

A clean audit IN 2014?

On 16 July 2009 the Department of Cooperative Governance and Traditional Affairs (COGTA) launched an ambitious project dubbed 'Operation Clean Audit 2014'. This operation is part of a bigger project called 'Operation Clean Up', which has three other components: Clean Cities and Towns, Debt Collection, and Public Mobilisation and Revenue Enhancement.



The overall aim of Operation Clean Up, according to the Minister of Cooperative Governance and Traditional Affairs, Sicelo Shiceka, is to 'clean up governance and enhance service delivery at both local and provincial levels of government'. Operation Clean Audit 2014 in particular seeks to ensure that none of the 283 municipalities of the Republic has either a disclaimer or an adverse audit opinion in their audit report by the end of 2011. In the long term, the operation aspires to ensure that all municipalities have a clean audit report in 2014, which not only relates to disclaimers or adverse audit reports, but anticipates that there will be no qualified audit reports across the board. This is an ambitious goal that has never been achieved in South Africa before.

The Auditor-General's reports are the primary indicators and means of verification as to whether the operation has achieved its goal. In view of this, the Auditor-General has published a consolidated general report on local government audit outcomes – the first report since the launch of Operation Clean Audit 2014 – covering the 2009/10 fiscal year.

The report could not have been more timely, since there are just a few months until the end of 2011. By highlighting the main findings of the report, we can gain an indication of whether Operation Clean Audit 2014 is edging towards its goals or lagging behind schedule.

Overall trends

The overall progress towards a clean audit is not encouraging. While it is true that 57 (24%) municipalities registered an

improvement on their 2008/09 audit outcome, as did 12 (25%) municipal entities, in the main improvements were insignificant, and progress towards a clean audit seems sluggish. The number of municipalities that received clean audits increased only marginally, from four to seven. On the negative side, 15 (6%) municipalities and 2 (4%) municipal entities regressed. A further 95 municipalities once again received financially unqualified reports with findings, while 70 received either disclaimers or adverse opinions.

Key findings

Submission of financial statements and useful comparisons

A major problem remaining is the failure of municipalities to submit their financial statements for auditing in time. To measure any improvement in the financial management of municipalities, the figures for the 2009/10 financial year had to be compared with those for 2008/09, and this is where the main challenge lies. In terms of the Municipal Finance Management Act (MFMA), municipalities must submit their financial statements by 31 August, and their consolidated statements, including those of municipal entities, by 30 September. Out of the 283 municipalities, 227 managed to do so for the 2009/10 financial year, a 2% improvement on the previous year. A further 24 municipalities submitted late, but before 31 January 2011, and 22 were still pending by then. The majority of the unaudited municipalities (53%) were in the North West and the Northern Cape.

Moreover, the Auditor-General found that of the reports submitted, only 18 were in line with regulatory requirements and could be considered reliable. The Auditor-General's report indicated that there were extensive errors and omissions in the financial statements of many municipalities as submitted for audit. The report also indicated that there was a 'high incidence of non-compliance with the MSA [Municipal Systems Act] and MFMA'. Most of the municipalities have poor documentation systems. As a result, cases of missing and inadequate documentation are widespread.

Clean audits

Progress towards a clean audit by 2014 is slow. As mentioned above, only seven municipalities received financially unqualified reports with no findings on predetermined objectives and/or compliance with legislation (three better than the year before). Three of the seven municipalities that obtained clean audit reports were from Mpumalanga: namely, Ehlanzeni District Municipality and Steve Tshwete and Victor Khanye Local Municipalities. The City of Cape Town Metropolitan Municipality was the only municipality in the Western Cape with an unqualified audit. The district municipalities of Metsweding in Gauteng and Frances Baard in the Northern Cape and the local municipality of Fetakgomo in Limpopo also received clean audits. Ten municipal entities obtained clean audits, seven of them in Gauteng, one in the Eastern Cape and two in the Western Cape.

There were 122 municipalities that received an unqualified report, but with findings (seven more than the year before). None of the municipalities and municipal entities in KwaZulu-Natal, the Free State and the North West were found to have unqualified audit reports. There are still 51 audits outstanding. Based on previous patterns and trends, the unaudited municipalities and municipal entities are likely to receive qualified opinions or worse.

The results for audits completed by June 2011 are shown in table 1.

Relative improvements

Some overall improvements were discernible. The number of municipalities in the 'most negative' territory, namely disclaimer and adverse opinion, fell from 121 in 2008/09 to 65 in 2009/10, a 46% reduction. Also, the number of municipalities that failed to obtain unqualified reports fell from 163 to 110, which constitutes nearly a quarter of the



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audited municipalities. The most notable improvements came from Gauteng and KwaZulu-Natal, although none of the municipalities or municipal entities in KwaZulu-Natal received unqualified audit reports. According to the Auditor-General's report, KwaZulu-Natal, Gauteng and the Western Cape were the leaders in respect of progress made towards achieving financially unqualified audit reports, as 80% of the auditees in these provinces were financially unqualified.

Table 1: Results of audits completed by June 2011

Audit outcomes of municipalities	2009/10	2008/09
Financially unqualified with no findings	7	4
Financially unqualified with findings	122	113
Qualified opinion	57	50
Adverse opinion	11*	10
Disclaimer of opinion	57*	103
Total number of audits reported on	254	280
Number of audit reports not issued by 31 January 2011	46	3
Total number of audits	283	283
Predetermined objectives	219	256
Compliance with laws and regulations	224	231

*Eight audits were categorised as either a disclaimer or an adverse opinion (and were then randomly allocated to either category, four each).

Yet the improvements do not warrant celebration. The Auditor-General expressed the concern that 110 out of the 163 municipalities that received qualified reports in 2008/09 did not address the qualification findings of 2008/09. Moreover, six of them actually regressed. Also, 69 of the 110 municipalities were again disclaimed, or received an adverse or qualified opinion. Even worse, in 38 of them, adverse/disclaimer audit reports have been issued consistently for the past five years. And then, 31 of the 69 attracted further qualifications, while 21 failed to address any of their qualifications from the 2008/09 audit report. About 97% of these municipalities are in the Eastern Cape (17), the Free State (7), Limpopo (7) and the Northern Cape (9).

Supply chain management

The Auditor-General also performed an audit for compliance with the applicable legislation. Of particular importance was compliance with supply chain management regulations. Although such an audit was performed on only 40% of municipalities that submitted their financial reports, the findings showed large-scale disregard for the carefully constructed system of procurement to minimise corruption. The report indicated that 94% of the irregular expenditure that the municipalities and municipal entities incurred, amounting to R3.9 billion, was due to the violation of supply-chain management policy and legislation. The main problems included the procurement of services and goods from persons in the service of the state or their family members (63, or 56%, of auditees), and uncompetitive or unfair procurement processes (159, or 56%, of auditees). Contracts to the value of R76 million were awarded to persons in the employ of the municipality, including 19 councillors, a mayor and a municipal manager. A further R102 million was linked to contracts with close family members of persons in the service of the municipalities.

What makes for improved audit reports?

Given the fact that there were municipalities that did improve their position, the Auditor-General addressed the important question of determining



what factors led to such improvement, as they are important for replication purposes. First, it would appear that municipal leadership plays an important role in pursuing audit issues of earlier years. As the Auditor-General's report put it, 'strong ethical leadership and monitoring, well-established policies, processes and procedures for SCM [supply chain management] and fraud prevention and detection as well as active governance by internal audit and audit committees can solve the problem'. Second, the appointment of consultants helped address specific deficiencies. However, too much dependency on consultants is not to be encouraged. Third, improved management of record-keeping is obviously essential.

Implications

The question that remains is how to achieve a clean audit of all municipalities by 2014, in line with COGTA's campaign. Is the problem a lack of capacity or a lack of political leadership? The question of capacity is being addressed by both the National Treasury and COGTA. The National Treasury's competency level regulations, requiring municipal managers as accounting officers and personnel responsible for supply chain management to have appropriate qualifications, kick in at the end of December 2012. From 1 January 2013, no person who fails to meet the requirements set out in the regulations may perform the designated functions.



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The new Municipal Systems Amendment Act of 2011 has also established a framework laying down minimum competency and experience requirements for senior managers. This framework still needs to be developed and implemented. Appropriately qualified persons to manage municipalities' finances are essential, but, as the Auditor-General reported, it is also a question of leadership. If there is the will to do so, a clear audit can be achieved.

The implementation of a sound supply management system is a question of leadership. It does not require capacity to prevent a municipal official or councillor, or their family members, from contracting with a municipality. What is required is honest leadership.