 financial year was included in the financial statements of the department as no separate financial reporting system existed for the trust. As a result, payables and cash and cash equivalents in the prior year were overstated by an amount of R3.175 million.

Qualified opinion

14. In my opinion, except for the effects of the matters referred to in the Basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Department of Water Affairs and Forestry as at 31 March 2007 and its financial performance and cash flows for the year then ended, in accordance with the modified cash basis of accounting determined by the National Treasury and in the manner required by the PFMA, as described in note 1 of the accounting policies.

OTHER MATTERS

I draw attention to the following matters that are ancillary to my responsibilities in the audit of the financial statements:

MATTERS OF GOVERNANCE

Expenditure trends

15. The expenditure for the last two months of the year amounted to 28 per cent of the total expenditure. Expenditure was not monitored on a continuous basis during the year. As a result, substantial expenditure increases towards the end of the year had the effect of avoiding the surrendering of unutilised funds.

Segregation

16. Inadequate segregation between the main and trading account existed due to the lack of a formal structure and related processes for the trading entity. As a result, a significant number of journals were processed to allocate expenditure between the main and trading account.

Governance

17. I could not rely on the work of internal audit as planned, as the internal audit reports relating to the work performed on the planned areas of reliance were not completed timeously.

NON-COMPLIANCE WITH APPLICABLE LEGISLATION

Division of Revenue Act

18. Due to inadequate planning and budgeting, the transfer agreements with municipalities were not timeously finalised to facilitate the transfers in terms of the Division of Revenue Act, 2006 (Act No. 2 of 2006) (DoRA). As a result, amounts were not always transferred to municipalities according to the allocations of schedules 6 and 7 of DoRA.

As a result of a lack of monitoring and control mechanisms in the department, evidence could not be provided that the performance of programmes funded or partially funded was evaluated in terms of section 25 (6) of DoRA. Furthermore, the annual report of the department did not indicate the extent to which the capacity of any municipality was improved in terms of section 12.3 of DoRA.

Public Finance Management Act

19. No assurance could be obtained from the department that the eight municipalities to whom advances were made amounting to R49.673 million, included in the prepayments and advances line item in the statement of financial position, had effective, efficient and transparent financial management and internal control systems as required by section 38(1)(j) of the PFMA.

Departmental policies and procedures

20. The following instances of non-compliance with departmental financial rules relating to the administration of debt, which were due to the inadequate administration and monitoring of these debts, were noted:
- Included in debtors were long outstanding balances that had shown no movement since 2002 and 2003.
 - Debtors were not handed over to the state attorney within 14 days after second reminder.
 - Employees were not terminated timeously on PERSAL upon resignation or death, with the result that 47 per cent of staff debtor balances related to salary overpayments.

State guarantees

21. Due to a lack of monitoring, instances were identified where employees whose services were terminated were still reflected in the list of state guarantees, as these guarantees were not cancelled with the financial institutions.

Performance audit reports issued during the year

22. A performance audit was performed on the provision of sanitation services. This performance audit will be tabled separately when finalised.

Value for money matters

23. The department's human resource plan had not been approved at the time of the audit, although it had a vacancy rate of approximately 19.32 per cent for the year under review.

Material corrections made to the financial statements submitted for audit

24. The following material corrections were made during the audit process to the financial statements submitted for audit on 31 May 2007, due to inadequate or lack of financial reporting systems:
- An adjustment of R16.980 million was made to increase commitments.
 - R3.435 million relating to financial information of the Trust was taken out of payables and cash & cash equivalents.
 - A provision for irrecoverable loan balances amounting to R36.847 million was made in note 30 to the annual financial statements.

SCOPA resolutions

25. A hearing attended by SCOPA and the department was held on 13 March 2007. At the date of finalisation of this report the draft resolutions with regard to the 2005-06 financial period had not been adopted.

Delay in finalisation of audit

26. Due to the national public sector strike action during June 2007, the finalisation of the audit for the 2006-07 financial year was delayed until the date of this report.

OTHER REPORTING RESPONSIBILITIES

Reporting on performance information

27. I have audited the performance information as set out on pages 119 to 187.

Responsibility of the accounting officer

28. The accounting officer has additional responsibilities as required by section 40(3)(a) of the PFMA to ensure that the annual report and audited financial statements fairly present the performance against predetermined objectives of the department.

Responsibility of the Auditor-General

29. I conducted my engagement in accordance with section 13 of the Public Audit Act, 2004 (Act No. 25 of 2004) read with General Notice 646 of 2007, issued in Government Gazette No. 29919 of 25 May 2007.

30. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate audit evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.

31. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit conclusions reported below.

Audit findings

The following deficiencies were noted due to a lack of documented policies and procedures to govern the collection, recording and reporting of performance information:

32. No policies and procedures existed to facilitate effective monitoring, evaluation and corrective action, in contravention of Treasury Regulation 5.3.
33. The financial statements of the department included the performance information of the Water Trading Account as the Water Trading Account did not have separate information. Clearly defined objectives for the department and trading entity were not included in the strategic plan of the department to facilitate proper reporting.
34. Several inconsistencies appeared in the objectives of the strategic plan, budget and annual report. Not all objectives could be measured in terms of percentage of completion, timing, quantity and quality.
35. Information reported in the annual report could not be verified against the predetermined objectives as set out in the strategic plan. Information reported in quarterly reports could not be substantiated by source documents such as closeout reports, feasibility study reports, attendance register of training courses and minutes of meetings.

APPRECIATION

36. The assistance rendered by the staff of the Department of Water Affairs and Forestry during the audit is sincerely appreciated.



P Bhana for Auditor-General

Pretoria

31 August 2007



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