

ANNUAL REPORT BY THE CHAIRMAN OF THE AUDIT & PERFORMANCE AUDIT COMMITTEES FOR THE FINANCIAL YEAR ENDING 30 JUNE 2011

Mr Mayor, It is my duty and privileged to present this report to the council of Theewaterskloof Municipality. In doing so, I want to at the outset convey the Committees congratulations to the Municipality, the Municipal Manager and his team of dedicated Officials on receiving an unqualified report from the Auditor General in respect of the 2009/2010 financial year. The target remains the same however – a ‘clean’ audit report is on the horizon. Continued hard work, commitment and leadership are going to make it real.

1. THE AUDIT & PERFORMANCE AUDIT COMMITTEES

These committees are statutory committees created in terms of Section 166 of the Municipal Finance Management Act, Act 56 of 2003. Their duties and responsibilities are delegated to it by Council. These duties are clearly articulated in the respective Audit Charters which have already been approved by Council in compliance with the MFMA. An Audit Committee is primarily established to serve as an independent governance structure whose function is to provide an oversight role on the systems of internal control, risk management and governance. The Audit Committee therefore assists the Accounting Officer or Municipal Manager in the effective execution of his responsibilities with the ultimate aim being the achievement of the Municipality’s objectives.

During the past financial year 2010/2011, the Audit Committee consisted of five (5) independent members and the Performance Audit Committee of three (3) suitably qualified members. Both Committees have each held a minimum of four (4) meetings during the year under review. These meetings were held on -

AUDIT COMMITTEE	PERFORMANCE AUDIT COMMITTEE
30 July 2010	30 August 2010
30 September 2010	26 November 2010
26 November 2010	11 February 2011
21 January 2011	27 May 2011
11 February 2011	
27 May 2011	

They were on the average well attended by committee members, the Municipal Manager, Executive Directors and other Officials, when required. Participation and preparation by some Committee Members was however not over enthusiastic and at times

disappointing. Improvement in this regard is anticipated when the new committees are constituted.

The Audit Committee conducted self-assessments during August 2010 in order to measure its performance. Input from management, internal audit and external audit was part of the assessment process. The results of the performance was reviewed and discussed. *[Please refer to Agenda Item AC 31/2010 – Annexure A for more detail pertaining the self-evaluation.]*

2. THE INTERNAL AUDIT UNIT

The Internal Audit unit remains fully staffed as reported in the previous review. Guided by the risk based approach, this unit has been able to address strategic issues in its quest to deliver an effective and efficient internal audit service.

The Office of the Account-General within the National Treasury, conducted an Internal Audit Review on the Internal Audit unit of TWK to ensure compliance with the IIA Standards. The Audit Committee takes cognizance of the report and comments of the Municipal Manager that the Deputy Director; Internal Audit has in a fairly short time placed the unit unofficially in amongst the top 30% of Municipalities in the Western Cape. *[Please refer to Agenda Item AC 27/2011 – Annexure B for more detail pertaining National Treasury’s Review.]*

Furthermore, in terms of the IIA (Institute of Internal Auditors) standards, the internal audit unit must undergo an internal quality assessment. In February 2011 the Audit Committee and the Management team evaluated the Internal Audit unit. *[Please refer to Agenda Item AC 26/2011 – Annexure C for more detail pertaining Internal Audit Evaluation.]*

The internal audit unit conducted twenty-three (23) investigations during the year under review. Fifty-two (52) findings were made of which Twenty-seven (27) were regarded as significant (serious). The remaining twenty-five (25) findings were regarded as house-keeping i.e. minor transgressions which could easily be rectified.

A special word of thanks is extended to the Manager and Staff of Internal Audit for their support and submission of accurate and meaningful reports. There has indeed been a continued improvement in this regard, which augers well for the standard of Auditing for

the forthcoming period. It is the aim of the Audit Committee to have a level of auditing that is fully competent to meet the highest professional standards.

Up until now the Auditor-General has not relied on the work of the Internal Audit Unit when performing their external audit, except for using the findings of the internal audit unit for risk identification purposes.

The Audit Committee would like to see a situation whereby Internal Audit Unit is operating at a level of effectiveness and status, where greater reliance can be placed on their work by the Auditor-General. The Audit Committee has therefore tasked the Internal Audit Unit with the responsibility of liaising with the Auditor-General to identify audit areas within its 2011/2012 audit plan, where work can be performed by the Internal Audit Unit of Theewaterskloof in a manner that the Auditor-General is able to place a greater level of reliance on its findings in order to reduce the extent of the External Audit process and all that follows. In general the Audit Committee is satisfied with the performance of the Internal Audit unit.

3. RISK MANAGEMENT

Proper implementation of appropriate risk management ensures that regular risk assessments, IT risks and fraud prevention are conducted. It also encompasses the management and control of supply chain procedures and that a risk strategy exists to address constant monitoring.

Risk management is an essential part of effective corporate governance and whilst it is essentially a management responsibility the Audit Committee in the discharge of its mandate has to oversee, advise and review the process and adopted management framework. Part and parcel of this process is also the monitoring and evaluation of all fraud prevention plans to ensure that they remain appropriate and effective. It is therefore of importance that Audit Committee Members have a good understanding of the Council's control environment. The Audit Committee is able to confirm that it has been adequately informed in this regard via the comprehensive reporting it has received during the year under review.

The first risk identification and evaluation was done during June & July 2010 by means of a one on one session with all senior management staff per department. The Risk Management Committee was established during October 2010 and the bi-annual revision

of the identified risks was done during January & February 2011 and the revised Risk Management Policy and pertaining documentation was adopted by Council on 9 February 2011.

The Risk Management Implementation Strategy along with the Risk Management Policy serves as induction documentation for new employees, however an official induction presentation is being developed for that purpose. Constant interaction with Departments in terms of risk contributes towards risk awareness.

The official risk register of TWK was adopted by the Risk Management Committee on 6 May 2011, where after the process started to establish required action plans if any as well as identifying the key risk indicators relating to these risks. These risks were reported to the Audit Committee and internal Audit also conducts regular reviews on the effectiveness of Risk Management. *[Please refer to Agenda Item AC 28/2011 – Annexure D for more detail pertaining Risk Management.]*

The Audit Committee has however noted the comments of Council's Consultants in this regard. They have reported as follows, "the institutional capacity of the Finance Department has been severely affected by the Minimum Competency Regulations and the large number of finance employees that are attending such training. Due to the poor response to our advertisements there was also an unexpected long delay with the filling of the Accountant position in the Revenue Section. The full impact of the newly introduced Risk Management function was also felt during this period. The Risk Management function is performed by the same official who is also responsible for the Asset Management and Insurance functions and it has now become obvious that an additional post will have to be established to assist him in the performance of the Asset Management, Risk Management and Insurance functions."

4. FINANCIAL MANAGEMENT

Financial statements of TWK are compiled by consultants (MUBESKO AFRICA).

The Municipality failed to complete its annual financial statements for the year ended 30 June 2011 in time for it to be reviewed by the Audit Committee prior to it being presented for auditing to the Auditor- General. After the initial submission of the financial statements, the statements had to be withdrawn due to errors that were discovered, resulting in a late submission of the annual financial statements to the

Auditor-General. The late submission has been ascribed to difficulties experienced by the finance department in dealing with the unbundling of fixed assets.

Subsequent to the re-submission of the financial statements to the Auditor-General, further errors were discovered after review of the financial statements by the Audit Committee.

As Audit Committee we are concerned that the errors in the financial statements were not detected due to a lack of adequate review procedures within the finance department relating to the preparation of the annual financial statements. It is the responsibility of the Accounting Officer to ensure that adequate internal control measures are implemented to prevent the future re-occurrence of the errors and non-compliance which arose during the 2011 financial statement preparation process.

The Municipality resolved to early adopt the GRAP standards which have been issued by the Accounting Standards Board, but were not yet effective during the 2010/2011 financial year. The adoption of GRAP standards in the preparation of annual financial statements enhances the reliability and usefulness of financial information to the users thereof. The following GRAP standards which have been early adopted by the Municipality had the greatest impact in the preparation of financial statements for the year ending 30 June 2011:

Standard	Description
GRAP 16 (Revised)	Investment Property
GRAP 17 (Revised)	Property, Plant & Equipment
GRAP 25	Employee Benefits
GRAP 104	Financial Instruments

Total revenue for the year amounted to R288, 4 million. In line with the prior year, revenue from exchange transactions and property taxes accounted 44% (R129, 5 million) and 14% (R41, 1 million) of total revenue respectively. The Municipality remains highly dependent on Government grants and subsidies which account for 35% (R101,2 million) of total revenue in order to ensure its sustainability.

Although the Municipality has achieved a net surplus of R14, 2 million for the financial year R11, 4 million of revenue related to fair value adjustments on investment property (increases in the fair market value of investment property). If the effect of fair value adjustments is removed the operating surplus for the year amounts to only R2,8 million It should be of concern to Council that during the year R14,9 million was written off as bad debts and at year-end the total Allowance for Doubtful Debts amounted to R90 million (prior year, R84,5 million). This is indicative of a deterioration in the level of recoverability for outstanding debts due to the Municipality.

At year-end, the Municipality had investment property with a fair market value of R234 million consisting of commonage land (R209 million) and buildings (R25 million). Given the fact that the Municipality is faced with the challenge of having limited cash resources to facilitate effective service delivery to residents in the Municipal area, the disposal of non-strategic investment property should be considered by Council.

At year-end, the Municipality had property, plant and equipment with a carrying value of R380 million, consisting predominantly of infrastructure assets (Roads and Storm Water drainage, Electricity, sewerage and water networks) of R239, 8 million (63%) and land and buildings of R105, 7 million (27, 6%).

Other significant assets of the Municipality relates to expected recoverable debtors of R22, 3 million (after allowing for doubtful debts of R90 million), and cash resources of R23 million. The level of cash resources of the Municipality is considered to be very low in relation the level of current liabilities (cash ratio of 0, 45:1).

The most significant liabilities of the municipality at year-end relates to annuity loans (R85.4 million), stock loans (R19 million), Employee benefit obligations (R39.6 million), Provisions for the rehabilitation of landfill sites (R22.6 million), monies due to suppliers and services providers (R19 million) and a tax liability recognized in respect of possible VAT due SARS (R10.5 million).

The ratio of current assets to current liabilities at year-end was 1:1 and although it is a significant improvement from the prior year ratio of 0.7:1, this ratio is still considered to be too low and it is recommended that actions be implemented to improve the ratio to be closer to 2:1

The overall financial performance of the Municipality for the financial year ended 30 June 2011 is considered to be satisfactory and commendable as the Municipality was able to generate a surplus for the year. In particular, management should be commended for achieving a reduction in water distribution losses from 15, 53% in the prior year to 8, 9% in the current year.

The Municipality is also considered to be financially solvent and able to continue operating on a going concern basis in the foreseeable future, although actions should be taken by Council to increase the level of liquidity within the Municipality (increase cash resources and decrease non-current assets such as investment property.)

5. GOVERNANCE

King III applies to all entities regardless whether in the public, private or non-profit sectors. Municipalities require a deeper understanding of governance in order to decide how governance principles and practices should be adopted and implemented as it will differ from sector to sector.

The Internal Audit unit conducted a compliance review on TWK's effort to comply with the King III, the Code of Governance Principles.

The Audit Committee supported the King III Compliance Report and the Council adopted the King III principles on 28 October 2010 as best practice. *[Please refer to Agenda Item AC 29/2010 – Annexure E & C 75/2010 – Annexure F for more detail pertaining Governance Principles.]*

6. SERVICE DELIVERY

The Audit Committee is pleased to inform its satisfaction with the Service Delivery of TWK, despite many of the challenges the Municipality has faced.

The Performance Audit Committee requested a field trip to visit some of the capital projects of TWK. All the projects created a positive impression on the Performance Audit Committee members. The Committee wants to thank the personnel for their dedication and hard work with a special reference to the Rooidakke Housing Project which received an award for the Project of the Year from the SA Housing Foundation (SAHF). *[Please refer to Annexure G for more detail pertaining the Field Trip.]*

7. PERFORMANCE MANAGEMENT

The recently adopted system of Performance Management as provided by "IGNITE" has proven to be an effective and reasonably accurate instrument of measuring the output and performance of the activities of TWK, its Executive and Management Staff.

Areas of concern do however continue to exist and whilst some may be ascribed to the implementation and interpretive stages of the system, shortcomings are causing concern. The Performance Audit Committee, in a report on the 4th Quarter Performance Assessment, resolved to record its discomfort with the inadequacy of the feedback, it had received from senior officials and that more improved decisions were not forthcoming.

The number of (KPA's) Key Performance Areas was recorded as being excessive. There were also instances where status reports on technical service delivery were not submitted timeously or not at all.

Expenditure on Capital Projects was also not up to anticipated levels.

The Audit Committees have consequently requested that reporting on S.D.B.I.P. be closely monitored during the new financial year and that it would be placing these reports under optimum scrutiny.

The Municipal Manager's on-going commitment to Strategic Management review has been noted with appreciation and that he will continue to identify and rationalise over-ambitious KPI's.

The Audit Committee has taken cognisance of the side effects of the recent Municipal Elections which has influenced certain programs during the latter end of the financial year.

G N LAWRENCE
CHAIRMAN OF AUDIT COMMITTEE &
PERFORMANCE AUDIT COMMITTEE

18 October 2011

