

Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on Kou-Kamma Local Municipality

Report on the financial statements

Introduction

1. I audited the financial statements of the Kou-Kamma Local Municipality set out on pages ... to ... , which comprise the statement of financial position as at 30 June 2016, the statement of financial performance, statement of changes in equity, cash flow statement and statement of comparison of budget information with actual information for the year then ended, as well as 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 these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of Grap) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2015 (Act No. 1 of 2015) (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 these financial statements based on my audit. 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 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 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.

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

Opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Kou-Kamma Municipality as at 30 June 2016 and its financial performance and cash flows for the year then ended, in accordance with applicable financial reporting framework and the requirements of the MFMA and DoRA.

Emphasis of matters

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

Irregular expenditure

8. Irregular expenditure of R57,9 million (2015: R57,5 million) has accumulated over the last 4 years and has not been recovered, written off or condoned was disclosed in note 34.2 to the financial statements. Irregular expenditure of R0,4 million (2015: R7,6 million) incurred during the year under review was included in the amount disclosed.

Material impairments

9. As disclosed in note 3 to the financial statements, an amount of R51,7 million (2015: R34,7 million) in respect of receivables from exchange transactions has been impaired.
10. As disclosed in note 4 to the financial statements, an amount of R13,2 million (2015: R11,2 million) in respect of receivables from non-exchange transactions has been impaired.

Material losses

11. As disclosed in note 36 to the financial statements, the municipality incurred material water losses of R15,5 million (2015: R6,2 million).

Going concern

12. The municipality's current liabilities exceeded its current assets. This situation, along with other matters as disclosed in note 45, indicates that the municipality may encounter difficulty realising its assets and discharging its liabilities during the normal course of business.

Restatement of corresponding figures

13. As disclosed in note 35 to the financial statements, the corresponding figures for 30 June 2015 have been restated as a result of an errors discovered during the year ended 30 June 2016.

Additional matter

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

Unaudited disclosure notes

15. 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.

Unaudited supplementary information

16. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. We have not audited these schedules and, accordingly, we do not express an opinion thereon.

Report on other legal and regulatory requirements

17. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report findings on the reported performance information against predetermined objectives of selected development priorities presented in the annual performance report, compliance with legislation and 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

18. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information of the following selected key performance area (KPA) in the annual performance report of the municipality for the year ended 30 June 2016:

KPA 2 – basic service delivery and infrastructure investment, on pages x to x

19. 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 priorities. 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).

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

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

KPA 2: basic service delivery and infrastructure investment

Usefulness of reported performance information

22. Performance indicator should be clearly defined so that data can be collected consistently and is easy to understand and use, as required by the FMPPI. A significant amount of indicators were not well defined.
23. The processes and systems that produced the indicator should be verifiable, as required by the FMPPI. A significant amount of indicators were not verifiable.
24. The above were due to management did not adhere to the requirements of the FMPPI due to a lack of proper systems and processes.

Reliability of reported performance information

25. 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. For significant targets the performance information was not valid, accurate and complete when compared to the source information or evidence provided. This was due to a lack of standard operating procedures and documented system descriptions for the accurate recording of actual achievements and technical indicator descriptions for the accurate measurement, recording monitoring of the completeness of source documentation in support of actual achievements.

Additional matters

26. I draw attention to the following matters:

Achievement of planned targets

27. Refer to the annual performance report on pages x to x and 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 in paragraphs 26 to 28 of this report.

Unaudited supplementary information

28. The supplementary information set out on pages x to x does not form part of the annual performance report and is presented as additional information. I have not audited these schedules and, accordingly, I do not report on them.

Compliance with legislation

29. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My material findings on compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Annual financial statements

30. 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 expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.

Expenditure management

31. Reasonable steps were not taken to prevent irregular and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.
32. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.

Consequence management

33. Irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person was liable for the expenditure, as required by section 32(2)(b) of the MFMA.

Liability management

34. Short-term debt was incurred without a resolution of the municipal council approving the debt agreement, in contravention of section 45(2)(a) of the MFMA.

Internal control

35. 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 the opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

Leadership

36. The leadership did not implement all the disciplines necessary to enable effective oversight that promotes efficiency and effectiveness in service delivery reporting and compliance with legislation. This was due to leadership not ensuring that there were adequately skilled resources and an effective performance management system to monitor, oversee and hold all personnel accountable for their performance throughout the year.

Financial and performance management

37. Due to inadequate review processes, financial statements submitted for audit contained material misstatements which were subsequently corrected. The municipality did not have an effective records management system to reliably account for the disclosed performance reporting. Furthermore, they did not ensure that compliance with legislation was monitored throughout the financial year.

Governance

38. A risk register was in place; however, the risk assessment which took place during the year was inadequate and risks identified in this assessment were not appropriately mitigated within the control environment. Due to these limitations the municipality could not be sufficiently guarded against risks relating to internal controls and performance management.
39. While the internal audit unit and the audit committee fulfilled their responsibilities by making the appropriate recommendations, management did not adequately implement these recommendations.

Auditor-General

East London

30 November 2016



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence