

Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on the King Sabata Dalindyebo Local Municipality

Report on the audit of the financial statements

Opinion

1. I have audited the financial statements of the King Sabata Dalindyebo Local Municipality set out on pages XX to XX, which comprise the statement of financial position as at 30 June 2017, and the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, the financial statements present fairly, in all material respects, the financial position of the King Sabata Dalindyebo Local Municipality as at 30 June 2017, and its financial performance and cash flows for the year then ended 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, 2013 (Act no. 56 of 2003) (MFMA) and the Division of Revenue Act, 2016 (Act no. 3 of 2016) (DORA).

Basis for Opinion

3. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of this report.
4. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' Code of ethics for professional accountants (IESBA code) together with the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Financial sustainability

6. I draw attention to note 60 to the financial statements, which indicates that the municipality is experiencing financial difficulties in that current liabilities exceed current assets. As included in note 60, these events or conditions, along with the other matters as set forth in the same note, indicate that a material uncertainty exists that may cast significant doubt on the municipality's ability to continue to fund its operations.

Emphasis of matters

7. I draw attention to the matters below.

Significant uncertainty

8. As disclosed in note 45 to the financial statements, the municipality is the defendant in a number of lawsuits. The municipality is opposing the claims and the ultimate outcome of the matters cannot presently be determined and no provision has been made in the financial statements for any liabilities that may result.

Distribution Losses

9. As disclosed in note 50 to the financial statements, material losses to the amount of R19,1 million (2015-16: R35,8 million) were incurred as a result of distribution losses in the provision of electricity.

Impairment loss

10. As disclosed in the financial statements material debt impairments of R218,6 million (2015-16: R200,4 million) and R180,4 million (2015-16: R184,9 million) on receivables from exchange and non-exchange transactions were disclosed in note 4 and 5 respectively to the financial statements.

Irregular expenditure

11. Irregular expenditure of R1,1 billion that has accumulated over a number of years and that has not been recovered, written off or condoned is disclosed in note 49 to the financial statements. Irregular expenditure of R57 million (2015-16: R221,5 million) incurred during the current year is included in the amount disclosed. Furthermore, the municipality has disclosed in note 58 to the financial statements that it was impracticable to restate the irregular expenditure for the period ending 2012-13 and earlier.

Unauthorised expenditure

12. Unauthorised expenditure of R374,7 million that has accumulated over a number of years and that has not been recovered, written off or condoned is disclosed in note 47 to the financial statements. Unauthorised expenditure of R21 million incurred during the current year is included in the amount disclosed.

Fruitless and wasteful expenditure

13. Fruitless and wasteful expenditure of R360,9 million that has accumulated over a number of years and that has not been recovered, written off or condoned is disclosed in note 48 to the financial statements. Fruitless and wasteful expenditure of R12,2 million (2015-16: R5,3 million) incurred during the current year is included in the amount disclosed.

Restatement of corresponding figures

14. As disclosed in note 57 to the financial statements, the corresponding figures for 30 June 2016 have been restated as a result of errors discovered during the year ended 30 June 2017 in the financial statements of the municipality at, and for the year ended, 30 June 2016.

Responsibilities of the accounting officer for the preparation of the financial statements

15. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and 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.
16. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the accounting officer either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

17. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
18. A further description of my responsibilities for the audit of the financial statements is included in the annexure to the auditor's report.

Report on the audit of the annual performance report

Introduction and scope

19. 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 material findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
20. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
21. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2017:

Development priorities	Pages in annual performance report
Basic service delivery and infrastructure (Technical service and Human settlement)	XX – XX & XX – XX
Local economic development	XX - XX

22. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.

23. I have identified material findings on the usefulness and reliability of the reported performance information for the following development priorities:

Development priority: Basic service delivery and infrastructure

Changes to indicators and targets were not approved

24. The following indicators and targets in the technical services priority objective as reported were not consistent with the indicators and targets approved in the integrated development plan. This is not in line with the requirements of section 41 (c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA). These changes were made without the necessary approval as required by section 25(2) of the MSA.

Planned indicator	Reported indicator	Planned target	Reported target
Repairs and maintenance of 800 Street Lights and High Masts by June 2017	1000 streetlights and high mast lights repaired by June 2017	800 Repaired and maintained by June 2017	800 Repaired and maintained by June 2017
Construction of 2 Community Halls by June 2017	Construct 3 Community Halls by June 2017	2Community Halls constructed by June 2017	3 community halls
1200 households to be electrified in the rural areas by June 2017	Electrify 1500 households by June 2017	1200 electrical connections	1500 households electrified
Monitoring and implementation of the construction of self-service chalets in Lutshaba Nature Reserve conducted Working for the Parks by June 2017	Establish accommodation facilities by constructing self-service chalets in Lutshaba Nature Reserve Ward 12	Review IWMP by June 2017	Constructed self-service chalets in Lutshaba Nature Reserve by June 2017
Cleaning and repairing of 28 000 metres Storm water infrastructure in the Urban Areas by June 2017	Inspect and maintain 40 000 m of Storm water infrastructure in the Urban Areas by June 2017	28000 Cleaned and repaired by June 2017	40 000m
Repair and Maintenance of 22000 Square m urban roads by June 2017	Maintain and repair 50 000m ² of urban roads by June 2017	22000Square m repaired and maintained by June 2017	50000m ²
Refurbishment 30km overhead Low Voltage Network in CBD and surrounding areas by	Refurbish 21km of overhead line in Zamakalungisa and Vulindlela Heights by	Refurbished 30km of LV network by June 2017	Refurbishment complete

Planned indicator	Reported indicator	Planned target	Reported target
June 2017	March 2017		
Refurbishment of High Voltage Line between Unitra and Thornhill by June 2017	Refurbish 28km of 11kv overhead line from Thornhill to Waterfall by March 2017	Completion of designs from Thornhill to Unitra by June 2017	28km overhead line complete
350 households to be electrified in the municipal licensed area by June 2017	Not reported	350 household connected by June 2017	Not reported
70km of new roads constructed or rehabilitated using MIG funding by June 2017	Not reported	70km of new roads constructed or rehabilitated using MIG funding by June 2017	Not reported
Facilitate provision alternate energy supply by installation of Solar Heater Geysers by June	Not reported	Secure funding and implementation of solar heater geysers by June 2017	Not reported
Provide solar energy for 1000 household lighting by June 2017	Not reported	1000 households connected	Not reported
Replacement of 10 miniature substations and 100 kiosks in suburbs by June 2017	Not reported	Replace 10 minisubs and 100 kiosks by June 2017	Not reported
Indicator not planned	Construction of 6km of 66kv overhead lines by June 2017	Target not planned	Complete Construction Mbuqe and Sidwadwa
Indicator not planned	Refurbish 4km of cable network in CBD and Mthatha South by December 2016	Target not planned	4km of cable network refurbished
Indicator not planned	Refurbish 12km of 11kv overhead line in the Big 5 by January 2017	Target not planned	12km overhead line refurbished
Indicator not planned	Construct 50 Hawker stalls by June 2017	Target not planned	50 Hawker stalls Completed
Indicator not planned	Install fencing for 1 cemetery by June 2017	Target not planned	1 Cemetery fencing completed
Indicator not planned	Rehabilitation of a sports field by June 2017	Target not planned	1 Sports field under rehabilitation

Reported achievement did not agree with the evidence provided

25. The reported achievements for the following targets were misstated, as the evidence provided did not agree with the reported achievements. The system and processes implemented by the municipality to ensure accurate, valid and complete reporting of its actual performance against planned indicators and targets of basic service delivery and infrastructure priority objective were not effective. As a result, the reported achievement of 19 indicators and targets out of 21 are misstated.

Performance indicator	Planned target	Reported achievement	Audited Value
Technical services			
Refurbish 21km of overhead line in Zamakalungisa and Vulindlela Heights by March 2017	21kms	Not reported	21kms
Refurbish 12km of 11kv overhead line from Thornhill to Waterfall by March 2017	12km overhead line complete	Not reported	12kms
1000 streetlights and high mast lights repaired by June 2017	800 Repaired and maintained by June 2017	787	441 streets
Install 15 High Masts Lights by June 2017	15 high mast lights installed	Not reported	15 high mast
Electrify 1500 households by June 2017	1500 households electrified	910 connections	350
Inspect and maintain 40 000 m of Storm water infrastructure in the Urban Areas by June 2017	40 000m	51761m	39372.2m
Construction of 6km of 66kv overhead lines by June 2017	Complete Construction Mbuqe and Sidwadwa	Not reported	6 km
Refurbish 4km of cable network in CBD and Mthatha South by December 2016	4km of cable network refurbished	Not reported	4km
Construct 50 Hawker stalls by June 2017	50 Hawker stalls Completed	Not reported	50
Install fencing for 1 cemetery by June 2017	1 Cemetery fencing completed	Not reported	1
Rehabilitation of a sports field by June 2017	1 Sports field under rehabilitation	Not reported	1
Refurbish 28 km of 11kv overhead line from Thornhill to Waterfall by March 2017	28km overhead line complete	Not reported	28
Human settlement			
Construction of 234 houses in Maydene Farm Ext. Project- A by June 2017	234 houses by June 2017	Not reported	156
Surfacing of 2.6 km and construction of storm water drainage of Mgxaji road, stadium road, Hlaba road, Madikane road and Xhosana road under Ngangelizwe ISUP by June 2017	Fully surfaced roads and Construction of storm water drainage by June 2017	Not reported	2.6
Housing development for New Brighton township by June 2017	Approved township layout and general plan by June 2017	Not reported	1
Annual review of tariffs for various services by June 2017	Reviewed and approved tariffs by June 2017	Not reported	1

Performance indicator	Planned target	Reported achievement	Audited Value
To provide title deeds to Ngangelizwe, Khwezi, Hill Crest and New Brighton community by June 2017	190 Title Deeds issued by June 2017	Not reported	36
Approval of all submitted building plans for KSDM area of jurisdiction by June 2017	All circulated building plans approved by June 2017	Not reported	172
Acquire Qweqwe landfill site permit and water license and facilitate development of the landfill site by June 2017	Acquire landfill site licence & Water Use License by September 2017	Not reported	1

Local economic development

Performance indicators are not well defined and not verifiable

26. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of the following indicators. This was due to lack of technical indicator descriptions, proper performance management systems and processes and formal standard operating procedures that predetermined how the achievement would be measured, monitored and reported, as required by the FMPPI. I was unable to confirm that the reported achievement of 9 out of 11 indicators were reliable by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement of the following indicators:

Description	Number of indicators
Workers employed in designated sectors	3
Capacity building and support programmes	4
Upgrading, maintenance and facilitation of municipal libraries	1
Target youth activities	1
Total	9

Reported achievement did not agree with the evidence provided

27. The municipality did not have an adequate record keeping system to enable reliable reporting on achievement of the indicators listed below. Sufficient appropriate audit evidence could not be provided in some instances. In other cases, the evidence provided did not agree to the reported achievements, which resulted in misstatements of the reported achievements, as the evidence provided did not agree to the reported achievements. I was also unable to confirm the reported achievements by alternative means.

Performance indicator	Reported achievement
Number of workers employed: <ul style="list-style-type: none"> • Agriculture and forestry • Manufacturing • Trade and services 	<ul style="list-style-type: none"> • Not reported • 15 jobs created • Not reported
Capacity building and support programmes: <ul style="list-style-type: none"> • Conduct 4 capacity building programmes to informal traders by June 2017 • Facilitate the business support and 	<ul style="list-style-type: none"> • 3 programmes achieve 2 training and 1 WRSETA • 40 informal traders capacitated through

Performance indicator	Reported achievement
capacitate 360 informal traders by June 2017 <ul style="list-style-type: none"> Develop support programmes for informal traders by 16/17 Provide capacity building for 200 local enterprises and community members by June 2017 	equipment <ul style="list-style-type: none"> 1 Horrow Road Market Plan Development Ntozonke Market Banner 60 street kitchens procured 10 Furntech youth; 10 Innovator Youth; 40 unemployed SMMEs trained by CATH SETA; 40 Informal traders capacitated; 10 SMMEs capacity through Flea Market
Facilitate the upgrading and maintenance of ICT infrastructure, telecommunications and facilities in all municipal libraries by June 2017	Not Reported
Target youth specific activities and development programmes	2 youth workshops conducted

Number of EPWP work opportunities created

28. In addition to the above, the reported achievement of 200 EPWP work opportunities reported was misstated as the evidence provided indicated 128 and not 192 as reported.

Other matters

29. I draw attention to the matters below:

Achievement of planned targets

30. Refer to the annual performance report on pages x to x for information on the achievement of planned targets for the year and explanations provided for the under or overachievement of a number of targets.

Adjustment of material misstatements

31. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of Basic service delivery and Infrastructure and Local Economic. As management subsequently corrected only some of the misstatements, I reported material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are included in the basis for adverse conclusions paragraphs.

Report on audit of compliance with legislation

Introduction and scope

32. In accordance with the PAA and the general notice issued in terms thereof I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

33. The material findings in respect of the compliance criteria for the applicable subject matters are as follows:

Annual financial statements, performance and annual report

34. 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 disclosure items identified by the auditors in the submitted financial statements were subsequently corrected.

Strategic planning and performance monitoring

35. The performance management system and related controls were not maintained as it did not describe how the performance monitoring processes should be conducted and managed, as required by municipal planning and performance management regulation 7(1).
36. General key performance indicators are not included in the IDP and SDBIP as per the requirements with MSA sec. 43, Local Government: Municipal Planning and Performance Management Regulations (GNR. 796 of 24 August 2001) Reg 10(a).

Budgets

37. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R21 million, as disclosed in note 47 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by high litigation costs.

Expenditure management

38. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
39. Effective steps were not taken to prevent irregular expenditure amounting to R57 million as disclosed in note 49 to the annual financial statements, as required by section 62(1)(d) of the MFMA.
40. Effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R12,2 million, as disclosed in note 48 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA.

Consequence management

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

Asset Management

42. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Human Resource management and compensation

43. Appropriate systems and procedures to monitor, measure and evaluate performance of staff were not developed and adopted as required by section 67(1)(d) of the MSA.

Procurement and contract management

44. Awards were made to providers who were in the service of the municipality, in contravention of section 112(j) of the MFMA and SCM regulation 44. Furthermore the provider failed to declare that he or she was in the service of the municipality, as required by SCM regulation 13(c).
45. Awards were made to providers who were in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulation 44. Similar awards were identified in the previous year and no effective steps were taken to prevent or combat the abuse of the SCM process, as required by SCM regulation 38(1).
46. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e) the code of conduct for staff members issued in terms of the MSA.
47. Persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e) the code of conduct for staff members issued in terms of the MSA.

Other information

48. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes the audit committee's report.
49. The other information does not include the financial statements, the auditor's report thereon and those selected development priorities presented in the annual performance report that have been specifically reported on in the auditor's report.
50. My opinion and findings do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
51. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
52. I have not received the annual report. When I do receive this information, if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected I may have to re-issue my auditor's report as appropriate.

Internal control deficiencies

53. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on the annual performance report and the findings on compliance with legislation included in this report.
54. The lack of stability in critical positions during the financial period has contributed to leadership not providing sufficient oversight with regard to the implementation and monitoring of internal control, including of monitoring of debt and credit controls of the municipality.
55. There have been inadequate consequences for prior year supply chain management transgressions and was inappropriate evidence that leadership has followed up or investigated the transgressions of these officials which resulted in accumulated irregular expenditure of R1,1 billion disclosed in note 49 to the financial statements. The lack of appropriate action against officials who undermines a culture of accountability.
56. A valid, accurate and complete performance report was not prepared by a designated official as the municipality had the position vacant, therefore no official was responsible for collecting and collating the performance information. This resulted in a regression in the credibility of the performance report submitted for audit.
57. Action was not taken by the governance structures in the municipality during the year under review to ensure that risks relating to the monitoring and reporting of financial and performance information as well as the achievement of performance objectives were addressed. Furthermore the audit committee was not in place for the entire financial year which limited their ability to provide adequate assurance over the reports issued by internal audit.

AUDITOR-GENERAL

East London

30 November 2017



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence