



Comparative Analysis of Municipalities that have Consistently Achieved Clean Audits: The Case of West Coast District Municipality, Overstrand Local Municipality and Okhahlamba Local Municipality

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Abstract

The Auditor-General (South Africa) (2024) in her consolidated report of the state of audit outcomes of municipalities expressed a concern about the decreasing number of the quality audit outcomes. In particular, the number of municipalities that achieve clean audit outcomes has over the years decreased which is an indication that some, if not most of South African municipalities, are regressing in terms of governance, performance (service delivery) and financial management. A clean audit opinion is by no means an ultimate reflection that there is effective service delivery. However, it does present the municipality as a transparent organization that is able to function effectively and efficiently in fulfilling its constitutional mandate. It therefore becomes imperative to establish how other municipalities are able to achieve clean audits especially those that have done it consistently over the longer period of time. It is for this reason that the study is a comparative analysis of municipalities that consistently achieved clean audits with a view to learn how they have managed to obtain these clean audit opinions.

Keywords: *Clean Audit; Audit Outcomes; Financial Statements; Local Government; Accountability, Financial Management; Accounting Policies; Auditing Standards; Irrecoverable Debt; Infrastructure Grants; Collection Rate; Creditors; Debtors*

Introduction

Local government all over the world is experiencing difficulties in terms of general financial management which then impacts negatively on the audit outcomes. South Africa is flagged as having municipalities that have continuously failed to comply with municipal legislation (Khaile, et al., 2021).

The Auditor-General of South Africa (AGSA) has also on numerous occasions emphasized that South African municipalities are generally failing to comply with the relevant legislation thus compromising their audit outcomes and service delivery at the same time. When releasing the 2022-2023 consolidated general report, the Auditor-General called on all role-players in the accountability eco-system to work deliberately and with urgency towards a culture of performance, accountability, transparency and institutional integrity to ultimately result in a better life for the people of South Africa (AGSA, 2024). Recurring problems in the audit outcomes of South African municipalities are weaknesses in service delivery planning; failures in reporting achievement; failing municipal infrastructure such as water, electricity and roads; increased pressure on local finances due to lack of prudent financial management.

Seitheisho (2018) states that local governments have come under intense scrutiny recently because of local government's repeated failure to attain clean audit results. Whilst only 13% of South African municipalities obtained clean audits in the 2022-2023 financial year, which is not a good percentage at all, there are a few municipalities that have consistently obtained clean audits for several consecutive years. It then becomes paramount that the audit performance of these municipalities be examined with a view to learn from them.

It is for this reason that three municipalities that have consistently obtained clean audits over the years have been selected and these are West Coast District Municipality (Western Cape), Overstrand Local Municipality (Western Cape) and Okhahlamba Local Municipality (KwaZulu-Natal).

Aim and Objectives of the Study

The main aim of the study was to do a comparative analysis of three municipalities (West Coast District Municipality, Overstrand Local Municipality and Okhahlamba Local Municipality) that have consistently achieved clean audits.

The objectives of the study were to:

- Review the international and national (South African) audit perspectives
- Review the audit landscape in South Africa
- Provide an understanding of the clean audit opinion
- Analyze and compare municipalities that have consistently achieved clean audits during the period under review

Literature Review

International auditing perspective

The challenge of financial mismanagement and irregularities is a global phenomenon and according to Allen and Koshima (2018), in several countries the Supreme Audit Institutions (SAIs) have reported financial irregularities amounting to more than 10 to 15% of the government's total budget expenditure. This is supported by Mnguni and Subban (2022) who maintain that procurement irregularities continue to be a major source of these financial irregularities.

As part of the international standards on auditing, the United Kingdom (UK) Auditor-General (FRC, 2023):

- Identifies and assesses the risks of material misstatements of the entity's financial statements, whether due to fraud or error, designs and performs audit procedures responsive to those risks,

and obtains audit evidence that is sufficient and appropriate to provide a basis for the auditor's opinion.

- Obtains an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.
- Evaluates the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Concludes on the appropriateness of directors' use of the going concern basis of accounting and, based on evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern.
- Evaluates the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

The Auditor's Report is expected to present an audit opinion on the financial statements as a whole and the opinion concludes whether:

- the financial statements adequately refer to or describe the applicable financial reporting framework;
- the financial statements appropriately disclose the significant accounting policies selected and applied;
- the accounting policies selected and applied are consistent with the applicable financial reporting framework, and are appropriate;
- the accounting estimates made by the directors are reasonable;
- the information presented in the financial statements is relevant, reliable, comparable and understandable;
- the information that should have been included has been included, and whether such information is appropriately classified, aggregated or disaggregated, and characterized;
- the overall presentation of the financial statements has been undermined by including information that is not relevant or that obscures a proper understanding of the matter disclosed;
- the financial statements provide adequate disclosures to enable the intended users to understand the effect of material transactions and events on the information conveyed in the financial statements;
- the terminology used in the financial statements, including the title of each financial statement that is appropriate.

The audit outcomes in the UK are categorized according to unmodified, modified, qualified, adverse and disclaimer audit opinions. This categorization is more or less the same as the audit opinions in South Africa where the unmodified audit opinion is popularly known as the clean audit. Within the UK context an unmodified opinion is expressed when the auditor is able to conclude that the financial statements give a true and a fair view and comply in all material respects with the applicable financial reporting framework. A modified opinion is when the auditor concludes that based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or the auditor is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement. A qualified audit opinion is expressed when either misstatements; individually or in the aggregate, are material but not pervasive to the financial statements; or the possible effects on the financial statements of undetected misstatements.

The audit landscape in South Africa

Auditing and financial management is enshrined in the Constitution in South Africa which then emphasizes its importance and high recognition as part of governance and oversight. The Constitution of the Republic of South Africa (Act no. 108 of 1996) Section 181 (1)(e) establishes the Auditor-General of South Africa to audit and report on the accounts, financial statements and financial management of all national, provincial and local state departments and other institutions. The Municipal Finance Management Act, 2003 (Act No. 56 of 2003) further elaborates by seeking to secure sound and sustainable management of the fiscal and financial affairs of municipalities and municipal entities by establishing norms and standards to ensure transparent financial accountability.

The Public Audit Act, 2004

The objects of the Act are:

- to give effect to the provisions of the Constitution establishing, and assigning supreme auditing functions to, an Auditor-General;
- to provide for the auditing of institutions and accounting entities in the public sector; and
- to provide for an oversight mechanism established in terms of section 10(3) –
 - i) to assist and protect the Auditor-General in order to ensure the independence, impartiality, dignity and effectiveness of the Auditor-General; and
 - ii) to advise the National Assembly.

The Auditor-General is empowered by the Constitution of the Republic of South Africa to be the only audit institution in the Republic to have a full legal capacity to audit all government institutions impartially without fear, favour or any prejudice. This supreme authority is further complemented by the fact that the Auditor-General is only accountable to the General Assembly in Parliament which means the office cannot be influenced even by politicians.

The role of the Auditor-General of South Africa

The Public Audit Act, 2004 (Act No. 25 of 2004) empowers the Auditor the Auditor-General to be the only public institution to audit financial management and control in all spheres of government. Section 20 of the Public Audit Act requires the Auditor-General to indicate:

- a) whether the annual financial statements of the auditee fairly present, in all material respects, the financial position at a specific date and results of its operations and cashflow for the period which ended on that date in accordance with applicable financial framework and legislation;
- b) the auditee's compliance with any applicable legislation relating to matters, financial management and other related matters; and
- c) the reported information relating to the performance of the auditee against predetermined objectives.

The Auditor-General is also empowered to investigate and to enquire into any matter, including the efficiency and effectiveness of internal control and management measures relating to expenditure by and revenue of an institution whose accounts are being audited. The Constitution also authorizes the Auditor-General to investigate whether any property, money, securities, loans, equipment, stores and other assets of an institution whose accounts are being audited have been obtained in an economical manner and are being applied for efficiently and effectively (Nzewi & Musokeru, 2014).

The clean audit opinion

The Auditor-General Report (2024) defines the Clean Audit Outcome as the opinion where the financial statements do not contain material errors and there are no material findings on performance information and compliance with legislation. The Auditor-General further amplifies that when a municipality receives a clean audit, this means it has accurate records that allows it to communicate transparently to communities about whether and when their needs will be met. This enables the Council and its stakeholders to judge the Council's performance. The Auditor-General Report (2024) recorded 1 Clean Audit for Metropolitan Municipalities, 4 for intermediate cities, 11 for district municipalities and 18 for local municipalities which totals 34 Clean Audits for the 2022/2023 financial year for all municipalities. This then translates to only 13% of municipalities that obtained clean audits in 2022/2023 financial year.

Good practices for clean audits

According to the Auditor-General Report (2024) municipalities that achieve clean audits have strong control environments that enable reliable financial and performance reporting and good practices that can be replicated. Municipalities that have institutionalized controls and systems in place to plan, measure, monitor and account for their finances and performance are more likely to have a solid foundation on which municipalities can build to improve their performance and deliver most of the promised services.

Effective planning for service delivery

Municipalities that get clean audits plan carefully and effectively for service delivery. Their Service Delivery Budget and Implementation Plans (SDBIPs) specify smart performance indicators that cover all their core delivery functions. They also have very effective Procurement Plans where all procurement is finalized before the end of the financial year so that projects are on the ground in the new financial year. This is aligned to the effective internal controls for effective monitoring of the performance of service providers and effective expenditure control. These municipalities have very effective budget planning processes that involve effective public participation where the views of the public are considered and effected in the budget. It should be noted though that clean audit outcomes cannot necessarily be equated to best service delivery. According to Matlala and Uwizeyimana (2020) the results of municipal audits are often reflections of the performance of a municipality in terms of delivering public services; however, their impact on service delivery appears to be limited and the relationship between the two variables (service delivery and financial performance which includes auditing) becomes even weaker in cases where municipalities lack key operational resources.

Communities are also given various platforms to monitor the budget implementation process and there is also very effective customer relations management which enables seamless complaints management system and reporting of service outages and the ability for effective turnaround in resolving complaints.

Investment in infrastructure projects and asset management

Many municipalities that obtain qualified audit opinions have challenges with infrastructure projects, asset management and even in some cases asset information. Municipalities that obtain clean audits can provide 8% of their capital budget to maintenance of infrastructure. New projects are properly monitored and captured accurately in the assets register once completed. They have a proper asset management system that stores all asset information including accurate information on ageing and lifespan of assets. They also ensure that the new assets are of high quality.

Strong and well performing governance ecosystem

Municipalities that get clean audits have competent, properly qualified and competent administrators. Dodo (2017) confirms that lack of personnel with financial audit capabilities and technical experience and inadequate internal controls have contributed to the negative audit outcomes. Municipal finance and Supply Chain management staff are properly qualified to perform their duties. There is a continuous and well-understood culture of good governance, high levels of productivity and high levels of accountability enforced right from the top to the lower levels. Consequence management is a priority and there is no tolerance for non-performance. All Council structures are in place and the accountability structures such as the Audit Committee, Ethics Committee, Public Accounts Committee are able to provide independent assurance and enforce accountability at all levels. There is an entrenched culture of good governance across the municipality practised even at lower levels. Good governance is also extended to and well-practised councillors who have a good understanding of their roles, mandate and means of engagement with their communities and are not interfering with administration.

Operation clean audit

The Operation Clean Audit is a bold strategy that was approved by government (to be led by the Department of Cooperative Governance and Traditional Affairs) in 2010. The main vision of the Operation Clean Audit was to have all 283 municipalities (at the time) in South Africa obtain and maintain clean audits. It is important to note that this target was never achieved however it is appreciated that government had such an ambitious target and there is a good reason why this strategy should be revisited because the failure is attributable to failed implementation not necessarily that it was a bad strategy. The Operation Clean Audit Strategy focused on 3 main focus areas which are adequate leadership involvement and oversight, effective governance arrangements and conducive financial management environment. The strategy also emphasized the importance of effective financial management systems for they make the job of overall financial management and accountability easy.

Comparative analysis of municipalities that have constantly achieved clean audits

The three selected municipalities (West Coast District Municipality, Overstrand Local Municipality and Okhahlamba Local Municipality) are comparatively analysed with a view to establish how they have successfully sustained clean audits.

West Coast District Municipality

West Coast District Municipality is a district municipality located in the Western Cape province and its seat is at Moorreesburg and is currently led by the Democratic Alliance (DA). It has consistently obtained clean audits for 5 consecutive years since 2018/2019 financial year until the last financial year (2023/2024). The municipality has consistently submitted financial statements for auditing by the legislated date which is the end of August and were of high quality. There were no findings on non-compliance with the legislation. There were no material findings on supply chain management. They never had any unauthorised expenditure over the period. They had fruitless, wasteful and irregular expenditure which totalled about R8m but was all regularized on time. The municipality on average took 26 days to pay creditors and the statutory requirement is less than 30 days. Only 2% of the municipal debt is irrecoverable. The municipality owned more than what it is owed. There was no overdraft used. More than 10% of the next year's budget was already spent in previous years. Infrastructure grants non-expenditure was less than 10%. The municipality spend 66% of the value of infrastructure assets on maintenance (the National Treasury norm is 8%).

Overstrand Local Municipality

Overstrand is a local municipality in the Western Cape province with its seat at Hermanus and is under the Overberg District Municipality. It is a very small municipality with 13 wards led by the

Democratic Alliance (DA). It has consistently obtained clean audits for 5 consecutive years under review since 2018/2019 financial year till the last financial year 2023/2024.

The municipality submitted its financial statements by the legislated date which is the end of August every year and were of good quality. There were no findings on non-compliance with legislation. There were no material findings on supply chain management. They had unauthorized expenditure of about R55m. Their combined fruitless, wasteful and irregular expenditure was about R5m, but all these were regularized. The municipality on average took 32 days to pay creditors which is 2 days above the National Treasury norm of 30 days. 29% of municipal debt is irrecoverable and it takes an average of 30 days to collect debt. The municipality owes more than what it is owed. It had money in the bank and had not used any overdraft. More than 10% of the next year's budget was already spent in previous years. The municipality did not underspend its infrastructure grants by more than 10%. It spent 6.1% on infrastructure maintenance.

Okhahlamba Local Municipality

Okhahlamba is a local municipality in the KwaZulu-Natal province and its seat is in Bergville and is led by the African National Congress (ANC). It has consistently obtained clean audits for 5 consecutive years under review since 2018/2019 until the last financial year 2023/2024. The municipality has consistently submitted financial statements within the legislated date which is before the end of August every year and were of good quality. There were no findings on financial statements. The municipality paid its creditors on average within 21 days (below the National Treasury norm of 30 days). It took them an average of 45 days to collect debt. It owned more than it is owed. More than 50% of the next year's budget had already been spent in previous years. They did not underspend infrastructure grants by more than 10%. They only spent 1.4% towards maintenance of infrastructure.

Research Methodology

The study was comparative in nature looking at how the three municipalities had managed to consistently achieve clean audits for a period of 5 consecutive years during the review period from 2018-2024.

Research Findings

Findings on the financial statements

All three municipalities had consistently submitted their financial statements by the legislated date which is the end of August every year and all financial statements were of good quality (no findings).

Findings on compliance with the legislation

None of the three municipalities had a finding on non-compliance with legislation governing local government. This is key if a municipality wants to achieve a clean audit. None of the municipalities were found to be non-compliant with supply chain management (SCM). This therefore means their processes were transparent, their tenders were awarded fairly and openly through a competitive bidding process and there was no corruption in the supply chain management processes.

Findings on unauthorized, irregular, fruitless and wasteful expenditure (UIFW)

It is only West Coast District Municipality that did not have unauthorized expenditure, and all three municipalities had irregular, fruitless and wasteful expenditure. It is important to note that all three municipalities regularized these kinds of expenditure as per the legislated requirements. This however

confirms that a municipality can still obtain a clean audit even if it has the UIFW as long as it regularizes it as per legislation and keeps it minimal. There is no actual benchmark to the minimum of the UIFW but anything less than 20% of the total budget (both operational and capital budgets) may not attract a finding if properly regularized.

Findings on the days to pay creditors

Only Overstrand Municipality took more than the prescribed 30 days to pay its creditors (32 days). Because this was an average over 5 years it did not affect their clean audit opinion. It is also important to note that municipalities can avoid a finding on the creditors' payments by giving a proper explanation.

Findings on debtors

Whilst West Coast District Municipality had 2% of irrecoverable debt, Overstrand and Okhahlamba Local Municipalities had less than 29% respectively. This therefore means that a municipality can still obtain a clean audit even if it has irrecoverable debt as long as it keeps it minimal and uses proper write-off procedures every year.

Findings on liquidity

All three municipalities owned more than what they were owed. They all had never used an overdraft in the 5 years under review and had all started expenditure for the following years in the previous years. Both West Coast and Overstrand municipalities kept their operations and maintenance budget within or above the statutory 8%. All three municipalities did not underspend infrastructure grants by more than 10%.

What can be concluded from these findings is that every municipality can get a clean audit, and it does not mean that municipalities must be 100 percent in everything, what is important is to ensure that the financial statements are of good quality and are submitted on time and are based on policy provisions. When municipalities have faltered there are mechanisms in terms of legislation to corrective measures for example regularization of any UIFW. One other area that is important to adhere to when municipalities want to achieve clean audits is compliance with legislation and the supply chain management. The latter is usually the area that leads to irregular or delayed expenditure sometimes because of proliferation of corruption.

Recommendations

The following are some of the recommendations for municipalities if they want to achieve clean audits:

- Municipalities should build capacity to prepare financial statements that are of quality and are free from any misstatements and these must be submitted on time before the end of August every year.
- They must ensure that they comply with all municipal legislation and reporting mechanisms to all different stakeholders within the stipulated deadlines.
- They must comply with all supply chain management legislation and processes and ensure that their procurement is open, transparent and competitive and above all free of corruption.
- They must keep the UIFW at least to less than 20% of the total expenditure and ensure that they follow the regularization processes including effective consequence management effectively.
- They must ensure that they comply with National Treasury norms such as the creditors' payment period, liquidity ratios, cash on hand, debt collection period, etc.
- They must keep irrecoverable debt to the minimum and also ensure that it is properly written-off.

- They must avoid using overdraft at all costs and only use it for emergencies and ensure repayment soon thereafter.
- They must ensure that they finalize procurement of the following year a financial year beforehand so that expenditure starts by the beginning of the new financial year.
- They must ensure 100% of grants, operational and capital expenditure.
- They must ensure that they provide for 8% in the budget for operation and maintenance of infrastructure.

Conclusion

The study was a comparison of three municipalities that have consistently achieved clean audits over a period of time and these municipalities are West Coast District Municipality (Western Cape), Overstrand Local Municipality (Western Cape) and Okhahlamba Local Municipality (KwaZulu-Natal). All three municipalities have achieved more than 10 clean audits however the period under review was a five-year period where they had consistently and consecutively achieved clean audits from 2018 to 2024. The main reason for choosing these municipalities was to find out how they are able to consistently achieve clean audits so that their strategies can be replicated by other municipalities.

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