



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

**REPORT ON THE FINANCIAL STATEMENTS**

**Introduction**

1. I have audited the accompanying financial statements of Mpofoana 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, and the accounting officer's report, as set out on the following pages.

**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 Institute of Municipal Financial Officers in its Code of Accounting Practice 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), 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. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

#### **Basis of accounting**

8. The municipality's policy is to prepare financial statements on the basis of accounting determined by the National Treasury as set out in accounting policy note 1 to the financial statements.

#### **Basis for qualified opinion**

##### **9. Limitation of scope**

The failure to furnish various supporting documents, satisfactory explanations, working papers and accounting records to substantiate the following balance sheet and income statement amounts in the financial statements limited the scope of the audit. For the year under review, the scope of my audit has been limited in the following areas:

##### **9.1 Income**

We were unable to verify the completeness and accuracy of the following categories of revenue:

**9.1.1** Prepaid electricity income as per the schedule provided from the system does not agree to the general ledger. Furthermore, the prepaid electricity receipts listing provided does not agree to the general ledger. No reconciliation was provided for the difference of R194 000.

**9.1.2** Reconnection fees per the report generated from the Venus System for connection fees reflected an amount R68 000 while the general ledger reflected an amount of R141 000. No reconciliation was provided for the difference of R73 000.

##### **9.2 Debtors**

The total per the debtors age-analysis provided for audit amounted to R56,7 million while the balance per the financial statements amounted to R56,4 million. No reconciliation was provided for the difference of R300 000. We are therefore unable to verify the accuracy, existence and completeness of the debtors balance at 30 June 2007.

The accounting policy states that a provision should be made on all debtors outstanding for greater than 90 days. The total as per the debtors age analysis for all debtors outstanding for greater than 90 days amounted to R46 million however the provision for doubtful debts only amounted to R41 million. Therefore, it appears that the provision is understated by R5 million.

##### **9.3 Long term liabilities**

The existence, valuation and completeness of the loan from Umsekeli Municipal Support Services amounting to R1 million could not be verified as no adequate documentation was made available for audit.

#### **Qualified opinion**

In my opinion, except for the effects of the matter(s) described in the Basis for qualified opinion paragraphs, the financial statements of Mpofana 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:

##### **10. Going concern**

It was noticed that while the municipality appeared to be in a net asset financial position at 30 June 2007, its current asset base comprised debtors which were considered slow paying and long outstanding at year end. The inability to recover debts on a regular basis has a negative impact on the cash flows which was overdrawn by R2,6 million. Furthermore, statutory funds and reserves of R34 million were not supported by sufficient concomitant assets (cash and investments) of R18,7 million.

##### **11. Highlighting a matter affecting the financial statements (that is disclosed in a note)**

**11.1** As indicated in note 6 of the financial statements, included in the assets balance is an amount of R19 million in respect of water and sanitation assets which will be transferred to uMgungundlovu District Municipality when the water function is taken over and agreements have been finalised.

**11.2** As indicated in note 10 of the financial statements, included in the debtors balance is an amount of R30,3 million in respect of water and sanitation debtors which will be transferred to uMgungundlovu District Municipality when the water function is taken over and agreements have been finalised.

#### **OTHER MATTERS**

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

##### **12. Non-compliance with applicable legislation**

No formal risk management policy or process has been established and incorporated into the municipality's system to assess, manage and control risk on a continuous basis as required by section 62(1)(c) of the MFMA.

##### **13. Material corrections made to the financial statements submitted for audit**

The financial statements, approved by the accounting officer as submitted for audit on 27 August 2007 were amended as follows:

**13.1** Fixed assets balance was understated in the financial statements which resulted in adjustments of R19 million to the fixed asset balance for additions and disposals, R19 million to capital grants and R666 000 to capital revenue.

**13.2** Investments were overstated in the financial statements which resulted in an adjustment of R593 000 to the investment and reserve balance.

**13.3** The bank balance was understated in the financial statements which resulted in an adjustment of R139 000 to the bank and debtors balance.



- 13.4** Sundry creditors was understated in the financial statements which resulted in an adjustment of R1,5 million to sundry creditors, R1,3 million to expenditure and R181 000 to VAT.
- 13.5** Provision for doubtful debts was understated in the financial statements which resulted in an adjustment of R30 million to provision for doubtful debts and accumulated deficit.
- 13.6** Debtors were understated in the financial statements which resulted in an adjustment of R30 million to debtors and accumulated deficit.

**14. Internal control**

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.

Finding	Control environment	Assessment of risks	Control activities	Information and communication	Monitoring
<b>Basis for qualification opinion</b>					
Income			X	X	
Debtors			X	X	X
Long-term liabilities			X		X
<b>Emphasis of matter</b>					
Going concern	X		X		
Highlighting a matter affecting the financial statements				X	
<b>Other matters</b>					
Non compliance with applicable legislation	X		X		



Finding	Control environment	Assessment of risks	Control activities	Information and communication	Monitoring
Material corrections made to the annual financial statements	X		X	X	X
<b>Other reporting responsibilities</b>					
Performance measurement	X		X	X	X

**Unaudited supplementary schedules**

**15.** The supplementary information set out on pages 22 to 27 do 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**

**16.** I was engaged to audit the performance information.

**Responsibility of the accounting officer**

**17.** 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**

**18.** I conducted my engagement in accordance with section 13 of the Public Audit Act, 2004 (Act No. 25 of 2004) read with *General Notice 646 of 2007*, issued in *Government Gazette No. 29919 of 25 May 2007* and section 45 of the MSA.

**19.** 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.

**20.** I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

**Audit findings**

**21.** The municipality has not reported performance against predetermined objectives as required by section 46 of the MSA.

**22.** The municipality has not adopted a performance management system before or at the same time as the commencement of the process of setting key performance indicators.

23. The IDP does not contain the performance targets determined in terms of section 41.
24. The IDP does not include an organogram required for the implementation of the IDP and addressing the municipality's transformation needs

**25. APPRECIATION**

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

*Auditor-General*

Pietermaritzburg

30 November 2007



AUDITOR - GENERAL