

ASSESSING MUNICIPAL PERFORMANCE - THE RELEVANCE OF AUDIT REPORTS**Veliswa Notshikila***Regensys Business School, Johannesburg, South Africa.***Krishna K Govender***Regensys Business School, Johannesburg, South Africa.***Abstract**

Municipalities are the most important service delivery level of the South African government because performance at this level of government is closely scrutinised since it impacts the citizens directly. This paper reports on an exploratory study to determine the extent to which the external audit reports reflect a South African municipality's performance. A qualitative approach using semi-structured interviews was employed to gather information from senior management of the municipality. It became evident that challenges emanate from a lack of integrated systems, proper documentation to reflect the performance of municipalities, and communication with external auditors. The aforementioned seems to be the primary reason for differences in opinions between the internal and external audits. It is recommended that improvements be instituted around the systems, policies and procedures, training of management employees, relationship with auditors, performance management for all employees and sharing of excellence across municipalities.

Keywords: *External Audit; Municipal Financial Performance; Service Delivery.*

Abbreviations

IDP: Integrated Development Plan, MED: Monitoring and Evaluation Department, MFMA: Municipal Finance Management Act, MSA: Municipal Systems Act, PDO: Predetermined Objectives, NPM: New Public Management, POE: Portfolio of Evidence, SALGA: South African Local Government Association, SDBIP: Service delivery Budget Implementation Plan

Introduction

South Africa comprises a country with nine provinces and three spheres of government namely, national, provincial and local, with the municipalities being the lowest level of democratically elected government structure (Van der Waldt, 2007:2). The foundation of this layer of government is set out in Chapter Seven of the Constitution of South Africa, and various Acts of parliament have further defined the municipal structures since inception of the Constitution. There are 283 municipalities in South Africa, which belong to one of the three categories, namely, metropolitan, district and local. Metropolitan municipalities of which there are currently nine, represent large densely urbanised regions that encompass multiple cities. (Department of Government Communication and Information system, 2011:261).

Local government in South Africa has contributed to the achievement of a number of social and economic development advances, since the ushering in of the new democratic municipal dispensation in December 2000. Although municipalities have made significant contributions in that the majority of citizens have increased access to a wide range of basic services and more opportunities have been created for their participation in the economy, key elements of the local government system began to show signs of distress since 2009 (Department of Cooperative Governance and Traditional Affairs, 2009:3). In 2009, the National Treasury reported to the Technical Committee for Finance, that 56 local municipalities and eight district municipalities were on their financial distress list. The aforementioned implied that the local sphere of government faced critical challenges and problems pertaining to effective and sustainable provision of basic services; administrative capacity and institutional performance to drive service delivery and effectively implement government policies and programmes (Koma, 2010:116).

Recently, some local municipalities in South Africa have been plagued by significant service delivery challenges, poor financial management, corruption, and poor capacity due to among others, the lack of skills. This situation resulted in a number of municipalities experiencing financial distress and a loss of confidence and trust in local governments. In general, the challenges faced by municipalities in South Africa mainly arise due to service delivery

failures stemming from huge backlogs, inadequate revenue collection, corruption and fraud, poor financial management systems, and lack of high-skilled personnel (Monkam, 2011:12).

The current political administration has a clear electoral mandate to deliver on key priorities that must ensure that visible, tangible and positive changes are felt in all communities. These must focus on, inter alia the Millennium Development Goals (MDGs) and more recently, the National Development Plan. Determining organisational (municipal) performance is vital because resources can be wasted if the people have no way of determining how their actions impact on the organisation's goals, and whether they are on track to achieve these goals. Organisational performance can be measured by mapping the mission statement of the organisation against organisational reports available in the form of outputs depicted in graphs and tables, and from other reporting tools of the organization which allows organisational teams and other stakeholders to know which areas require attention.

Audit reports, both internal and external are important tools for reflecting on and managing a units' performance, which eventually contributes to judgements/statements being made about the organizations' performance. Audits are conducted in terms of prevailing audit standards and audit reports are not necessarily a proxy for good financial management, and there is a risk that audit reports may focus on accounting technical matters rather than underlying internal controls and other elements of good financial management, and therefore more consideration needs to be given to the nature of the matters that have informed audit opinions (PDG & Akhil, 2010:58). Furthermore, March and Sutton (1997: 698) caution that inferences about the factors contributing to performance cannot be made only from the data available internally in an organization, and that external audits which are an independent examination of information in order to express an opinion on whether it meets set standards, can also be important. External audits are a key function in an organisation as it provides an independent view of the affairs of the organisation, and this is particularly important to the external stakeholders who have an interest in the organisation.

The independence of external auditors enables stakeholders to value the reports they issue, because the auditors are independent of the organisation they are auditing. Furthermore, due to all the ethical and governance challenges facing organisations, the external audit function has become even more critical. In South Africa, the Office of the Auditor-General is tasked with the responsibility of conducting external audits of municipalities. Since auditors are known to give reports based on information available in an organization, concerns are sometimes raised about the value of audit reports in measuring performance. Moreover, the internal auditors are sometimes privy to information which external auditors do not have or require to arrive at certain conclusions and recommendations. This concern provided motivation for the research on which findings this paper has been developed. Broadly, the implications of the audit report on the performance of the Mogale City Local Municipality in the Gauteng Province of South Africa, is being reported.

Literature Review

A distinguishing feature of public performance is that it is guided and assessed by multiple, equally important standards of effectiveness, efficiency and equity (Van der Waldt, 2004:36). A common focus of public sector performance is its concern with the managers' use of public resources and mandates to ensure that policy programmes meet public objectives and expectations. Developed in the private sector and adopted by the public sector, performance management is primarily a tool for improving service delivery. It matters in municipalities because it allows the local sphere of government to go beyond a zero tolerance for maladministration, waste, inefficiencies and lack of productivity and create a municipality that is better equipped to deliver promises to the people (Fourie *et al.*, 2011:321).

During the last three decades, the concept of New Public Management (NPM) has driven the public sector reforms carried out in many countries. In the public sector there is now an increasing emphasis on planning, budgeting and service delivery and hence a lessening of the differences between the public and private sectors. This has meant the defining of accountability from political accountability to managerial accountability, which is underscored by the principles of the NPM. The reporting of well-documented performance information is now fundamental to public

sector accountability. Khalo (2007:186) states that since municipalities do not have endless financial resources and they have to provide many services required by local communities, councillors and municipal officials can contribute to the more effective, efficient, proper and sound financial management of the municipal money received from the public as they play the most important part in municipal financial management.

There are several regulatory principles that are instituted to ensure the proper functioning and performance of South African Municipalities, and these include the Constitution of the Republic of South Africa, Act 108 of 1996, the White Paper on Transforming Public Service Delivery (1997), the White Paper on Local Government (1998), the Local Government: Municipal Systems Act 32 of 2000, the Local Government: Municipal Finance Management Act 56 of 2003, the Performance Management Guide for Municipalities (2001).

The quarterly reports issued by the South African National Treasury indicate that there had been a deterioration in the financial position of municipalities in the year ended 30 June 2009 (PDG & Akhile, 2010: vii). Challenges around revenue collection in particular weakened the cash flow position of most municipalities. This had implications on municipalities from a capital expenditure (service delivery perspective because capital expenditure is usually reduced when municipalities encounter cash flow difficulties) and asset management perspective (repairs and maintenance costs are also reduced where cash flow difficulties are encountered) (PDG & Akhile, 2010: viii). Of the 238 audit reports that were included in the South African Local Government Association's (SALGA's) database in 2008, 39% were the unqualified, 22% qualified, 35% were disclaimed and 4% were adverse. The underlying causes are not always apparent in the audit reports and a more analytic approach is needed to better understand what has contributed to qualified audit opinions (PDG & Akhile, 2010:8). During the 2009/2010 financial year, of the 237 municipal audits conducted by the Auditor-General, only seven municipalities received clean audit reports. This seems to be an annual occurrence and yet the government has a target of all municipalities receiving clean audits by 2014 (Downing, 2011). Of concern though is that 67% of the municipalities failed to address all the 2008-09 qualification findings, and 75 municipalities (34%) and twenty five (51%) municipal entities have had repeat findings on predetermined objectives and/or compliance with laws and regulations, while again having obtained financially unqualified audit reports (Auditor-General South Africa, 2011:2).

The performance of municipalities is constantly under scrutiny by a wide variety of stakeholders such as citizens, interest and pressure groups, the National Treasury, the media and politicians. It could be argued that the performance or lack thereof of municipalities is more visible and open to public enquiry because of their closeness to the people they serve (Van der Waldt, 2007:110). If people believe that municipalities do not provide the level and standard of service they expect, the legitimacy of the political structures and executive departments of municipalities could be in jeopardy.

According to Van der Waldt (2004:381), performance auditing is a systematic process of objectively obtaining and evaluating evidence regarding the performance of an institution, programme, function or activity. According to the aforementioned researcher, the aim of performance auditing is to provide an independent appraisal of activities by evaluating aspects of the systems of internal control outside the traditional financial area.

Section 45 of the Municipal Systems Act (MSA) prescribes that the results of performance measurements must be audited both internally by the internal audit and externally by the Auditor-General. As such, in terms of Regulation 14(1) (c) the internal auditors must on a continuous basis audit the performance of the municipality and submit quarterly reports to the municipal manager and the Audit Committee. In addition Regulation 14(1)(b) required the internal audit process to include assessment of the functionality and legal compliance of the performance management system and the extent to which the chosen indicators are reliable in measuring performance (Fourie *et al.*, 2011:325).

In light of the above background, this study explored the relevance of audits in assessing the performance of Mogale City Municipality, which is located in Gauteng, South Africa.

Methodology

A qualitative research approach was used, since the study aimed at studying people and systems, by interacting with the participants. More specifically, the case study research method which is a systematic inquiry into an event or set of related events, and which aim to describe and explain the phenomenon of interest, was used. Semi-structured interviews were considered appropriate for the study because it was very difficult to set up an appointment with the respondents who are key informants. The inclusion of open-ended questions provided the opportunity for identifying new ways of seeing and understanding the topic at hand¹.

The population broadly was all employees of the Mogale City municipality. More specifically, the population was the senior management employees of the municipality since they set the objectives/strategy and drive its achievement. Cluster sampling was used as the first step to identify the sample population of municipal employees who would participate in the study. This was done by dividing the municipal employees into different heterogeneous clusters being general employees, supervisors or junior managers, middle managers, senior managers and executive managers. The researchers decided to focus on the senior and executive management because they influence the decision-making process, although all employees of a municipality are ultimately responsible for its performance. The senior managers are also the public officials who should be well versed with government policies, interpreting such policies correctly, implementing the policies, and monitoring and evaluating the implementation process. They are also supposed to have the required skills to design the internal control systems that will ensure clean audit reports and excellent performance of the municipality.

Findings

It became evident that the Mogale City Local Municipality has a performance framework which is used to measure conformity to implementation of its performance legislation, audits processes and auditing reliability and the integrity of performance information. In order to achieve the above, each department has its set target for every fiscal year, which are detailed in the SDBIP. The target for the municipality is set in conjunction with the community, which implies a participatory process since the targets are meant to address the services needed by the community.

The municipality's Integrated Development Plan (IDP) is a five-year plan but subjected to annual review, in other words targets are subject to change depending on the demands of the people during the yearly review. This exercise affords the municipality the opportunity to constantly evaluate its performance. The strategic plan is submitted to the Mayoral Committee and Executive Committee for consideration and approval. This process is guided by the IDP which sets out the five-year targets. Afterwards, the municipality will develop the annual strategy plan and the Service Delivery Budget Implementation Plan (SDBIP) will break these targets into departmental annual targets. The SDBIP is a tool that is used to measure the performance of each target. It became evident that the Mogale City municipality had achieved 70% of its targets for the past five years.

The Mogale City municipality has a Monitoring and Evaluation Department (MED), whose function is to monitor and evaluate the performance of each department in relation to its target set out in the SDBIP. Furthermore, the Internal Audit department audits the various Proof of Evidences (POE's) documents that clearly show the performance of each department. It is also mandatory that each department submit a report of its performance quarterly. This feedback mechanism avails the MED the opportunity to continuously assess the performance of the department with a view to determining conformity to the PDO's. This does not suggest that the performance has been perfect, even though the report has been so far encouraging because the Municipality has not at any time operated below 50% performance.

It became evident that the Mogale City municipality adheres to the performance reporting requirements. There is constant implementation of the policies emanating from the reports of the monitoring and evaluation units of each

department. To this end, there is constant review and revision of such policies where necessary with communication of all documentations such as policies and procedures, to all the relevant units. Furthermore, the audit system remains a measure to ascertain the correctness and reliability of the portfolio of evidence, and a tool to assess delivery of projects, monitor and evaluate the performance of the municipality. Auditing in the municipality takes place quarterly by the internal audit department to provide an independent review. The report of such a review is submitted to the Audit Committee of the municipality; the committee will study the report and advise the Council on what to do. This internal auditing process is like an in-house measure to affirm compliance, before the external auditors are invited to carry out their own assessment.

The annual external audit is meant to assess compliance with reporting requirements, usefulness and reliability of information. This includes assessment of the process and procedures in relation to IDP, monitoring and evaluation. It is a Municipal Finance Management Act (MFMA) compliance requirement in the Republic of South Africa and its activities are in accordance with the audit standards and legislative requirements.

It became evident that in the Mogale City Local Municipality, there are conflicts between the reports of the internal and external auditors. While internal audits may produce positive reports on the performance of the municipality, the external auditor's reports have been negative for the period under review. Nevertheless, in the area of the financial audit, the municipality has been receiving positive reports, which implies that they have been performing well.

The differences in opinion alluded to above, are important and could be attributed to that fact that external auditors conduct their audits without taking into account the peculiar environment of the municipality. For instance, the municipality does not have an integrated information management system and therefore might not be able to produce the reports needed by the external auditors. Most of the time, the findings of the auditors are at variance with the reality of the service delivery since there are insufficient reports at their disposal. There is little problem with service delivery, but there is a dearth of information presented to the auditors for them to form and informed opinion, thus they tend to defect to reporting on the performance as being poor.

It was also ascertained that there is a lack of synergy of operation between the external auditors and the municipality officials. Since auditing is an evaluation mechanism, external auditors need to maintain effective communication with the municipality on their schedule of activities, so as to get all the necessary documentations ready. To this end, external auditors should behave more as compatriots rather than the 'police'. The audit is appropriate, however many departments internally need to improve the information submitted for audit so that it is appropriate for audit.

In spite of the difference between the audit reports and the actual performance, the adverse external auditor's reports indicate that there is a need to ensure that the city receives unqualified financial audit reports, and the factors responsible for the negative performance are managed closely. It became evident that there are no known consequences of negative audit report for municipality employees. Though this might be an internal mechanism to appraise performance, such reports seem not to be too relevant to the performance of the municipality. The findings also show that a lack of synergy between the internal and external auditors is the major factor responsible for the seemingly negative external auditors' report. Most of the time information presented to the auditors makes performance look bad, whereas the reality on ground shows good performance. This in itself is a reflection of the limitation of reporting accurately the performance of the municipality because not all reports needed by the auditors could be produced. The absence of integrated processes and systems hinders the ability of the municipality to present the various evaluation reports.

Conclusion and Recommendations

This study has shown the importance of performance audit in municipal administration. With the case study of Mogale City Local Municipality, it is obvious that internal and external audits are important routine exercises that stimulate performance. Staffers of the municipality, in realization of the institutions of audit, both internally and externally, are conscious of their activities and the need to perform to standard. As a pro-performance measure,

audit activities have shown the level of performance of the municipality and the continuous striving to ensure improvement over time.

Nevertheless, this does not suggest a perfect measure to induce performance. The lack of synergy between actual performance and available records to attest to this by the external auditor remain problematic. This lack of records of performance is a manifestation of the communication gap among different units and departments of the municipality. While this is unknown to the external auditors, it is a well noted issue by the internal auditor. The beauty of this is the fact that internal audit is a department within a municipality and gets to understand all other functions better. Thus, it is easier for the internal audit to have records of the series of activities of the different units for the purposes of its report.

The disparity in the reports of the internal and external auditors is a reflection of this communication gap. This is a lesson for other municipalities and Mogale City Local Municipality in particular. There should be a synergy between the performance and the records. In other words, all activities of the different units and departments should be properly documented for internal and external scrutiny. This will provide the opportunity for clear-cut assessment of performance with a view to improving service delivery to the people of the Municipality.

There is no doubt that auditing is a measure to improve performance rather than for punishment. The external audit report ought to have pointed out these disparities since there were no records of financial maladministration. External reports so far gave the municipality clean bill of financial records but negative report on performance. The question then arises, that if the performance is negative, why was that financial record clean? The truth here is that while external auditors relied on paper records, there were no attempts to assess the physical performance in terms of visits to the projects because auditors require physical evidence to base their opinion.

Another obvious lapse, which should be avoided, is the absence of ascribed sanctions for failure to perform. However, there are extant rules and regulations, as contained in the various statutes, governing the performance of municipalities in South Africa, it is necessary for each municipality to cultivate the culture of transparency in terms of physical documentation of projects from time to time. While there is a culture of transparency in administration because each officer is aware of the need for service delivery, for record purposes and future references, the preference of the people should be made known while the various projects are being presented to the various committees and statutory bodies.

The Mogale City Local Municipality has demonstrated a high measure of compliance with the requisite demands of the various statutes in terms of performance and service delivery. Adherence to the various targets of the different units has shown a consistent performance over the years though the external reports return negative performance assessment. Reports however show that the municipality has succeeded in meeting its targets. The decentralized system has proven feasible since the various units have shown a measure of commitment to the implementation of its targets. The committee system has greatly improved service delivery within the limit of the available resources. This is worth emulation by other municipalities in the country.

It is apparent from this exploratory study that although audit reports are valuable tools to measure the performance of a municipality, they should not be accepted at 'face value' as a result of the issues raised in this study.

Recommendations

In order to have audit reports which reflect the performance of a municipality there is a great need for an integrated information system that will ensure that information is captured once and filters through to all departments to avoid duplication. Municipalities also need to develop and document policies and procedures for all their processes. These must comply with all municipal statutory and audit requirements to ensure compliance and also assist with training of all employees and these documents should be reviewed by both internal and external auditors annually. Municipalities should improve their relationships with auditors to assist in changing perceptions that auditors are

there to policy and see them as partners. This can be done through continues communication to understand their requirements and auditors providing support and guidance to municipalities.

Continuous training of all employees would be beneficial to keep them up to date with the latest requirements and expectations of their jobs. A performance management process needs to in place for all employees with incentives for excellence and consequence for poor results. There should be more sharing of excellence across all municipalities to assist others to greatness. There are a lot of complexities faced by municipalities as demonstrated above therefore it is difficult to focus on the future. There are changes that can be implemented immediately and some changes will take a while to be implemented but they are needed to improve the functioning of municipalities and the relationships with stakeholders and auditors.

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