

REPORT OF THE AUDITOR-GENERAL TO THE KWAZULU-NATAL PROVINCIAL LEGISLATURE AND THE COUNCIL ON UTHUKELA DISTRICT MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the financial statements of the Uthukela District Municipality, which comprise the statement of financial position as at 30 June 2012, the statements of financial performance, changes in net assets and cash flows 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 the financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of 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, 2011 (Act No. 6 of 2011) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the *General Notice* issued in terms thereof and International Standards on Auditing. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer of opinion

Fruitless and wasteful expenditure

4. During the audit, fruitless and wasteful expenditure totalling R2,150 million was discovered, relating to penalty and interest charges incurred for the late payment of suppliers, as disclosed in note 44 to the financial statements. In this regard, I was unable to confirm the completeness of this subsequently disclosed expenditure, as management did not go back and examine the entire population to determine whether any further fruitless and wasteful expenditure was incurred by the municipality and whether section 125(2)(d) of the MFMA was fully complied with.

Irregular expenditure

5. During the audit, irregular expenditure totalling R14,606 million was discovered, relating to payments made to suppliers, in contravention of supply chain management requirements, as disclosed in note 45 to the financial statements. In this regard, I was unable to confirm the completeness of this subsequently disclosed expenditure, as management did not go back and examine the entire population to determine whether any further irregular expenditure was incurred by the municipality and whether section 125(2)(d) of the MFMA was fully complied with.

Property rates

6. Consumer debtors for municipal property rates and taxes was overstated by R281 554. This was as a consequence of a rateable area being transferred to another municipality in the district, which also raised property rates.

Service charges

7. Service charges income included income totalling R687 501, which was duplicated during a billing process for services, which were not rendered by the municipality. This amount has not been adjusted in the financial statements nor reversed on the municipality's financial management system.

Revenue

8. I was unable to obtain sufficient appropriate audit evidence as to the completeness and accuracy of journal adjustments totalling R2,414 million relating to interest income received. The municipality's records did not permit the application of alternative audit procedures.

Expenditure

9. I was unable to obtain sufficient appropriate audit evidence as to the completeness, accuracy, cut-off and classification of expenditure, as the municipality could not provide adequate explanations and/or supporting documentation for journal entries and/or expenditure vouchers amounting to R3,503 million. In addition, no clear audit trail exists to distinguish between expenditure vouchers and journal entries recorded in the general ledger. The municipality's records did not permit the application of alternative audit procedures.

Property, plant and equipment

10. The municipality did not maintain a proper and GRAP compliant fixed asset register. Consequently, I was unable to obtain sufficient appropriate audit evidence as to the completeness and valuation of assets totalling R712,293 million, as disclosed in note 3 to the financial statements.
11. I was unable to obtain sufficient appropriate evidence to confirm the existence of property, plant and equipment of R453,786 million selected for testing. In addition, the municipality's records did not permit the application of alternative audit procedures.
12. Unexplained and unsupported differences totalling R35,718 million regarding infrastructure asset additions existed between the asset register and financial statements. Furthermore, alternative audit procedures could not be performed to support the accuracy of the asset register, as the municipality did not review the residual values and useful lives of the assets at each reporting date in accordance with SA Standards of GRAP; GRAP 17, Property, plant and equipment. I have not determined the correct net carrying amount of assets as it was impracticable to do so.

Commitments

13. I was unable to obtain sufficient appropriate evidence of Council approval or confirm the validity of committed expenditure amounting to R299,438 million relating to property, plant and equipment, as disclosed in note 36 to the financial statements. In addition, the municipality's records did not permit the application of alternative audit procedures.

Trade and other receivables

14. The municipality could not provide sufficient appropriate evidence for debt impairment amounting to R16,391 million. Consequently, I was unable to determine the validity, accuracy and completeness of this amount, as disclosed in note 28 to the financial statements.
15. I was unable to obtain sufficient appropriate evidence to as the completeness, valuation, cut-off and classification of sundry debtors' suspense transactions and other third party arrangements, as the municipality could not provide adequate explanations or documentary evidence to support transactions amounting to R4,116 million. Furthermore, the municipality's records did not permit the application of alternative audit procedures.
16. In addition, I was unable to obtain sufficient appropriate evidence to support trade and other receivables from exchange transactions amounting to R3,242 million, as the municipality did not perform an assessment of recovery of debtors for the financial year.

Inventory

17. I was unable to obtain sufficient appropriate audit evidence to confirm the completeness, cut-off, classification and valuation of inventory. In this regard, the municipality could not provide adequate explanations or documentary evidence to support journal entries amounting to R4,117 million relating to inventory. Furthermore, the municipality's records did not permit the application of alternative audit procedures.

Accumulated surplus

18. I was unable to obtain sufficient appropriate audit evidence to support adjustments totalling R5,042 million to the accumulated surplus, described as a "Prior period error" and as disclosed in note 39 to the financial statements. Consequently, I was unable to determine whether any adjustments to the accumulated surplus figure were necessary.

Suspense accounts

19. Salary and other suspense accounts of R54,620 million were not supported by reconciliations, documentation and adequate explanations. I could not also determine the effect on the other account balances or classes of transactions as recorded in the financial statements.

Accumulation of misstatements

20. I was unable to obtain sufficient appropriate audit evidence to confirm or verify the following adjustments in preparation of the financial statements by alternative means:
 - Inventory of R226 865 and
 - Journal adjustments of R1,908 million affecting various classes of transactions and account balances, along with supporting documentation could not provided on request.

Provisions

21. I was unable to obtain sufficient and appropriate audit evidence to confirm the valuation of the provision for leave pay totalling R14,803 million, as disclosed in note 16 to the financial statements. In this regard, the municipality could not provide adequate explanations and/or documentation in support of the computations made to determine the provision.

Disclaimer of opinion

22. 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 the financial statements.

Emphasis of matters

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

Significant uncertainties

24. As disclosed in note 37 to the financial statements, the municipality is the defendant in seven lawsuits. The ultimate outcome of the matter cannot presently be determined and thus no provision for any liability that may arise has been made in the financial statements.

Restatement of corresponding figures

25. As disclosed in note xx to the financial statements, the corresponding figures at 30 June 2011 have been restated, as a result of errors identified and corrected during 2011-2012, in the financial statements of the Uthukela District Municipality at, and for the year ended, 30 June 2011.

Material losses

26. As disclosed in note 47 to the financial statements, the municipality incurred material water losses of R20,340 million (28,851 million kilolitres) during the year.

Material impairments

27. As disclosed in note 28 to the financial statements, the municipality provided for an impairment allowance amounting to R16,391 million on consumer and other debtors, as these debtors were considered doubtful.

Unauthorised expenditure

28. As disclosed in note 43 to the financial statements, the municipality incurred unauthorised expenditure of R62,147 million, due to overspending on certain votes within the approved budget.

Additional matter

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

Unaudited supplementary schedules

30. The supplementary information set out on pages xx to xx 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 thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

31. In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

32. The annual performance report included in the annual report was not presented in time for audit and consequently my findings below are limited to the procedures performed on the strategic planning and performance management documents.
33. The information was assessed to determine whether performance indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the *National Treasury Framework for managing programme performance information*.
34. The material findings are as follows:

Usefulness of information

35. The National Treasury *Framework for managing programme performance information (FMPPi)* requires that performance targets be specific in clearly identifying the nature and required level of performance. A total of 100% of the targets were not specific in clearly identifying the nature and the required level of performance. This was due to the fact that management was not complying with the requirements of the *FMPPi*.

Compliance with laws and regulations

36. I performed procedures to obtain evidence that the municipality has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the *General Notice* issued in terms of the PAA are as follows:

Strategic planning and performance management

37. The municipality's performance management system was not in line with the priorities, objectives, indicators and targets contained in its integrated development plan and did not clarify the roles and responsibilities of each role-player in the functioning of the system, as required by section 38 (a) of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) and regulation 7(2) of Municipal Planning and Performance Management Regulations of 24 August 2001.

Budget

38. Expenditure was incurred that was not budgeted for, contrary to section 15 of the MFMA.
39. The accounting officer did not assess the first half of the financial year performance of the municipality, as required by section 72(1)(a)(ii) and 88(1) of the MFMA.
40. Sufficient appropriate audit evidence could not be obtained confirming that monthly budget statements were submitted to the mayor and relevant provincial treasury, as required by section 71(1) of the MFMA.

Annual reports and performance reports

41. The 2010-2011 annual report was not tabled in the municipal council within seven months after the end of the financial year, as required by section 127(2) of the MFMA.
42. A written explanation was not submitted to council setting out the reasons for the delay in the tabling of the 2010-2011 annual report in the council, as required by section 127(3) of the MFMA.

43. The municipal council did not adopt an oversight report, containing comments on the annual report, within two months from the date on which the 2010-2011 annual report was tabled, as required by section 129(1) of the MFMA.
44. The accounting officer did not make public the council's oversight report on the 2010-2011 annual report within seven days of its adoption, as required by section 129(3) of the MFMA.
45. The annual performance report for the financial year under review was not prepared and was not included in the annual report, as required by section 46 of the MSA and section 121(3)(c) of the MFMA.

Annual financial statements,

46. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of non-current assets, current assets, liabilities, revenue, expenditure and other disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a disclaimer audit opinion

Audit committee

47. The audit committee did not substantially perform their functions for the year, as required by section 166 of the MFMA.

Internal audit

48. The internal audit unit did not report to the audit committee on the implementation of the internal audit plan, and internal audit reports were not sent to council on matters relating to internal audit, as required by section 165(2) of the MFMA.
49. The internal audit unit did not report to the audit committee on matters relating to compliance with all applicable legislation, such as DoRA, as required by section 165(2)(b) of the MFMA.

Expenditure management

50. Sufficient appropriate audit evidence could not be obtained that money owing by the municipality had always been paid within 30 days of receiving an invoice or statement, as required by section 65(2)(e) of the MFMA.
51. The accounting officer did not take effective steps to prevent unauthorised, irregular as well as fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.
52. Unauthorised, irregular as well as fruitless and wasteful expenditure was not recovered from the liable persons, as required by section 32(2) of the MFMA.
53. Sufficient appropriate audit evidence could not be obtained confirming that the accounting officer reported all cases of alleged irregular expenditure that constituted a criminal offence, theft and fraud that occurred in the municipality or losses suffered as a result of criminal conduct to the South African Police Service, as required by section 32(6) of the MFMA.

Revenue management

54. An adequate credit control and debt collection policy was not implemented, as required by section 96(b) of the MSA and section 62(1)(f)(iii) of the MFMA.
55. An adequate management, accounting and information system, which recognises accounts for revenue when it is earned, accounts for debtors and accounts for receipts of revenue, was not in place, as required by section 64(2)(e) of the MFMA.

Asset and liability management

56. An adequate management, accounting and information system which accounts for assets and liabilities was not in place, as required by section 63(2)(a) of the MFMA.
57. An effective system of internal control for assets (including an asset register) was not in place, as required by section 63(2)(c) of the MFMA.
58. Assets were disposed without the approval of the council, as required by section 14(2)(a) of the MFMA and regulation 5 of Municipal Asset Transfer Regulations of 22 August 2008.

Internal control

59. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for the disclaimer of opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

60. Management has failed to adopt an appropriate tone at the top to ensure that supervision, review and monitoring of the municipality's processes were undertaken, so as to ensure that controls were implemented and functioning effectively and efficiently and consistently throughout the year under review.

Financial and performance management

61. Systems and controls were not designed in a manner to prevent, detect and address risks that impact on financial and compliance reporting. The accounting officer did not ensure that regular, accurate and complete financial reports were prepared, which were supported and evidenced by reliable information. In addition, compliance with applicable laws and regulations was not monitored on a monthly basis, resulting in reportable non-compliance. In addition, material corrections to financial statements were required, as a result of errors identified by audit. The area of performance against predetermined objectives requires urgent attention and capacity building.

Governance

62. The municipality did not have a functioning audit committee to identify internal control deficiencies and recommend corrective action as well as perform its oversight function. In addition, the internal audit did not completely perform its functions as required.

OTHER REPORTS

Investigations in progress

63. An investigation is currently in progress into allegations of financial misconduct and maladministration against the former municipal manager.
64. The provincial government instituted a section 106 (of the MSA) investigation at the district municipality.

Auditor-General

Pietermaritzburg

30 November 2012



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence