

AUDITOR'S REPORT OF THE AUDITOR-GENERAL TO THE EASTERN CAPE PROVINCIAL LEGISLATURE AND THE COUNCIL ON MALETSWAI MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the accompanying financial statements of Maletswai Municipality, which comprise the statement of financial position as at 30 June 2010, and the statement of financial performance statement of changes in net assets and cash flow statement for the year then ended, a summary of significant accounting policies and other explanatory information as set out on pages XX to XX.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with Generally Recognised Accounting Practice and in the manner required by the Municipal Finance Management Act of South Africa and the Division of Revenue Act of South Africa. 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; and making accounting estimates that are reasonable in the circumstances.

Auditor-General's responsibility

3. As required by section 188 of the Constitution of South Africa, 1996 (Act No. 108 of 1996) and section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on these financial statements based on conducting the audit in accordance with the International Standards on Auditing and General Notice 1570 of 2009 issued in Government Gazette 32758 of 27 November 2009. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer opinion paragraph

Revenue from non-exchange transactions

4. In terms of South African Statement of Generally Recognised Accounting Practice, GRAP 23, *Revenue from non-exchange transactions*, revenue from a non-exchange transaction shall be measured at the amount of the increase in net assets recognised by the entity. Revenue amounting to R290,780 has been recognised at the incorrect amount due to incorrect rates being used in the calculations of rates revenue. Revenue from non-exchange transactions is thus overstated by this amount.

Other revenue

5. There was no supporting documentation to supporting an amount of R192,175 disclosed under fines, and there was no satisfactory audit procedures that I could perform to obtain reasonable assurance that the fines occurred, were accurate, correctly classified and related to the year under review.
6. There was no system of control over traffic fines on which I could rely for the purpose of my audit, and there were no satisfactory audit procedures that I could perform to obtain reasonable assurance that all fine revenue was properly recorded. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness of fine revenue of R223,957.

Revenue from exchange transactions

7. There was no supporting documentation available to support an amount of R2,1million disclosed as water service authority contribution, and there was no satisfactory audit procedures that I could perform to obtain reasonable assurance that the water services authority contribution was accurate.
8. There was no supporting documentation available to support an amount of R206,545 disclosed under rental of facilities and equipment, and there was no satisfactory audit procedures that I could perform to obtain reasonable assurance that the amount included under rental of facilities and equipment occurred, was accurate, correctly classified and related to the year under review.
9. There was no system of control over revenue from Electricity Re-Connection Fees disclosed under other income in note 24 to the financial statements, and there were no satisfactory audit procedures that I could perform to obtain reasonable assurance that all other income from Electricity Re-Connection Fees was properly recorded. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness of Electricity Re-Connection Fees of R735,658 disclosed in note 24 to the financial statements.
10. There was no system of control and documentation over additional refuse pickups to be included as services charges under revenue from exchange transactions on which I could rely for the purpose of my audit, and there were no satisfactory audit procedures that I could perform to obtain reasonable assurance that all service charge revenue was properly recorded. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness of refuse revenue to value of R4.2million included under service charges.
11. There was no supporting documentation available to support an amount of R455,260 disclosed under other income in note 24 to the financial statements, and there was no satisfactory audit procedures that I could perform to obtain reasonable assurance that the amount included under other income occurred, was accurate, correctly classified and related to the year under review.
12. In terms of South African Statement of Generally Recognised Accounting Practice, GRAP 9, *Revenue from exchange transactions*, revenue from an exchange transaction shall be measured at the fair value of the consideration received or receivable. Revenue for electricity amounting to R192,381 was recognised using the incorrect rates. As a result, revenue from exchange transactions has been overstated by this amount.
13. In terms of the credit control policy of the municipality, interest must be charged on debtors past the due date. Interest on outstanding debtors was not charged on various debtors accounts due to a system error that occurred. Interest amounting to R63,843 was thus not recognised and as a result I am not able to confirm the completeness of revenue from exchange transaction and trade and other receivables from exchange transactions and revenue has been understated by this amount.
14. In terms of South African Statement of Generally Recognised Accounting Practice, GRAP 9, *Revenue from exchange transactions*, revenue from an exchange transaction shall be measured at the fair value of the consideration received or receivable. Revenue for rentals of facilities and equipment amounting to R49,097 was not recognised as the escalations in terms of lease agreements was not applied. As a result I cannot confirm the completeness of revenue from exchange transactions and revenue has been understated by this amount.
15. As a result of a lack of system of control and documentation over revenue from Rental of Facilities and Equipment disclosed in the financial statements there were no satisfactory audit procedures that I could perform to obtain reasonable assurance that all revenue from Rental of

Facilities and Equipment was properly recorded. Consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the completeness of Rental of Facilities and Equipment of R1.5million disclosed in the financial statements.

Other receivables from non-exchange transactions

16. There was no supporting documentation available to support an amount of R110,579 included as other debtors in note 17 to the AFS and there were no satisfactory audit procedures that I could perform to obtain reasonable assurance that the amount included under other debtors existed.
17. There was no supporting documentation available to support an amount of R10.6million disclosed as Joe Gqabi District Municipality in note 17 to the AFS and there were no satisfactory audit procedures that I could perform to obtain reasonable assurance that the amount disclosed as Joe Gqabi District Municipality was correctly valued.
18. Included in other receivables from non-exchange transactions are amounts that have been outstanding for a long period of time and no payments subsequent to year end have been received. An impairment loss has not been recognised in accordance with South African Statement of Generally Accepted Accounting Practice, IAS 39, *Financial instruments: Recognition and Measurement*. Had this impairment loss been recognised other receivables from non-exchange transactions and accumulated surplus would have been reduced by an amount of R499,413.

Trade and other payables

19. Included in other creditors in note 7 to the financial statements is an amount of R1.2 million owing by the municipality. The amount was recognised in a prior financial reporting period and the municipality was unable to provide an explanation or supporting documentation to support the amount disclosed. As a result I am not able to confirm the valuation, rights and obligations and existence of this amount disclosed under other creditors.
20. Included in trade and other payables are debtors with credit balances of R917,193. The amount includes credit balances for indigent debtors that arose because subsidies were allocated to the debtors account but no debt was raised for services provided. An amount of R145,750 has therefore not been recognised as debtors in terms of South African Statement of Generally Accepted Accounting Practice, IAS 39, *Financial Instruments: Recognition and measurement*. Revenue and receivables are understated by this amount.
21. Included in trade and other payables is an amount of R671,839 for unidentified deposits. These amounts had been deposited by customers of the municipality for monies owing. This would either have been allocated to the debtors account or recognised as revenue depending on what the amount was for. The municipality was unable to provide any supporting documentation or explanations on why the amounts had been deposited into their bank account. The entities records did not permit the application of alternative audit procedures and consequently, I was unable to obtain sufficient appropriate audit evidence to satisfy myself as to the allocation of monies received. As a result revenue and trade receivables are understated and overstated respectively by an unknown allocation of the amount above.

Property, plant and equipment

22. The entity did not conduct regular asset counts to ensure that all property, plant and equipment was disclosed in the financial statements as required by the Standard of Generally Recognised Accounting Practice, GRAP 17, *Property, plant and equipment*. As a result I am not able to confirm the existence and rights and obligations of assets amounting to R1.9 million.

Inventory

23. Inventory consisting of fuel amounting to R13,463 was disclosed in the financial statements. During the audit it was discovered that the municipality maintains an inventory of electrical supplies which were not disclosed in the amount above. An inventory count of electrical supplies at 30 June was not conducted and an inventory listing of electrical supplies as at 30 June was not provided for audit purposes. As a result I cannot determine the completeness of inventory in the financial statements.

Employee benefits

24. In terms of South African Statement of Generally Accepted Accounting Practice, IAS 19, *Employee Benefits*, employee benefits include short term employee benefits such as paid annual leave. Audit procedures conducted on leave balances showed that leave days taken were not updated in the leave system and the balance of leave days was therefore overstated at year end. Leave days used to calculate the staff leave disclosed under employee benefits was therefore incorrect and the amount disclosed in note 5 to the financial statements has been overstated by an amount of R1.3million.

Corresponding figures

25. In my audit report on the financial statements for the year ended 30 June 2009 I was unable to express an opinion due to the material and pervasive nature of my findings. As a result the impact on the current period financial statements could not be determined and my opinion on the current period financial statements is modified in this regard.

Disclaimer of opinion

26. Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on these financial statements.

Emphasis of matter

27. I draw attention to the matters below. My opinion is not modified in respect of these matters:

Restatement of corresponding figures

28. As disclosed in note 33 to the financial statements, the corresponding figures for 30 June 2009 have been restated as a result of the change in accounting standards from IMFO to GRAP.

Matters important to the users of the financial statements:

Unauthorised and fruitless and wasteful expenditure

29. As disclosed in note 41.1 to the financial statements, unauthorised expenditure to the value of R8, 3million was incurred due to overspending particular votes and utilising unspent conditional grants for operating activities.

30. As disclosed in note 41.2 to the financial statements, fruitless and wasteful expenditure to the value of R63,994 was incurred due to interest incurred on late payments to suppliers.

Material losses

31. As disclosed in note 41.4 to the financial statements, material losses to the amount of R3,6million were incurred as a result of distribution losses in the provision of electricity.

Material under spending of the budget

32. As disclosed in note 40.3 to the financial statements, the municipality has materially under spent the budget on capital expenditure to the amount of R3,6million.

Additional matter

33. I draw attention to the matter below. My opinion is not modified in respect of this matter

Unaudited supplementary schedules

34. The supplementary information set out on pages XX to XX 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 thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

35. As required by the PAA and in terms of *General Notice 1570 of 2009* issued in *Government Gazette 32758 of 27 November 2009*, I include below my findings on the report on predetermined objectives, compliance with the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and financial management (internal control).

Predetermined objectives

36. Material findings on the report on predetermined objectives, as set out on pages XX to XX, are reported below:

Usefulness of information

37. The following criteria were used to assess the usefulness of the planned and reported performance:

- Consistency: Has the municipality reported on its performance with regard to its objectives, indicators and targets in its approved integrated development plan, i.e. are the objectives, indicators and targets consistent between planning and reporting documents?
- Relevance: Is there a clear and logical link between the objectives, outcomes, outputs, indicators and performance targets?
- Measurability: Are objectives made measurable by means of indicators and targets? Are indicators well defined and verifiable, and are targets specific, measurable, and time bound?

The following audit findings relate to the above criteria:

38. The targets for the following indicators are not consistent between the SDBIP and the annual report:

- Storm water
- Construction of Joe Gqabi bus route

39. The target for electrifications differs from the SDIB to the IDP

40. The IDP and SDBIP do not contain specific targets for the following objectives:

- Road and transport
- Electrification

- Water and sanitation

Reliability of information

41. The following criteria were used to assess the reliability of the planned and reported performance:

- **Validity:** Has the actual reported performance occurred and does it pertain to the entity i.e. can the reported performance information be traced back to the source data or documentation?
- **Accuracy:** Amounts, numbers and other data relating to reported actual performance has been recorded and reported appropriately.
- **Completeness:** All actual results and events that should have been recorded have been included in the reported performance information.

The following audit findings relate to the above criteria

42. It was not possible to determine if all the meter changes as reported in the annual report did occur as the municipality did not keep sufficient documentation on the installation of electricity meters.
43. The monthly reports on predetermined objectives do not agree to what was reported on in the annual report. The annual report states that 758 water connections took place during the year whereas the monthly reports show that only 333 connections took place.
44. The annual performance report does not reflect indicators for the following projects:
- Electrification for area 13
 - Storm water construction
 - Grading of streets (Jamestown and Aliwal North)
 - Fixing of Electricity and water faults
 - Joe Gqabi Bus route

Compliance with laws and regulations

Municipal Finance Management Act of South Africa, (Act No. 56 of 2003) (MFMA)

Expenditure was not paid within the parameters set by applicable legislation

45. Section 65(2)(e) of the MFMA states that the accounting officer must take all reasonable steps to ensure that all money owing by the municipality be paid within 30 days of receiving the relevant invoice or statement, unless prescribed otherwise for certain categories of expenditure. Audit procedures conducted on a sample of expenditure revealed that payments to the value of R236,897 were not paid within 30 days of receipt of invoice or statement.

Misstatements in the financial statements

46. The financial statements submitted for audit did not comply with section 122(1) of the MFMA. Material misstatements were identified during the audit and were not corrected. These misstatements are included in the basis for disclaimer of opinion paragraphs.

Responsibilities of the accounting officer

47. The accounting officer did not take all reasonable steps to ensure that fruitless and wasteful expenditure incurred was prevented as required by section 62(1)(d) of the MFMA.

INTERNAL CONTROL

48. I considered internal control relevant to my audit of the financial statements and the report on predetermined objectives as well as compliance with the MFMA, but not for the purpose of expressing an opinion on the effectiveness of internal control.
49. The matters reported below are limited to the significant deficiencies regarding the basis for disclaimer of opinion paragraph, the findings on the report on predetermined objectives and the findings on compliance with laws and regulations.

Leadership

50. The accounting officer did not exercise oversight responsibility over reporting and compliance with laws and regulations and internal control.

Financial and performance management

51. Manual and automated controls were not designed to ensure that the transaction occurred, were authorised and were completely and accurately processed.
52. Management and staff did not fulfil all their duties and responsibility and pertinent information was not identified and captured in a form and time frame to support financial and performance reporting.

OTHER REPORTS

Investigations

53. An investigation was conducted by PricewaterhouseCoopers over cheque payments at the municipality. The investigation was conducted and it was reported that a municipal employee was cashing cheques on behalf of other employees. The outcome of the report was that one municipal employee was found guilty of irregularly cashing a cheque of R400.

Auditor - General

East London

29 November 2010



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence