

**OVERSIGHT REPORT ON THE ANNUAL REPORT
OF THE ELUNDINI MUNICIPALITY FOR THE YEAR
ENDED 30 JUNE 2017**

1. PREAMBLE

The Elundini Municipality's Municipal Public Accounts Committee (MPAC) has been established in terms of the municipality's Standing Rules and Orders, which also provide the terms of reference for the committee. The primary functions of MPAC have been articulated in the Standing Rules and Orders as follows: -

- a) To consider and evaluate the content of the annual report and to make recommendations to Council when adopting an oversight report on the annual report;
- b) In order to assist with the conclusion of matters that have not been finalized, information pertaining to past recommendations made on the annual report must also be reviewed. This relates to quarterly in-year reports, mid-year and annual reports;
- c) To examine financial statements and audit reports of the municipality, and in doing so, the committee must consider improvements from the previous statements and reports and must evaluate the extent to which the Audit Committee's and Auditor General's recommendations have been implemented;
- d) To provide good governance, transparency and accountability on the use of municipal resources;
- e) To recommend and undertake an investigation, after reviewing any investigation report already undertaken by the municipality or Audit Committee; and
- f) To perform any other functions assigned to it through a resolution of Council within its area of responsibility.

The terms of reference further direct that the MPAC shall have permanent referral of documents as they become available relating to:-

- I. In-year reports of the municipality and municipal entities
- II. Annual financial statements of the municipality and municipal entities;
- III. Audit opinion, other reports and recommendations from the Audit Committee;
- IV. Information relating to compliance in terms of sections 128 and 133 of the MFMA;
- V. Information in respect of any disciplinary action taken in terms of the MFMA where it relates to an item that is currently serving or has served before the committee;
- VI. Any other audit report from the municipality or its entity; and
- VII. Performance information of the municipality and municipal entities.

At its meeting held in the Maclear Town Hall on 23 August 2016, the municipal council appointed the following councilors to serve in the Municipal Public Accounts Committee:

- (i) Councilor M Marubelela (Chairperson)
- (ii) Councilor M Telile
- (iii) Councilor X P Majikijela
- (iv) Councilor L Lubanga
- (v) Councilor K Mahlelebe
- (vi) Councilor Z Thwethiso

Subsequent to the appointment of the above councilors, Council further endorsed the membership of Chief M S Moshoeshe who is a nominee of the Traditional Leaders serving in council.

In order to minimize the potential for conflict of interest, Council has divested all members of MPAC of any further responsibilities in the committees of Council.

2. INTRODUCTION

The Mayor of the Elundini Municipality has, in terms of section 127(2) of the Municipal Financial Management Act 56 of 2003 (MFMA), read with section 58 of the same Act, tabled before a Special Meeting of the Council held on the 31 January 2018, an annual report of the Elundini Municipality for the year ended 30 June 2017. The annual report was prepared in terms of section 121 of the MFMA and section 46 of the Municipal System Act No 32 of 2000 (MSA).

Section 129 of the MFMA requires the Council of a municipality to consider the annual report and by no later than two months from the date on which the annual report was tabled in the Council in terms of section 127, to adopt an oversight report containing the council's comments on the annual report, which must include a statement whether the council:-

- I. Has approved the annual report with or without reservations;
- II. Has rejected the annual report; or
- III. Has referred the annual report back for revision of those components that can be revised.

Following the tabling of the annual report for the year ended 30 June 2017, the MPAC has developed a schedule of meetings for its intense consideration and the development of an oversight report. The meetings were sat as follows: -

Date of Meeting	Members in attendance	Major focus	Special Invitees
9/3/2018	<ul style="list-style-type: none">• Cllr M Marubelela• Cllr L Lubanga• Cllr Z L Thwethiso• Cllr M Telile• Cllr X Majikijela• Chief M S	Irregular expenditure	

	Moshoeshoe		
14/3/2018	<ul style="list-style-type: none"> • Cllr M Marubelela • Cllr L Lubanga • Cllr Z L Thwethiso • Cllr X Majikijela • Chief M S Moshoeshoe 	<ul style="list-style-type: none"> • Audited annual financial statements • Audit report • Audit action plan • Performance report 	Elundini Audit Committee chairman, Mr Thys de Beer CA(SA)
22/3/2018	<ul style="list-style-type: none"> • Cllr M Marubelela • Cllr L Mahlelebe • Cllr Z L Thwethiso • Cllr X Majikijela • Cllr M Telile 	<ul style="list-style-type: none"> • State of Records Review • CFO's presentation on irregular expenditure as disclosed in the AFS 	<ul style="list-style-type: none"> • Ms V Matanda, Senior Manager, Office of the Auditor General

Additional to the special invitees, and as a standard practice, members of the Elundini Municipality's management team were invited to attend meetings, particularly to give technical guidance on some of the matters as they appear in the annual report, as well as to account for those areas as the MPAC deemed it necessary.

A. Components of the annual report

Section 121 (3) of the MFMA prescribes that the annual report of the Elundini Municipality must include the following:-

- Annual Financial Statements of the municipality as submitted to the Auditor General for audit in terms of section 126 (1);
- The Auditor General's audit report in terms of section 126 (3) on those financial statements;
- The Annual Performance Report of the municipality prepared by the municipality in terms of sections 46 of the MSA;
- The Auditor General's audit report in terms of section 45 (b) of the MSA;

- An assessment by the municipality's accounting officer of any arrears on municipal taxes and service charges;
- An assessment by the municipality's accounting officer of the municipality's performance against measurable performance objectives referred to in section 17(3)(b) (of the MFMA) for revenue collection from each revenue source and for each vote in the municipality's approved budget for the relevant financial year;
- Particulars of any corrective action taken or to be taken in response to issues raised in the audit reports referred to in paragraph (b) and (d);
- Any explanations that may be necessary to clarify issues in connection with the financial statements;
- Any information as determined by the municipality;
- Any recommendations of the municipality's audit committee; and
- Any other information as may be prescribed.

B. Analysis of the annual report for the year ended 30 June 2017 and the observations by the MPAC

1. IRREGULAR EXPENDITURE – R6 645 697

The Chief Financial Officer was invited to provide reasons for the incurrence of the irregular expenditure. The irregular expenditure had not been disclosed in the original annual financial statements(AFS) submitted on 31 August 2018 but had been unearthed during the audit process, resulting in the AFS being amended with the inclusion, inter alia, of this item. The contributing factors to the irregular expenditure were outlined as follows: -

- **Regulation 32 of the SCM Regulations – R3 974 460**

The belated disclosure of this transaction as irregular emanates from a divergence of views between management and the Auditor General (AG) on the interpretation and application of Regulation 32. The transaction in question was the appointment of a service provider for the supply and installation of electricity SMART meters in the

Elundini Municipality, in an attempt to stem the spiraling tide of electricity distribution losses. The AG was of the opinion that the manner in which the municipality had implemented this procurement mechanism was not in terms of the letter and the spirit of the law and hence it falls to be classified as irregular.

The accounting officer advised the committee that, although the procurement process followed was declared irregular by the Auditor General and subsequently disclosed as such in the AFS, the implementation of the project had been proceeded with and he sought to understand from the representatives of the Auditor General what their attitude would be towards the payments made to the service provider arising from the contract. The AG was of the view that, at face value, such payments are irregular and would need to be disclosed as such and that the contract should have been cancelled pursuant to its declaration as irregular. It was view of management, this amounts to double jeopardy and that cancelling a contract would warrant approaching a court of law, and there was no guarantee that the service provider would not successfully defend such cancellation, and this might unwitting result in the incurrence of fruitless and wasteful expenditure as a result of the resultant legal fees.

Having considered the presentation made by management and appreciated the circumstances surrounding this transaction, the committee **RESOLVED** to **RECOMMEND** that Council: -

- i. **WRITES OFF** the irregular expenditure resulting from the procurement of the service provider
- ii. **ENDORSES** the non-cancellation of the contract and **APPRECIATES** the bona fides of its continued implementation
- iii. **DIRECTS** management to approach the provincial and/or national treasury with a view to solicit the condonation of the contract and the resultant expenditure

- **Local Content – R166 542**

This emanates from the deficiency in certain bid specifications for the procurement of prescribed products, not carrying the requirements for local content. This was reported

as an oversight by management who failed to appreciate the existence of an instruction manual from the National Treasury. Management committed that, training programmes have since been arranged for employees involved in supply chain and that the relevant bid specifications henceforth carry the local content requirements. The committee considered the circumstances and **RESOLVED** to **RECOMMEND** that the municipal council **WRITES OFF** the irregular expenditure.

- **Procurement of a vehicle from Mark Wilson – R354 900**

In this instance, the municipality's Bid Evaluation Committee (BEC) had declared that the service provider had failed to meet the functionality criteria due to the non-submission of a document essential for the procurement. The Bid Adjudication Committee (BAC) was of the view that the service provider had recently been awarded a bid on the strength, inter alia, of the document and that the BEC ought to have requested this document from the service provider rather than declaring the service provider non responsive. The BAC had went on to award the bid to the service provider against the recommendation of the BEC. The Auditor General concurred with the BEC and declared the award as irregular. The committee appreciated that the matter of divergence of opinions in this case resulted in the irregular expenditure and that there does not appear to have been any ill intentions, hence **RESOLVED** to **RECOMMEND** that the council **WRITES OFF** the irregular expenditure.

- **Procurement of a vehicle from William Hunt – R429 789**

In this instance, the AG was of the view that a bid specification which had a requirement that a service provider must have supplied to a municipality previously, was restrictive, thus resulting in an irregular award. The committee appreciated that there is no evidence of mala fides on the part of management in the transaction and **RESOLVED** to **RECOMMEND** that the municipal council **WRITES OFF** the irregular expenditure.

- **Deloitte – R115 230**

Management had in 2016 sought to procure a service provider to provide training on mSCOA. Quotations were sourced from Messrs. Deloitte and CIGFARO, and only the

former responded, resulting in the award. The prescribed deviation form was completed and signed off as part of the procurement documentation. The AG noted that a circular from the National Treasury issued in January 2017 had mandated that accreditation on mSCOA training had been given to mSCOA and that the procurement of Deloitte for this exercise was irregular. The committee appreciated the timing difference between the initiation of the procurement process and the circular from Treasury, and that CIGFARO had been given an opportunity to bid but had failed to do so. The committee accordingly **RESOLVED** to **RECOMMEND** that council **WRITES OFF** the irregular expenditure.

- **Liskho (Pty) Ltd – R129 739**

The bid for the supply of mayoral cup kit was awarded to Kairos Clothing Cooperative Ltd, who subsequently bailed out, per letter dated 27 June 2016, citing financial difficulties. The committee has not been able to appreciate the reasons why a deviation had to be effected in October 2016 for the appointment of Liskho (Pty) Ltd, three months after the original service provider had opted out. The committee is still seized with this matter and is evaluating submissions made by the SPU manager to determine if anyone ought to be held accountable for this irregular expenditure.

- **Hekima - R83 386**

Hekima was appointed some years ago (2012) for the preparation of a technical report for a sewer solution for the Ethembeni Housing Project. Due to the effluxion of time, there was a need for a variation order to update the technical report, an exercise that could only be undertaken by the same provider. The variation amounted to 79% of the original award, which necessitated that a council resolution be obtained. Indeed, the council obtained was obtained, as all variations of this nature in excess of 20% must be sanctioned by council. The AG was of the view that the variation work ought to have been tendered out. The committee has evaluated this matter and having noted the relevant treasury instruction, is of the view that there ought not to have been a disagreement. Committee therefore **RESOLVES** to **RECOMMEND** that council **WRITES OFF** the irregular expenditure.

- **Inkunzi Construction- R135 000**

This pertains to SABS certificates which were not in the name of the supplier but in the name of the manufacturer. The AG was of the view that the bidder should have been disqualified. The SABS certification can only be given to a manufacturer of a product and therefore this requirement would not support emerging suppliers. The committee **RECOMMENDS** that Council **WRITES OFF** the irregular expenditure

- **Kumkani Electrical – R1 122 705**

The AG was of the view that a procurement of this service provider through deviation was a result of poor planning. Management presented the historical processes pertaining to the offices now occupied by the Infrastructure Department and based on their explanation, Committee **RECOMMENDS** that Council **WRITES OFF** the irregular expenditure.

2. ANALYSIS OF THE AFS, AUDIT REPORT AND AUDIT ACTION PLAN

The committee invited the chairman of the municipality's Audit Committee, Mr Thys de Beer, CA (SA), so that he provide an independent, technical assistance to the committee. In prefacing his presentation, he intimated that the annual financial statements ought to be viewed against the backdrop of the municipality's core mandate, which is the delivery of services to communities. The analysis should therefore entail a critical and analytical review of important account balances and certain classes of transactions.

He made the following salient reflections from the audited annual financial statements: -

- Receivables from exchange transactions have decreased from R3,5 million (2016) to R2,7 million (2017). This could be attributable to two factors – firstly, that customers have paid their accounts or (2) concerns that people will not pay their accounts and the outstanding debtors have been impaired. The actual causative factor would be discernible from the cash flow statement.

- Cash and cash equivalents, which is basically the reserves of the municipality have declined by R10 million from the previous financial year. The Auditor General has raised this as a concern which may compromise the financial viability of the municipality.
- The decrease in employee benefit obligations from R10,4 million (2016) to R6,9million (2017). This is a decline of 33,6% from the previous financial year and could be reflective of (1) an exodus of employees from the municipality resulting in the payout of exit benefits, or (2) a significant decrease in the accumulated leave provision and other related provisions. Management indicated that the leave provision, alone, declined by almost 15%, and this could be attributable, inter alia, to the change in the method of calculating the leave provision for those employees who were converted from fixed term contracts to permanent
- Payables from exchange transactions have increased from R23,6 million (2016) to R27,7million (2017). This increase is problematic when viewed against the backdrop of a decline in cash and cash equivalents, as it indicates that the cash resources have not necessarily been used to settle creditors. Consideration must also be had to the fact that these creditors constitute almost two thirds of the available cash resources at 30 June 2017, and in view of the MFMA stipulations, the entire amount would have to be settled by 31 July 2017 and would therefore hollow out the available reserves. Solace is to be found in that the first tranche of the equitable share was received in July 2017.
- Service charges as per the income statement have increased from R21 million (2016) to R24 million (2017). This could be due to (1) tariffs and (2) volume. To justify the factor of tariffs, there would have to be a demonstration that the tariffs were increased on average by 14%, which is not possible, hence this factor has to be discounted. This leaves the option of the volume of electricity sales, whose positive effect would be as an indicator of economic growth. It is noted, however, that the electricity distribution losses have also increased, which might indicate that the increase in electricity consumption could be due to pilferage. This is an area that management has to look at.

- Revenue from non exchange transactions increased from R14million (2016) to R17million (2017). This is a positive indicator, which may further improve with the implementation of a new valuation roll.
- The increase in government grants and subsidies from R190,7 million (2016) to R193,6 (2017) amounts to 1,5% and is significantly below the inflation rate. It is evident that government is slowing down on dispensing grants and the message is clear – there ought to be new revenue streams identified to replace lost revenue.
- The increase in the debt impairment from R6 million (2016) to R9 million (2017) is a clear indicator that the reduction in the receivables from exchange transactions, reported above, is due to non-payment by debtors rather than that collection of debtors.
- Overall, expenditure has increased from R205 million (2016) to R224million (2017), and this is clearly resonates with the decline of R10 million in cash reserves. Areas which warrant closer attention are general expenses, which increased from R36,7 million(2016) to R51,1 million (2017) .
- The implementation of the regulations on the municipal standard chart of accounts (mSCOA) has resulted in the incurrence of once off expenditure of R4 million. Government did not provide a specific purpose grant for the implementation of mSCOA.
- Increases of more than 100% on security costs have been noted, and management explanations have been that there was an increase in the number of service points, and a requirement that night guards carry firearms, relative to the previous financial year.
- The cash flow statement is, analogically, the blood flow in the body of a human being. Without blood, a person dies. If cash flows are persistently negative, the organization is steadily heading towards its demise.
- Total receipts increased by 0,3% from R231,7million (2016) to R232,5 million (2017), but total payments increased from R172,7 million (2016) to R186,5 million (2017), an increase of 8%. This is a clear case that the municipality is not

generating as much revenue as it spends, which spells doom for its long term financial viability.

In as far as the audit report is concerned, the municipality has retained its unqualified opinion for a seventh consecutive year, but there has been an increase in the number of compliance findings, which is basically related, predominantly, to the implementation of the supply chain management policy. Management has developed an action plan which was presented to the Audit Committee and is found to be adequate to address the identified internal control deficiencies noted. Management has made the following commitments: -

- Relevant officials will be trained on the local content requirements to avert similar findings occurring in the future
- There will be tightening of procurement planning, to defeat the appetite for the use of Regulation 32 of the SCM Regulations
- There will be an instruction manual issued to all employees on the interpretation and application of the deviation provisions in the SCM Regulations, to combat abuse.
- Systems will be introduced for contract management and monitoring

3. PROJECT VISITS BY THE COMMITTEE

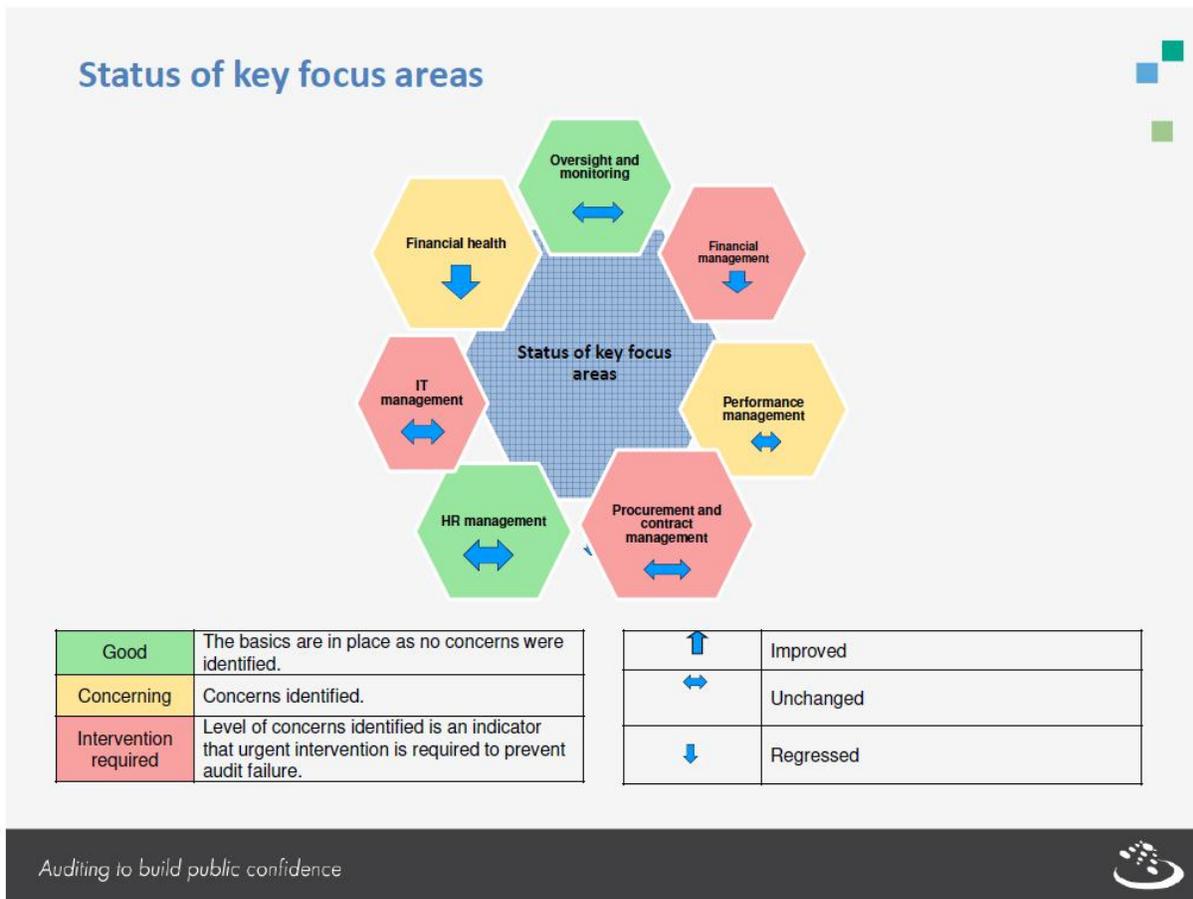
As part of the development of the oversight report, the committee embarked on project visits to the Ngcele (Hopedale), The TV Park and Ugie Sports fields. Previously, the management of the Infrastructure Planning and Development department were invited to talk to the committee on a number of project and this visit to projects was against the backdrop of management representations. It is the view of the committee that: -

- a) There has been a systematic failure of project and contract management in the municipality, which has resulted in a number of projects not being delivered according to time and quality specifications
- b) The findings by the AG that management failed to implement proper contract monitoring as required by section 116 of the MFMA resonates with the physical inspection of the sports fields by the committee

c) The Ngcele (Hopedale) sports field has deteriorated tremendously, with evidence of vandalism, and it would be a disservice to that community if nothing is done. Accordingly, the Committee **RECOMMENDS** that Her Worship the Mayor must, subject to a comprehensive report on the project, facilitate that funds be allocated towards its rehabilitation and completion

4. **STATE OF RECORDS REVIEW**

As part of its value added service, the Auditor General has conducted a review of the state of the records (SORR) of the Elundini Local Municipality for the second quarter of 2017/2018, and will further conduct another review in respect of the third quarter.



As can be observed from the above summary, out of the seven areas of focus of the review, only two were found to be good. The Senior Manager from the Office of the Auditor General was invited to present the report at one of the meetings of the committee. Following her presentation, the accounting officer and chief financial officer

were requested to provide management comments on the report, focusing predominantly on the areas requiring intervention.

- **Financial Management**

This finding is as a result of the understanding by the Auditor General that no billing of customers happened for the first four months of the 2017/2018 financial year. The CFO advised the committee that system (mSCOA) related challenges were experienced after the accounts of July 2017 had been billed. This challenge was resolved in November 2017 when retrospective billing was done. Furthermore, the billing is now up to date.

Secondly. The AG mistakenly understood that the payroll did not work for six months. The CFO acknowledged that there interface problems between payroll system and the general ledger, however, manual interventions were done and the payroll has been updated in the general ledger.

- **Procurement and contract management**

The AG was of the view that the nonattendance of the meetings of the Bid Adjudication Committee by four senior managers was a violation of Regulation 29(2) of the SCM Regulations. This had the potential that all awards made by the BAC whilst it was improperly constituted could amount to irregular expenditure.

The accounting officer advised the committee that the regulation speaks to the composition of the BAC and not necessarily to the attendance of meetings. In order to address the interpretation conundrum, the accounting officer had addressed a letter to the Provincial Treasury, seeking their interpretive understanding of the Regulation. Furthermore, in the event that the Regulation is deemed to deal with attendance of meetings, the following scenario was playing itself out: -

- 87,5% of all meetings of the BAC did not have all the senior managers in attendance, due to the vacancies that occurred from 1 October 2017, as well as due to leave of absence that would be tendered in the ordinary course of operations. Potentially, 87,5% of bids awarded fall to be condemned as irregular.

- There was a possibility that, in the event of the non-availability of any one of the senior managers appointed, the BAC would not sit and service delivery would be the victim.

The accounting officer has since advised that Provincial Treasury has concurred with the management's interpretation of Regulation 29(2).

- **IT Management**

This is predominantly due to malfunctioning of some modules in the mSCOA system. The chief financial officer advised that a majority of modules have since been functional and that all attempts are made to ensure that the financial statements for 2017/2018 would be drawn from an accurate and complete general ledger.

The management has advised the committee that the matters raised by the Auditor General in the SORR are receiving attention for the purpose of remediation.

Having considered the annual report of the Elundini Local Municipality for the year ended 30 June 2017, and having considered all responses that have been presented as against the questions raised, advices received, and specific recommendations made, the MPAC makes the following overall recommendations:-

3. RECOMMENDATIONS

The Municipal Public Accounts Committee therefore **RECOMMENDS** that Council **RESOLVES** as follows:-

- a) That Council, having fully considered the Annual Report for the financial year ended on 30 June 2017, **APPROVES** the annual report; and
- b) Council **APPROVES** the Annual report for the year ended 30 June 2017 without reservations.

4. CONCLUSION

On behalf of the MPAC, I take this opportunity to congratulate the leadership of the municipality, and the council at large for the support given to the Committee to enable it to discharge its responsibilities.

I am particularly grateful to my colleagues in MPAC as well as the Mr de Beer, chairperson of the Audit Committee for their resilience as they continue to assist the municipal council to provide accountable governance to the community of Elundini.

Thank you.

Councilor M Marubelela

Chairman: Municipal Public Accounts Committee

