

**AUDITOR'S REPORT OF THE AUDITOR-GENERAL TO THE KWAZULU-NATAL
PROVINCIAL LEGISLATURE AND THE COUNCIL ON UMKHANYAKUDE DISTRICT
MUNICIPALITY**

REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying consolidated financial statements of the uMkhanyakude District Municipality, which comprise the consolidated and separate statement of financial position as at 30 June 2010, the consolidated and separate statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information, as set out on pages xx to xx.

Accounting officer's responsibility for the consolidated financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and in the manner required by the Local Government: Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2010 (Act No. 1 of 2010) (DoRA). 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), section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and section 126(3) of the MFMA, my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with International Standards on Auditing and *General Notice 1570 of 2009* issued in *Government Gazette 32758 of 27 November 2009*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance that 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. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Basis for qualified opinion**Electricity sales**

7. The municipality could not provide sufficient appropriate audit evidence to support a journal entry processed on electricity sales amounting to R1 909 942,83. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that all electricity sales had been properly recorded. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the accuracy and occurrence of the electricity sales.

Accumulated surplus

8. The municipality could not provide sufficient appropriate audit evidence to support prior years' expenses that affected the accumulated surplus of R3 225 906. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that the prior years' expenses of R3 225 906 had been properly recorded. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness and valuation of the amount disclosed as the accumulated surplus.
9. The municipality could not provide sufficient appropriate evidence to support automatic transfers incorrectly processed on the statement of changes in net assets totalling R1 455 906. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance on these automatic transfers. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the completeness and valuation of the amount disclosed as the accumulated surplus.

Qualified opinion

10. In my opinion, except for the effects of the matters described in the basis for qualified opinion paragraphs, these financial statements present fairly, in all material respects, the consolidated and separate financial position of the uMkhanyakude District Municipality as at 30 June 2010, and its consolidated and separate financial performance and its consolidated and separate cash flows for the year then ended, in accordance with the SA Standards of GRAP and in the manner required by the MFMA and DoRA.

Emphasis of matters

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

Restatement of corresponding figures

12. As disclosed in note 33 to the financial statements, corresponding figures have been restated due to prior period errors.

Matters important to the users of the financial statements**Unauthorised expenditure**

13. As disclosed in note 37.1 to the consolidated financial statements, the municipality incurred unauthorised expenditure of R48,646 million (2009: R55,815 million) as a result of overexpenditure on the approved budget.

Fruitless and wasteful expenditure

14. As disclosed in note 37.2 to the consolidated financial statements, the municipality incurred fruitless and wasteful expenditure of R858 934 (2009: R206 944) as a result of interest and penalties on late payments.

Irregular expenditure

15. As disclosed in note 37.3 to the consolidated financial statements, the municipality incurred irregular expenditure by deviating from the supply chain management process in procuring goods and services amounting to R1,476 million as well as expenditure incurred as a result of contracts not being signed in 2008-09 and expenditure incurred on consultant fees for compiling an annual report without council approval (2009: R34,017 million).

Going concern

16. Although the municipality prepared financial statements on a going concern basis, note 33 to the financial statements reflect indicators that financial sustainability is under threat, as the municipality incurred a net loss during the year and the current liabilities exceeded the current assets. Management has adopted a plan of action with clear targets to ensure that the municipality continues to operate as a going concern for the foreseeable future.

Material losses

17. As disclosed in note 38 to the financial statements, the municipality incurred significant water distribution losses of 69%, amounting to R18,313 million (6 655 622 kilolitres). The municipality also incurred electricity distribution losses of approximately 72%, amounting to R2,962 million (6 978 266 kilowatts).

Additional matter

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

Unaudited supplementary schedules

19. 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

20. 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 MFMA and the Local Government: Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA), and financial management (internal control).

Predetermined objectives

21. Material findings on the report on predetermined objectives, as set out on pages xx to xx, are reported below.

Usefulness of reported performance information

22. 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:

23. There was a lack of consistency between the allocation of performance measures and targets between the integrated development plan, the service delivery and budget implementation plan and the annual performance report.
24. Performance targets were not measurable.

Reliability of reported performance information

25. 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:** Have amounts, numbers and other data relating to reported actual performance been recorded and reported appropriately?
- **Completeness:** Have all actual results and events that should have been recorded been included in the reported performance information?

The following audit findings relate to the above criteria:

Presentation of reported performance information

26. The annual performance report was not complete, as it did not include the performance of the municipality and each of its service providers; a comparison of the performance with targets set for and performances in the previous financial year; and measures taken to improve performance.
27. The integrated development plan did not reflect input and outcome performance indicators for the key performance indicators.

Compliance with laws and regulations

28. Included below are findings related to material non-compliance with the MFMA and the MSA.

Local Government: Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003)

29. Contrary to the requirements of section 32(4) of the MFMA, the accounting officer did not promptly inform the mayor, the MEC for local government in the province and the auditor-general, in writing, of any unauthorised, irregular or fruitless and wasteful expenditure incurred by the municipality.
30. Contrary to the requirements of sections 126(1)(a) and 126(1)(b) of the MFMA, the accounting officer of the municipality did not prepare the annual financial statements of the municipality within two months after the end of the financial year to which those statements relate and submit the statements to the auditor-general for auditing.
31. Contrary to the requirements of section 122(2) of the MFMA, the annual consolidated financial statements were not submitted to the auditor-general for auditing within three months after the end of the financial year.
32. Contrary to the requirement of section 87(1) of the MFMA, the municipal entity did not submit a proposed budget to its parent municipality within the required time frame.
33. Contrary to the requirement of section 86(1) of the MFMA, the municipal entity opened a new bank account but did not submit the details of the account to the parent municipality.
34. Contrary to the requirement of section 95(c)(1) of the MFMA, the municipal entity did not have a risk assessment strategy that included a fraud prevention plan.
35. Contrary to the requirement of section 166(4)(b) of the MFMA, the municipal entity's audit committee only met twice in the financial year instead of four times.
36. Contrary to the requirement of section 99(2)(b) of the MFMA, the municipal entity did not settle invoices totalling R2,37 million within 30 days of receipt thereof.
37. Contrary to the requirements of sections 97(1) and 99(2)(d) of the MFMA, the municipal entity did not have or did not maintain effective, efficient and transparent systems of internal control, as required by legislation, for debtors, revenue, creditors and payments.

Local Government: Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000)

38. Contrary to the requirement of section 93 of the MSA, the business plan between the municipal entity and the municipality was not signed.
39. Contrary to the requirements of section 46(1) of the MSA, the annual performance report and internal management reports did not accurately reflect the progress achieved for all of the targets set for the year. There was also inconsistency in reporting on municipal infrastructure grant projects.

40. Contrary to the requirements of section 72(1) of the MSA, there was no evidence to confirm that the accounting officer had assessed the performance of the municipality during the first half of the financial year.
41. Contrary to the requirements of section 76(b)(i) of the MSA, the municipality did not sign the service delivery agreement with the municipal entity.

INTERNAL CONTROL

42. 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.
43. The matters reported below are limited to the findings on the report on predetermined objectives and the findings on compliance with laws and regulations.

Leadership

44. The accounting officer did not exercise oversight responsibility over reporting, compliance with laws and regulations as well as internal control.

Financial and performance management

45. Pertinent information was not identified and captured in a form and time frame to support financial and performance reporting. The financial statements and performance information were subject to material adjustments resulting from the audit.
46. The annual financial statements and the report on predetermined objectives were not submitted for auditing as per the legislated deadlines.
47. The requested information was not supplied timeously, as record management was not effective.

Governance

48. A fraud prevention plan was not documented and used as per the requirements of applicable legislation.
49. The audit committee did not fulfil its responsibilities as set out in legislation.
50. The implementation of internal and external audit recommendations was not monitored.

OTHER REPORT**Investigation**

51. The chief financial officer is currently under investigation.

Auditor-General

Pietermaritzburg

15 March 2011



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence



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Herewith attached audit report as per your request.

Regards

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Coast