

REPORT OF THE AUDITOR-GENERAL TO THE MUNICIPAL COUNCIL AND KWAZULU-NATAL PROVINCIAL LEGISLATURE ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF UMSHWATHI MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2007

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the Umshwathi Municipality which comprise the balance sheet as at 30 June 2007, income statement and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages 6 to 14.

Responsibility of the accounting officer for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the basis of accounting determined by National Treasury, as set out in accounting policy note 1 to the financial statements and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA). This responsibility includes:
 - designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
 - selecting and applying appropriate accounting policies
 - making accounting estimates that are reasonable in the circumstances.

Responsibility of the Auditor-General

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA) and section 92 of the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA), my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with the International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements 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.

6. An audit also includes evaluating the:
 - appropriateness of accounting policies used
 - reasonableness of accounting estimates made by management
 - overall presentation of the financial statements.
7. Paragraph 11 et seq. of the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of Financial Statements* requires that financial reporting by entities shall provide information on whether resources were obtained and used in accordance with the legally adopted budget. As the budget reporting standard is still in the process of being developed, I have determined that my audit of any disclosures made by the Msunduzi Municipality in this respect will be limited to reporting on non-compliance with this disclosure requirement.
8. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Basis of accounting

9. The municipality has not prepared the financial statements on a basis of accounting determined by the National Treasury.

Basis for a qualified opinion

Provisions

10. A recalculation of the provision for bad debts on debtors outstanding for more than 90 days (per the summarised age-analysis) was compared to the bad debt provision. This comparison indicated that the bad debt provision was understated by R7,5 million.

Other

11. A material casting error amounting to R2 million exists in the prior year's Distributable reserves total.

Property, plant and equipment

12. A material difference of R898 000 exists between the fixed asset register and the financial statements. Furthermore, the accounting policy for property, plant and equipment does not state the depreciation rate and the useful life of each asset used to calculate depreciation.

Receivables

13. Unsupported balances of R404 000 and (R419 000) were included in debtors. Explanations for these balances could not be provided and consequently, I was unable to establish their reasonability.

Qualified opinion

14. In my opinion, except for the effects of the matters described in the Basis for qualified opinion paragraphs, the financial statements of Umshwathi Municipality as at 30 June 2007 and its financial performance and cash flows for the year then ended have been prepared, in all material respects, in accordance with the basis of accounting as set out in accounting policy note 1 and in the manner required by the MFMA.

Emphasis of matter

I draw attention to the following matters:

Basis of accounting (departures and deviations)

15. From a review of the financial statements and accounting policy 1 - Basis of preparation, it was noted that the municipality has only partly adopted Standards of GAMAP. In terms of General Notice 552 of 2007 issued by the Minister of Finance, there is no provision for the partial adoption of the standards, other than the exemptions permitted by the aforementioned notice. Evidence of correspondence from the Department of Finance permitting partial adoption was requested, but was not produced for audit purposes.

OTHER MATTERS

I draw attention to the following matters that are ancillary to my responsibilities in the audit of the financial statements:

Non-compliance with applicable legislation

16. Municipal Finance Management Act

The budget was not tabled at least 90 days before the start of the financial year, as required by section 16(2) of the MFMA.

The municipality did not perform an asset count in the year under audit. In this regard, attention is invited to section 63(2)(c) of the MFMA, which states that the accounting officer must take all reasonable steps to ensure that the municipality has and maintains a system of internal control of assets and liabilities.

No evidence exists that the accounting officer within 30 days after the end of each quarter submitted a copy of the consolidated report of withdrawals reported to council to the Auditor-General and provincial treasury, as required by section 11(4) of the MFMA.

17. Basic Conditions of Employment Act

It was noted that employees had worked excessive overtime which, in some instances, were above 30% of their basic income. This was in contravention of section 10 of the Basic Conditions of Employment Act.

Matters of governance

18. No disclosure has been made in the financial statements for related party transactions incurred with councillors during the year.

Material corrections made to the financial statements submitted for audit

19. The financial statements, approved by the accounting officer and submitted for audit on 30 August 2007, have been significantly revised in respect of the following misstatements identified during the audit:

- Differences between the general ledger, trial balance and financial statements affecting the appropriation account, amounting to R7,7 million and R305 000, were corrected.
- A difference between the trial balance and financial statements affecting the cash and cash equivalents, amounting to R1,3 million was corrected.
- Interest income of R323 000 was reclassified as other income.
- Investments of R7,6 million was reclassified as current assets, and a difference between the trial balance and financial statements affecting the investments, amounting to R8 million was corrected.
- A transaction amounting to R3 million between the asset financing fund and the NDR reflected in the financial statements but not effected in the general ledger, was corrected.
- The asset financing fund was adjusted by R4,4 million from R11,2 million in order for the fund to be covered by investments.
- Creditors were adjusted by R698 000 due to credit balances being included in the debtors listing, and a difference between the trial balance and financial statements.
- Unexplained adjustments amounting to R5,3 million were made to debtors.

Value-for-money matters

20. Supply chain management regulations

Cases exist where the services of suppliers were procured without complying with the SCM policy and with regulation 35 of the SCM regulations.

Internal control

21. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes of the matters indicated, as they relate to the five

components of internal control. In some instances deficiencies exist in more than one internal control component.

Reporting item	Control environment	Assessment of risks	Control activities	Information and communication	Monitoring
Basis for qualified opinion					
Provisions			X		X
Other			X		X
Property, plant and equipment			X		X
Receivables			X		X
Emphasis of matter					
Basis of accounting (departures and deviations)					X
Other matters					
Non-compliance with applicable laws and regulations	X				
Matters of governance			X		X
Material corrections to the financial statements	X		X		X
Value for money matters			X		X

Unaudited supplementary schedules

22. The supplementary information set out on pages 15 to 21 does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion on them.

OTHER REPORTING RESPONSIBILITIES

Reporting on performance information

23. I was engaged to audit the performance information.

Responsibility of the accounting officer for the performance information

24. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

Responsibility of the Auditor-General

25. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 646 of 2007*, issued in *Government Gazette No. 29919 of 25 May 2007* and section 45 of the MSA.

26. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.
27. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

Audit findings (performance information)

Non-compliance with regulatory requirements

Process to guide planning, drafting, adoption and review of integrated development plan (IDP)

28. It was established that although ward committee meetings are held in order to consult with communities prior to drafting the IDP, no minutes are kept as evidence that these meetings in fact took place.

Setting of key performance indicators

29. It was established that although the municipality has entered into contracts with service providers, no service level agreements have been entered into informing the service providers of the key performance indicators expected. Attention is invited to regulation 9(2) of the Local Government: Municipal Planning and Performance Management Regulations, 2001.

Establishment of a performance management system

30. It was established that although the municipality has a performance management system, this is limited to section 57 employees only. In this regard, your attention is invited to sections 38 and 39 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000), and regulation 7(1) prescribing the requirements of a performance management system.

Monitoring, measurement and review of performance

31. It was established that as a result of capacity constraints, the monitoring, measurement and review of performance, as required by regulation 13 of the Local Government: Municipal Planning and Performance Management Regulations, 2001, was not done.

APPRECIATION

32. The assistance rendered by the staff of the Umshwathi Municipality during the audit is sincerely appreciated.

Auditor - General

Pietermaritzburg

14 December 2007



A U D I T O R - G E N E R A L