



Local government audit outcomes | 2017-18

**Accountability for financial and performance
management continues to deteriorate**



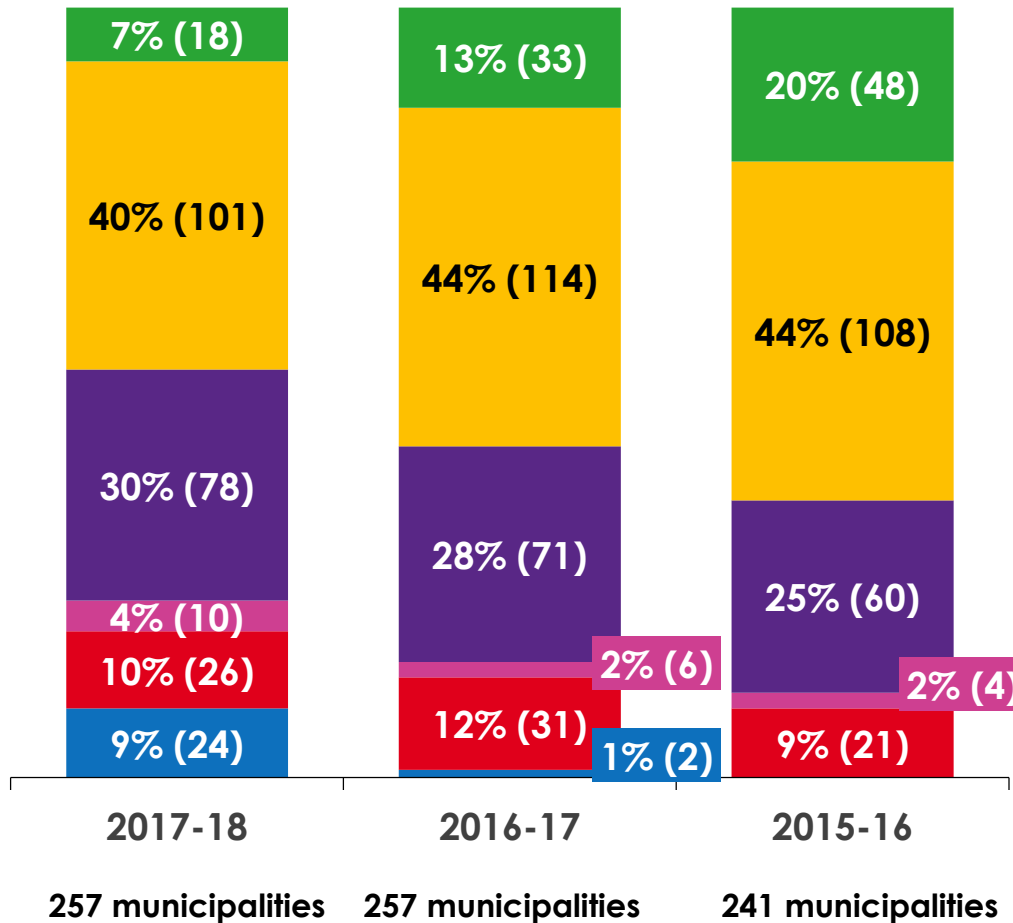
AUDITOR-GENERAL
SOUTH AFRICA

Reputation promise

The Auditor-General of South Africa (AGSA) 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.



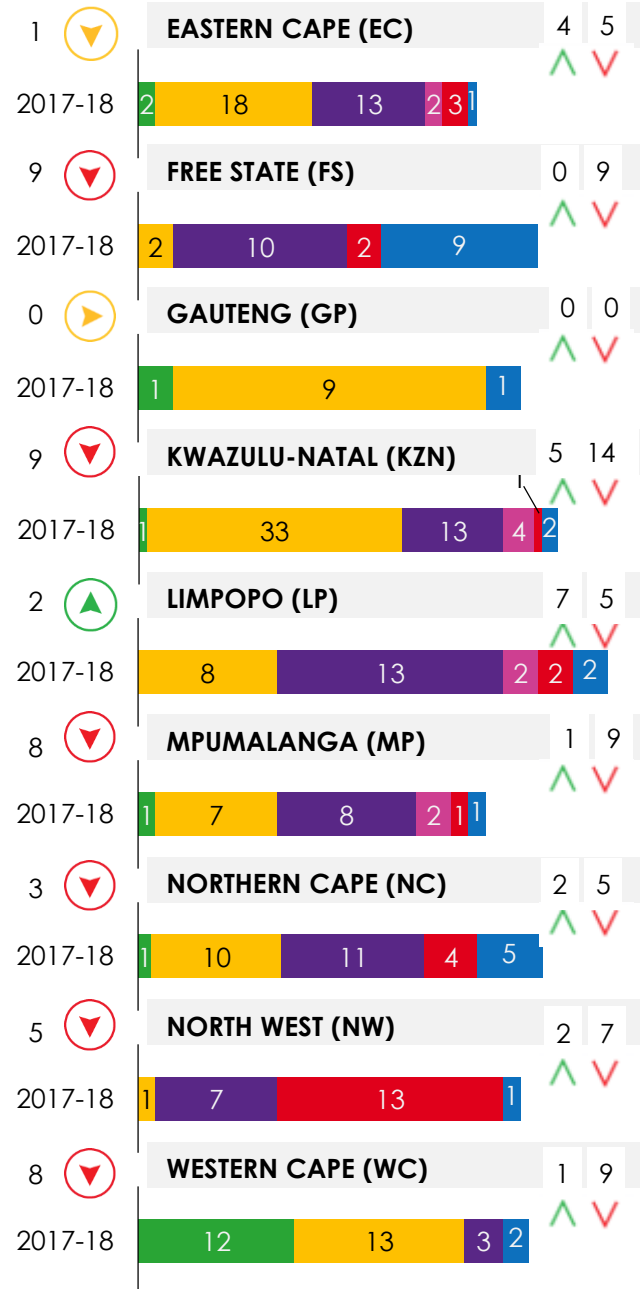
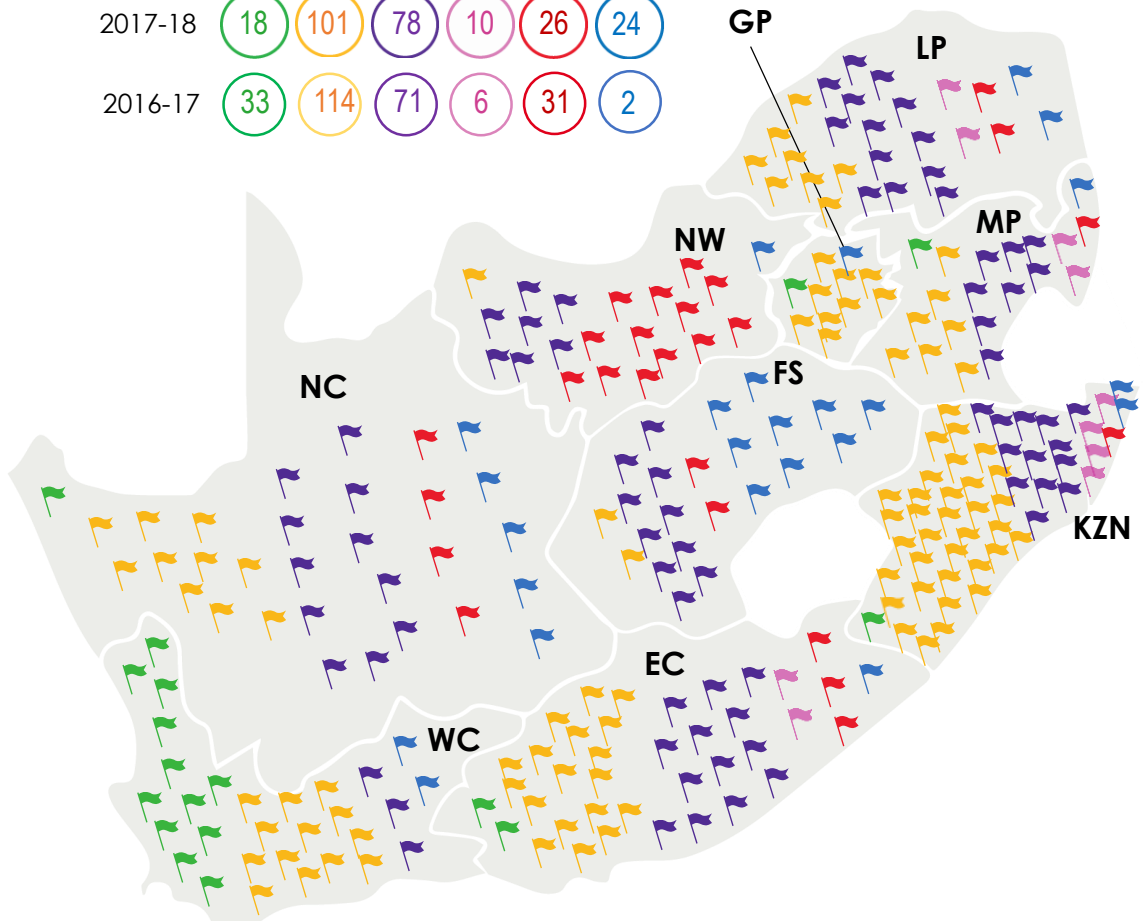
In the second year of administration, audit outcomes continue to regress



Movement	
▲	22
▼	63
▶	148
Outstanding audits as at 31 January 2019	24



Movement in audit outcomes



Accountability continues to deteriorate

Impact

Key issues

Financial statements

- Late submission of financial statements
- Quality of financial statements submitted for audit very poor
- Quality of published financial statements worse than previous year

Performance reports

- Quality of performance reports submitted for auditing slightly improved
- Performance indicators and targets not useful
- Achievement reported not reliable

Compliance with key legislation

- Material non-compliance with key legislation on financial and performance management continues to escalate
- Material non-compliance identified at all metros

Supply chain management and irregular expenditure

- Material non-compliance with supply chain management widespread – highest since 2011-12
- Irregular expenditure decreased but remained high

Effecting consequences

- Material non-compliance with legislation on implementing consequences regressed
- Inadequate follow-up of allegations of financial and supply chain management misconduct and fraud
- Council failed to conduct investigations into all instances of UIFW
- Sufficient steps not taken to recover, write-off, approve or condone UIFW

Difficult environment

- Increased contestations, pushbacks, treats and intimidation
- Regular service delivery protests
- Lack of commitments towards implementing recommendations that enable improved audit outcomes

Financial health

- Financial health status of 76% of municipalities is concerning or require intervention
- Inability to collect debt
- 34% of municipalities disclosed a deficit
- 87% of municipalities exceeded 30-day payment period (average payment-period 174 days)
- Total outstanding debt (R18,28 billion owed to Eskom and R9,05 billion owed to water boards)
- 31% of municipalities in vulnerable financial position
- Financial losses suffered at 14 municipalities due to VBS investments – R1,6 billion write-off
- 18 municipalities placed under administration

Delivery and maintenance of infrastructure

- No or poor service delivery due to underspending of grants, poor project management and delays and non-compliance with supply chain management legislation
- Condition of water and sanitation infrastructure not assessed by 32% of municipalities
- 39% of municipalities disclosed water losses of more than 30% - loss of R2,6 billion
- Condition of roads not assessed (23%) and no road maintenance plan (41%)



Accountability continues to deteriorate/ deteriorations marked with an X

Key issues		Eastern Cape	Free State	Gauteng	KwaZulu-Natal	Limpopo	Mpumalanga	Northern Cape	North West	Western Cape
Financial statements	Late submission of financial statements – 11% (2016-17: 10%)	X	X				X	X	X	X
	Financial statements submitted for auditing contained material misstatements - 81% (2016-17: 77%)		X	X	X	X	X		X	X
	Quality of published financial statements worse than previous year – 119 municipalities received unqualified audits (2016-17: 143 municipalities)	X	X		X	X	X	X	X	X
Performance reports	Performance reports submitted for auditing contained material misstatements - 89% (2016-17: 90%)	X	X		X	X	X	X	X	
	Performance indicators and targets not useful – 55% (2016-17: 51%)	X	X			X	X		X	
	Achievement reported not reliable – 53% (2016-17: 52%)	X	X			X			X	
Compliance with key legislation	Material non-compliance with key legislation on financial and performance management – 92% (2016-17: 85%)	X	X	X	X	X	X	X	X	X
	Material non-compliance identified at all metros	X		X	X					X
Supply chain management and irregular expenditure	Material non-compliance with supply chain management widespread – 81% (highest since 2011-12) (2016-17: 72%)	X	X	X	X	X	X	X	X	X
	Overall irregular expenditure decreased although some provinces showed an increase		X		X			X		X



Accountability continues to deteriorate/ deteriorations marked with an X

Key issues		Eastern Cape	Free State	Gauteng	KwaZulu-Natal	Limpopo	Mpumalanga	Northern Cape	North West	Western Cape
Effecting consequences	Material non-compliance with legislation on implementing consequences – 60% (2016-17: 54%)	X	X	X	X	X	X	X	X	X
	Inadequate follow-up of allegations of financial and supply chain management misconduct and fraud – 74% (2016-17: 66%)	X	X	X	X	X	X	X	X	X
	Council failed to conduct investigations into all instances of UIFW – 62% (2016-17: 60%)	X	X	X	X	X	X	X	X	X
	Sufficient steps not taken to recover, write-off, approve or condone UIFW	X	X	X	X	X	X	X	X	X
Difficult environment	Increased contestations, pushbacks, threats and intimidation	X		X	X	X	X	X	X	X
	Regular service delivery protests	X	X	X	X	X	X	X	X	X
	Lack of commitments towards implementing recommendations that enable improved audit outcomes - No response most evident in Free State and North West	X	X		X	X	X	X	X	
Municipalities under administration		X			X	X	X		X	
VBS investments				X		X			X	



Accountability and transparency not enabled through credible financial and performance reporting



Financial statements

Target

Submission of financial statements by legislated date (all municipalities)

Movement



2017-18

2016-17

89%

90%

Quality submission for auditing



19%

23%

Quality of published financial statements



51%

61%

32% achieved unqualified opinions only because they corrected all misstatements identified during the audit



Performance report

Target

Preparation of performance reports

Movement



2017-18

2016-17

97%

98%

Quality submission for auditing



11%

10%

Quality of published performance report



35%

38%

Reliable reporting of achievements



47%

48%

Usefulness of performance indicators and targets



45%

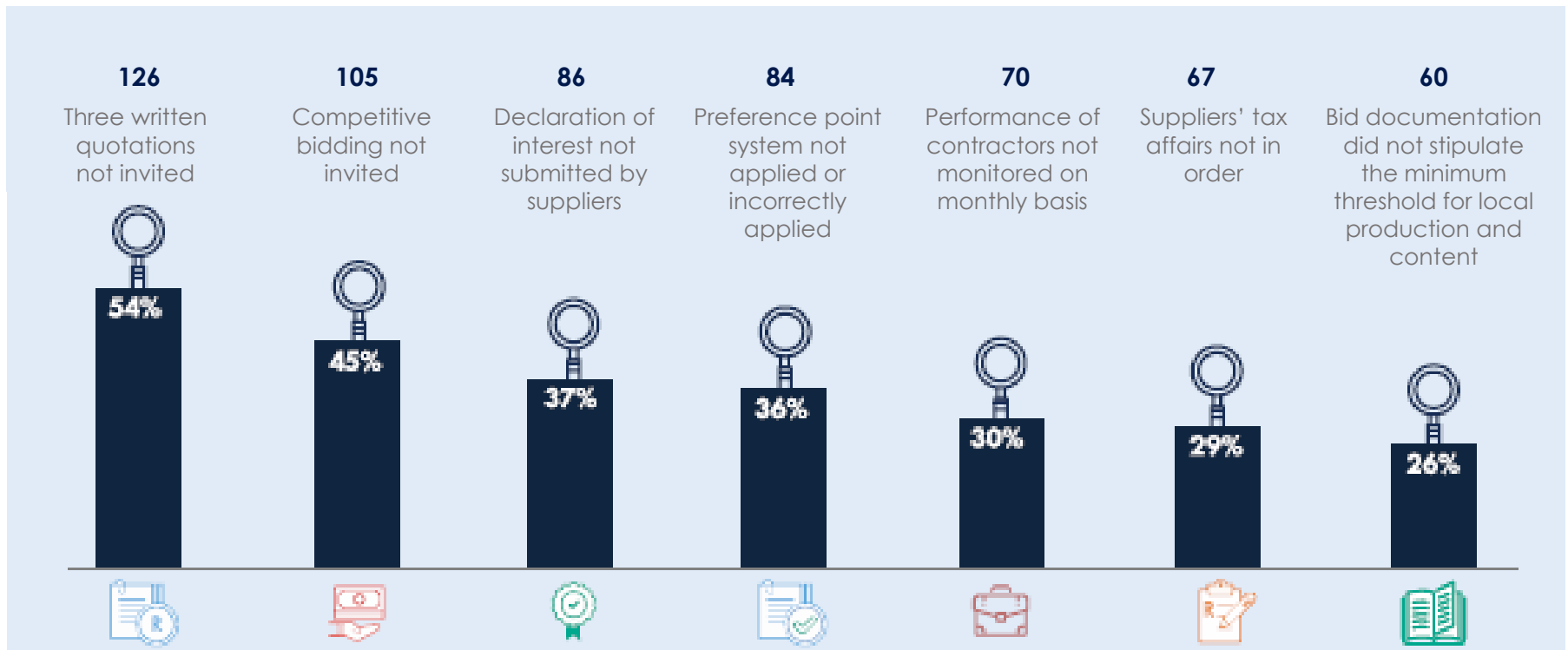
49%

24% had no material findings only because they corrected all misstatements identified during the audit

Non-compliance with supply chain management legislation is widespread

Unfair or uncompetitive procurement processes – most often lead to **higher prices or potential losses** and exclusion of preferential suppliers (including local suppliers), which undermines the country's **social transformation goals**.

The most common findings were:



Irregular Expenditure - 3Ms



(Hu)Mans

humans are given power to apply money in obtaining material for service delivery

Money

the money must be applied in accordance with applicable legislation

Material

the materials must be used to secure quality service delivery to the citizens

Irregular expenditure remains high



Annual irregular expenditure decreased from R29,7 billion to **R25,2 billion***

[Included in these figures is irregular expenditure of R4 billion (2016-17: R2,08 billion) as disclosed in the unaudited financial statements of the **24 municipalities of which the audit outcomes were outstanding**]

* The figure is not complete because:

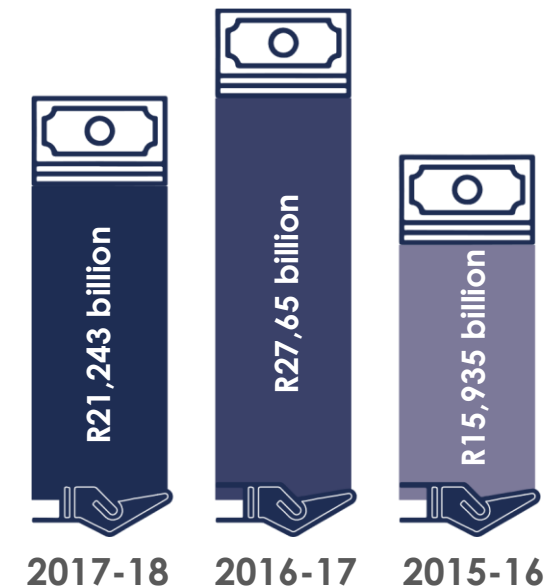
- **58 municipalities (25%)** were qualified on incomplete disclosure of irregular expenditure while **40 municipalities (17%)** were qualified on the accuracy of irregular expenditure the disclosure. At an overall **61 municipalities (26%)** were qualified on irregular expenditure .

Annual irregular expenditure

(as per audited financial statements)

The number of municipalities incurring irregular expenditure slightly increased from 211 to 219

- **81%** (R17,262 billion) were payments or expenses in 2017-18
 - **R10,819 billion** represents non-compliance in 2017-18
 - **R6,443 billion** is expenditure on ongoing multi-year contracts
- **19%** (R3,981 billion) were payments or expenses in previous years only uncovered and disclosed in 2017-18



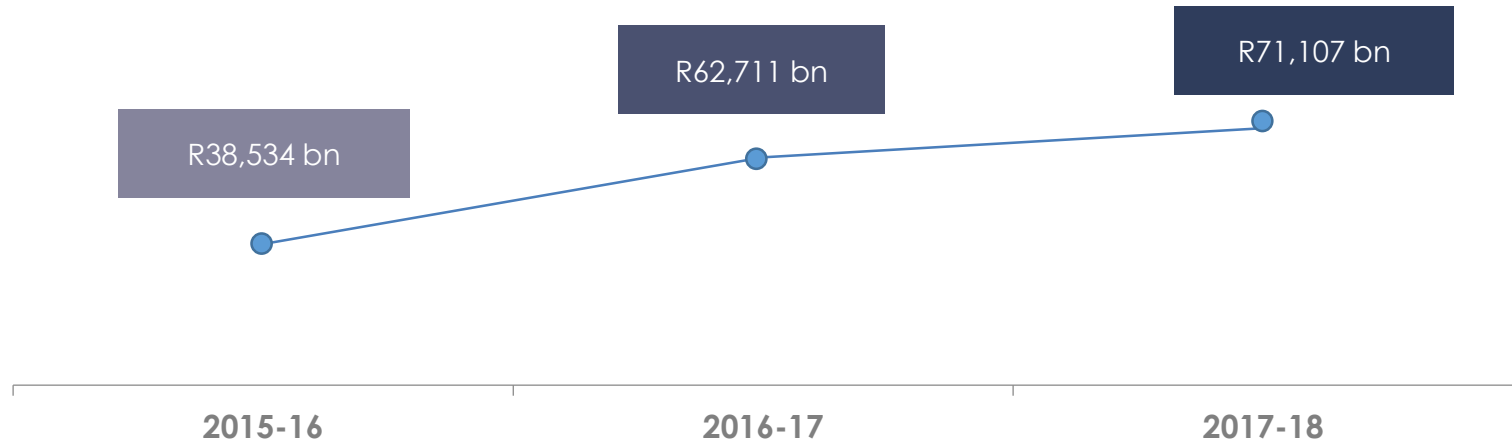
How can irregular expenditure on multi-year contracts be reduced?

Through **investigation**, followed by **condonement** or **cancellation** as provided for in legislation of contracts irregularly awarded



Irregular expenditure remains high

Closing balance of irregular expenditure



Irregular expenditure of previous years is not properly dealt with through investigation, and followed by **condonement, recovery** or **write-off** of the expenditure

Top 5 contributors to the accumulated irregular expenditure (constitutes 32% of R71,107 billion) which also did not **investigate all instances** of the prior year's irregular expenditure were:

- Nelson Mandela Bay Metro (EC) – R12,379 billion
- OR Tambo District (EC) – R3,151 billion
- City of Matlosana (NW) – R2,748 billion
- City of Johannesburg Metro (GP) – R2,724 billion
- Mogalekwena (LP) – R1,718 billion



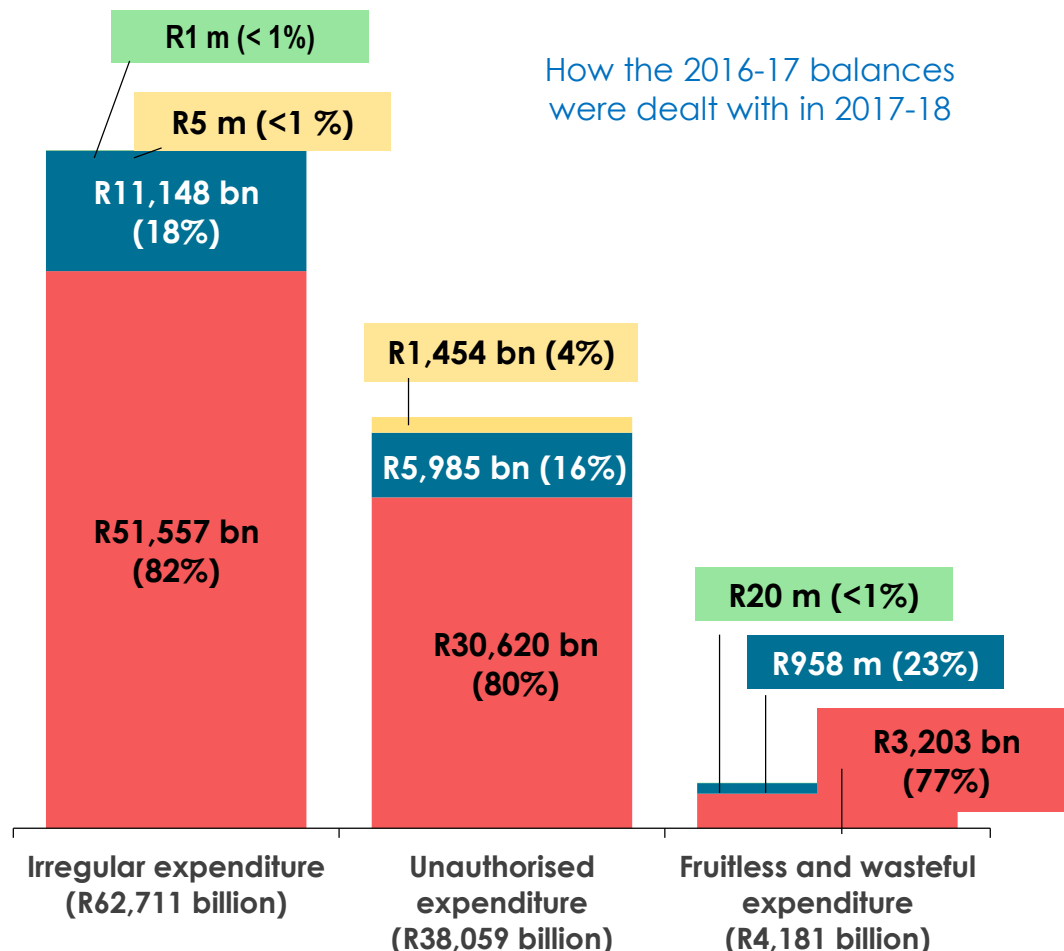
Material non-compliance with legislation on implementing consequences increased from 54% to 60%

Most common findings were that unauthorised, irregular and/or fruitless and wasteful expenditure were not being investigated:

- Irregular expenditure – 125 municipalities (54%)
- Fruitless and wasteful expenditure – 117 municipalities (50%)
- Unauthorised expenditure – 108 municipalities (46%)



How the 2016-17 balances were dealt with in 2017-18



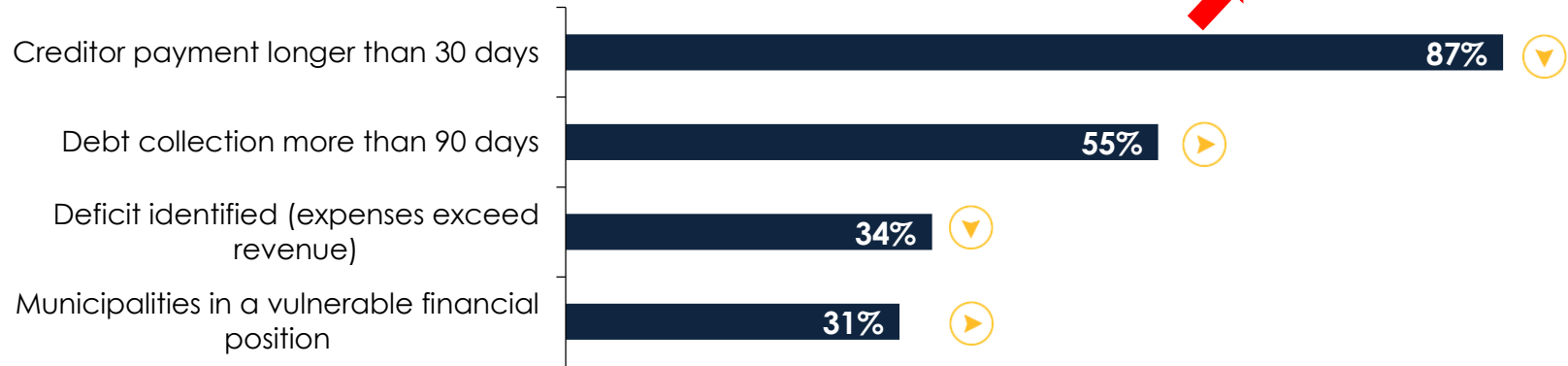
■ Money recovered
 ■ Condoned or authorised
 ■ Written off by council
 ■ Not dealt with by council



Declining financial health and losses

53257
281760
260935

What the numbers say



The average payment period was 174 days – affecting the sustainability of suppliers

- **Unauthorised expenditure increased from R11 157 million to R12 851 million; R7 004 million of R12 851 million was as a result of non-cash items; Nearly 100% of unauthorised expenditure was as a result of overspending**
- **Fruitless and wasteful expenditure decreased slightly from R1 549 million to R1 332 million**



VBS investments

The MFMA prohibited municipalities from investing in mutual banks. 16 municipalities invested in VBS mutual bank.

Two municipalities were able to withdraw the investments in time, but **14** municipalities had investments with VBS Mutual Bank when it was placed under curatorship

Gauteng (2)	Limpopo (8) – 72% of the loss	North West (4)
<ul style="list-style-type: none"> West Rand District Merafong 	<ul style="list-style-type: none"> Makhado Greater Giyani Collins Chabane Elias Motsoaledi Vhembe District Ephraim Mogale Fetakgomo Tubatse Lepelle-Nkumpi 	<ul style="list-style-type: none"> Dr Ruth S Mompati District Mahikeng Moretele Madibeng

Total invested at year-end was **R1,6 billion** – the investments are considered irrecoverable

An estimated **32%** of the funds invested were from grants intended to fund infrastructure projects

The financial losses suffered gave rise to:

- Projects that were to be funded by the invested money could not begin.
- Projects were delayed or completed late.
- Future projects will also be affected, as some of the funds were earmarked for longer term capital projects.
- The financial position of the municipalities weakened significantly, leading to unauthorised expenditure, deficits, bank overdrafts, and insufficient funds to cover their liabilities.



Municipalities requiring special intervention

48 municipalities were identified requiring special intervention from national and provincial role players to improve audit outcomes.

The worst performing municipalities in each province were selected based on their history over 3 years of:

- Disclaimed or adverse audit opinions, or
- A poor financial health assessment, or
- Unauthorised, irregular and fruitless and wasteful expenditure

Of the identified municipalities:

23 were also highlighted for special intervention in our 2015-16 general report

7 are receiving attention from provincial leadership through provincial interventions and/ or administration



Municipalities requiring special intervention – continued

Eastern Cape (7)	Free State (11)	Gauteng (1)	KwaZulu-Natal (4)
<ul style="list-style-type: none"> • Dr Beyers Naudé • Enoch Mgijima ▲ • Inxuba Yethemba ● • Makana ● • Mbizana ● • Raymond Mhlaba • Walter Sisulu 	<ul style="list-style-type: none"> • Kopanong • Letsemeng ● • Mafube ● • Maluti-A-Phofung ● • Mantsopa ● • Matjhabeng ● • Masilonyana • Nala ● • Ngwathe ● • Nketoana • Phumelela ● 	<ul style="list-style-type: none"> • Rand West City 	<ul style="list-style-type: none"> • AbaQulusi • Inkosi Langalibalele ▲ • Mpofana ▲ • uMkhanyakude District ●

● Municipalities also identified in 2015-16 for intervention

▲ Municipalities subject to provincial interventions and/or administration



Municipalities requiring special intervention – continued

Limpopo (6)	Mpumalanga (2)	Northern Cape (7)	North West (8)
<ul style="list-style-type: none"> Fetakgomo Tubatse Modimolle-Mookgophong ▲ Mogalakwena Mopani District Thabazimbi ● Vhembe District ● 	<ul style="list-style-type: none"> Emalahleni ▲ ● Thaba Chweu ▲ ● 	<ul style="list-style-type: none"> Ga-Segonyana ● Joe Morolong Kamiesberg ● Magareng ● Nama Khoi ● Renosterberg ● Tsantsabane ● 	<ul style="list-style-type: none"> Bojanala Platinum District Ditsobotla ▲ ● Lekwa-Teemane Madibeng Mahikeng Mamusa ● Moses Kotane Ngaka Modiri Molema District

Western Cape (2)
<ul style="list-style-type: none"> Kannaland ● Laingsburg

- Municipalities also identified in 2015-16 for intervention
- ▲ Municipalities subject to provincial interventions and/or administration





AUDITOR - GENERAL
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PAA amendments – the key expansion to our mandate

Audit

Report

For
Accountability

What is a material irregularity?

Definition from the Amendment Act

irregularity

“Material irregularity” means any non-compliance with, or contravention of, legislation, fraud, theft or a breach of a fiduciary duty ...



material irregularity

***identified during an audit performed** under this Act that resulted in or is likely to result in ...*

material

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.



Our expanded mandate



Refer material irregularities to relevant public bodies for further investigations



Take binding remedial action for failure to implement the AG's recommendations for material irregularities



Issue a certificate of debt for failure to implement the remedial action if financial loss was involved



Effective date of amendments to PAA is 1 April 2019

The Municipal Finance Management Act (MFMA) – responsibilities of accounting officers

The PAA amendments emphasise the existing provisions that are already in the different legislations

Key general responsibilities of accounting officers of municipalities (s.62) and municipal entities (s. 95)

- Effective, efficient and transparent systems of **financial and risk management** and **internal control**
- Effective, efficient, economical and transparent use of **resources**
- **Prevention of UIFW** expenditure and other losses
- Ensure **full and proper records** of the financial affairs are kept
- Implementation of a tariff policy, a rates policy and a credit control and debt collection policy and **a supply chain management policy**
- Take **disciplinary** or, when appropriate, **criminal proceedings** against any official of the municipality who has allegedly committed an act of financial misconduct



Responsibilities - financial misconduct (MFMA sections 171/172)

An accounting officer of a municipality or municipal entity **commits an act of financial misconduct** if deliberately or negligently –

- **Contravenes a provision in the MFMA**
- Makes or permits or instructs another official to **incur UIFW expenditure**
- **Provides incorrect or misleading information** to the mayor, council, AGSA, National Treasury or other organs of state and the public

Officials commit financial misconduct if deliberately or negligently fails to carry out delegated duty, makes or permits or instructs another official to incur UIFW expenditure or provides incorrect or misleading information to the accounting officer

A municipality/municipal entity must **investigate allegations of financial misconduct** and, where warranted, **institute disciplinary proceedings**

The financial misconduct regulations provides requirements for dealing with financial misconduct, including that the allegation should be referred to the disciplinary boards within 7 days after receiving report of the allegation.



Responsibilities - dealing with corruption and abuse

Accounting officers responsibilities to prevent and combat corruption and corrupt activities (PRECCA sec. 34)

- Known / suspected instances of corruption, theft, fraud, extortion, forgery or uttering a forged document, involving an amount of R100 000 or more, should **reported to the SAPS.**

Key accounting officers or authorities responsibilities to avoid supply chain management (SCM) system abuse (SCM regulation 38)

- take all reasonable steps to **prevent abuse** of the SCM system.
- **investigate any allegations** against an official or other role player of fraud, corruption, favouritism, unfair or irregular practices or failure to comply with the SCM policy
- when justified, **take** appropriate **steps** against such official or other role player **report to SAPS**
- **cancel a contract** awarded to a supplier if the supplier /any role player committed any corrupt or fraudulent act during the bidding process or the execution of that contract



Role of oversight

In line with the oversight's mandate, the relevant committee may:

- **Consider the AG's accountability report** that provides information on the material irregularities raised during the specific audit cycle
- **Request regular updates** from the accounting officers / authorities on the implementation of the AG's recommendation
- **Convene oversight discussions** with any organs of state
- **Set the tone** for accountability and consequence management by investigating and dealing with any allegations of financial misconduct and irregularities by accounting officers and authorities and **monitor the progress of investigations**



Implementation of expanded mandate **2018-19**

To allow for establishing capacity and processes, a **phased approach** for implementation was agreed with SCoAG.

The basis of the approach are:

1. the type of material irregularity to be identified and reported
2. Implementation only at a selection of auditees

Type of material irregularity

Type of material irregularity = Material non-compliance (which would be reported in the audit report) that resulted in (or is likely to result in) a material financial loss

Selection of auditees

Selection criteria

- Latest audit outcome not clean or unqualified with findings – except if there was a material finding on prevention or follow-up of irregular expenditure
- High irregular expenditure over the last three years
- Sufficient coverage across spheres of government and provinces.



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ACCOUNTABILITY = PLAN + DO + CHECK + ACT

