

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

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the uThukela District Municipality set out on pages ... to ..., which comprise, the statement of financial position as at 30 June 2014, the statement of financial performance, statement of changes in net assets, the cash flow statement and the statement of comparison of budget information with actual information for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

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, 2013 (Act No. 2 of 2013) (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 my audit. I conducted my 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. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. 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 municipality'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 municipality'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.
5. 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

Operating expenditure

6. I was unable to obtain sufficient appropriate audit evidence that management had properly accounted for general expenses for the current year due to the breakdown in controls over the management of documentation at the municipality. I was unable to confirm general expenses by alternative means. Consequently, I was unable to determine whether any adjustment to general expenses stated at R97,89 million (2013: R75,09 million) in note 25 to the financial statements was necessary.
7. The municipality did not fully recognise bulk purchases stated at R7,23 million in note 36 to the financial statements, in accordance with GRAP 1 *Presentation of financial statements*. The bulk purchases and revenue from service charges and water losses revealed that there was no correlation between these amounts to justify the reasonability of bulk purchases. I was not able to determine the full extent of the understatement of bulk purchases and payables from exchange transactions, as it was impracticable to do so.

Receivables from exchange transactions

8. I was unable to obtain sufficient appropriate audit evidence to support sundry debtors for the current year, due to the breakdown in controls over the management of documentation at the municipality. I was unable to confirm the sundry debtors by alternative means. Consequently, I was unable to determine whether any adjustment to receivables from exchange transactions stated at R5,60 million (2013: R6,18 million) in note 8 to the financial statements was necessary.

Accruals

9. I was unable to obtain sufficient appropriate audit evidence regarding leave pay accrual in the current year, due to the breakdown in controls over the management of leave records. I was unable to confirm the leave pay accrual by alternative means. Consequently, I was unable to determine whether any adjustment to leave pay accrual stated at R11,71 million (2013: R13,15 million) in note 19 to the financial statements was necessary.

Commitments

10. I was unable to obtain sufficient appropriate audit evidence regarding commitments in the current year, due to the breakdown in controls over the management of records. I was unable to confirm the commitments by alternative means. Consequently, I was unable to determine whether any adjustment to commitments stated at R549,37 million (2013: R409,82 million) in note 38 to the financial statements was necessary.

Irregular expenditure

11. The municipality made payments in contravention of the supply chain management requirements that were not included in irregular expenditure stated at R83,63 million (2013: R40,83 million) in note 45 to the financial statements. I was not able to determine the full extent of the understatement of irregular expenditure, as it was impracticable to do so.

Water losses

12. I was unable to obtain sufficient appropriate audit evidence regarding water losses, as the municipality did not implement adequate processes and procedures for the management and monitoring of water extraction. I was unable to confirm the water losses by alternative means. Consequently, I was unable to determine whether any adjustment to water losses stated at R111,41 million (2013: R19,50 million) in note 47 to the financial statements was necessary.

Comparative amounts

13. During 2013, I was unable to obtain sufficient appropriate audit evidence for the revenue from service charges, interest received, employee costs, grant expenditure, inventory, consumer debtors, the cash flow statement and fruitless and wasteful expenditure due to the breakdown in controls over the management of documents at the municipality. I was unable to confirm these transactions, balances and disclosures by alternative means. Consequently, I was unable to determine whether any adjustments in the financial statements were necessary. My audit opinion on the financial statements for the period ended 31 March 2013 was modified accordingly. My opinion on the current period's financial statements is also modified because of the possible effects of these matters on the comparability of the current period's figures.

Qualified opinion

14. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the uThukela District Municipality as at 30 June 2014 and its financial performance and cash flows for the year then ended, in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

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

Material losses and impairments

16. As disclosed in note 3 to the financial statements, the municipality had written-off property, plant and equipment totalling R12,52 million at 30 June 2014, as they could not be identified during the verification process.
17. As disclosed in note 10 to the financial statements, the municipality raised a provision for bad debt impairment amounting to R441,10 million (2013: R481,69 million) on consumer debts as the recoverability of these amounts are was doubtful.

Restatement of corresponding figures

18. As disclosed in note 40 to the financial statements, the corresponding figures for property, plant and equipment and accumulated surplus for 30 June 2013 have been restated as a result of errors discovered during 30 June 2014 in the financial statements of the uThukela District Municipality at, and for the year ended 30 June 2013.

Additional matters

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

Unaudited supplementary information

20. 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 this information and, accordingly, I do not express an opinion thereon.

Unaudited disclosure notes

21. In terms of section 125(2) (e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

22. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings on the reported performance information against predetermined objectives for selected development priority presented in the annual performance report, non-compliance with legislation as well as internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

23. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development priority presented in the annual performance report of the municipality for the year ended 30 June 2014:

- Development priority: Basic service delivery on pages x to x

24. I evaluated the reported performance information against the overall criteria of usefulness and reliability.

25. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned development priority. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).

26. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.

27. The material findings in respect of the selected development priority are as follows:

Basic service delivery

Usefulness of reported performance information

Consistency of objectives, indicators and targets

28. Section 41(c) of the Local Government: Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) requires the integrated development plan to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 50% of the reported objectives, 78% of the reported indicators and 74% of the reported targets were not consistent with those in the integrated development plan. This was due to inadequate reviews of the performance report as a result of the performance manager vacancy.

Measurability of indicators

Indicators not well defined

29. The FMPPI requires that performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 74% of the indicators were not well defined. This was due to inadequate reviews of the performance plan as a result of the performance manager vacancy.

Reliability of reported performance information

Validity, accuracy and completeness

30. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of the reported performance information. This was due to limitations placed on the scope of my work as the auditee could not provide sufficient appropriate evidence in support of the reported performance information. The auditee's records did not permit the application of alternative audit procedures.

Additional matter

31. I draw attention to the following matter:

Achievement of planned targets

32. Refer to the annual performance report on pages x to x for information on the achievement of the planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information for the selected development priority reported in paragraphs 28 to 29 of this report.

Compliance with legislation

33. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other

related matters. My findings on material non-compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Strategic planning and performance management

34. The adopted integrated development plan (IDP) did not reflect and identify a financial plan and the key performance indicators and targets, as required by sections 26 and 41 of the MSA, as well as Municipal planning and performance management (MPPM) regulation 2(1) (c).
35. The municipality did not establish mechanisms to monitor and review its performance management system, as required by section 40 of the MSA.
36. Key performance indicators, including input, output and outcome indicators, in respect of each of the development priorities were not set out in the IDP, as required by section 41(1) (a) of the MSA and the MPPM regulation 1 and 9(1) (a).
37. Measurable performance targets for the financial year with regard to each of the development priorities and key performance indicators were not set in the IDP, as required by section 41(1) (b) of the MSA and the MPPM regulations 12(1) and 12(2) (e).
38. The annual performance report for the year under review did not include the performance of the municipality and each external service provider, a comparison with the previous financial year and measures taken to improve performance as required by section 46 (1)(a), (b) and (c) of the MSA.
39. The performance management system and related controls were not in place as it did not describe and represent the processes of performance planning, monitoring, measurement, review, reporting and improvement and how it is conducted, organised and managed as required by sections 38 of the MSA and regulation 7 of the MPPM regulations.

Budgets

40. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 87(8) of the MFMA.

Financial statements

41. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets, liabilities expenditure and 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 qualified audit opinion.

Procurement and contract management

42. Sufficient appropriate audit evidence could not be obtained that goods and services of a transaction value above R200 000 were procured by means of inviting competitive bids and that deviations approved by the accounting officer were only if it was impractical to invite competitive bids, as required by SCM regulation 19(a) and 36(1).

43. Sufficient appropriate audit evidence could not be obtained that goods and services with a transaction value of below R200 000 were procured by means of obtaining the required price quotations, as required by SCM regulation 17(a) and (c).
44. Sufficient appropriate audit evidence could not be obtained that contracts were only extended or modified after tabling the reasons for the proposed amendment in the council of the municipality, as required by section 116(3) of the MFMA.
45. Construction contracts were awarded to contractors that did not qualify for the contract, in accordance with section 18(1) of the Construction Industry Development Board Act, 2000 (Act no. 38 of 2000) (CIDB) and CIDB regulations 17 and 25(7A).

Expenditure management

46. Sufficient appropriate audit evidence could not be obtained that money owed by the municipality had always been paid within 30 days, as required by section 65(2) (e) of the MFMA.
47. Sufficient appropriate audit evidence could not be obtained that payments/ withdrawals from the municipality's bank account were approved by the accounting officer, the chief financial officer or a properly authorised official, as required by section 11(1) of the MFMA.
48. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1) (d) of the MFMA.

Consequence management

49. Unauthorised, irregular and fruitless and wasteful expenditure incurred by the municipality were not investigated to determine if any person is liable for the expenditure, as required by section 32(2) (a) (ii) of the MFMA

Internal control

50. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for qualified opinion, the findings on the annual performance report and the findings on non-compliance with legislation included in this report.

Leadership

51. Significant deficiencies were noted in the communication and consistent implementation of policies and procedures and related internal controls as well as the lack of monitoring and oversight, to enable and support understanding and execution of internal control objectives, processes and responsibilities with respect to performance management, procurement and contract management, asset management, expenditure management, liability management and conditional grant management.

Financial and performance management

52. Management have failed to implement a proper record keeping system to ensure complete, relevant and accurate information is accessible and available to support performance management, procurement and contract management, asset management, expenditure management, liability management and conditional grant management.

Governance

53. Notwithstanding deficiencies identified by the risk management processes, internal audit and audit committee in the municipal processes, management failed to timeously implement recommendations made by the governance structures to ensure deficiencies were corrected and to enable credible and reliable financial and performance reporting.

OTHER REPORTS

Investigations

54. Management performed an investigation which covered a period from 1 March 2014 to 28 February 2014. The investigation was based on an allegation of possible misappropriation of the municipality's assets. The investigation is completed with 13 employees being dismissed and one employee being handed a final warning. Twelve suspended employees are currently awaiting the outcomes of the hearing.

Pietermaritzburg

28 November 2014



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence