

Report of the auditor-general to Eastern Cape Provincial Legislature and council of Mbashe Local Municipality

Report on the audit of the financial statements

Opinion

1. I have audited the financial statements of the Mbashe Local Municipality set out on pages ... to ..., which comprises the statement of financial position as at 30 June 2018, 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 Mbashe Local Municipality as at 30 June 2018, and its financial performance and cash flows for the year then ended in accordance with South African Standards of Generally Recognised Accounting Practice (SA standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2017 (Act No. 3 of 2017) (Dora).

Basis for the 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 auditor's 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) and 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.

Emphasis of matters

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

Restatement of corresponding figures

7. As disclosed in note 37 to the financial statements, the corresponding figures for 30 June 2017 have been restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2018.

Impairment loss – trade debtors

8. As disclosed in note 11 to the financial statements, material impairments of R21,2 million (2017: R17,8 million) were incurred as a result of a provision of impairment of irrecoverable trade and other receivables from exchange and non-exchange transactions.

Irregular expenditure

9. As disclosed in note 41 to the financial statements, the municipality incurred irregular expenditure of R137 million (2017: R134,3 million) as a result of non-compliance with procurement requirements.

Other matters

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

Unaudited disclosure notes

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

Responsibilities of accounting officer for the financial statements

12. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with 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.
13. 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 appropriate governance structure 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

14. 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 the 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 aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
15. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.

Introduction and scope

16. 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.
17. 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.
18. 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 programmes presented in the annual performance report of the municipality for the year ended 30 June 2018.

Programmes	Pages in the annual performance report
KPA 2: basic services and infrastructure development	x – x
KPA3: local economic development	x – x

19. 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.
20. The material findings in respect of the usefulness and reliability of KPA2: basic services and infrastructure development and reliability of KPA3: local economic development are as follows:

KPA 2 – basic services and infrastructure development

Reliability of reported performance

Various indicators

21. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of targets listed below. This was due to limitations placed on the scope of my work. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the achievement of the reported targets listed below as reported in the annual performance report.

Indicator	Performance target	Reported achievement	Audited value
SD1.5 Number of surface roads maintained	11km	11km	0
SD1.9 Number of households provided with solar energy	1000	2948	0
SD2.1 Number of households serviced	60124	60124	0
SD6.1 Number of informal settlements with full services	1	1	0

22. The reported achievement in the annual performance report did not agree to the supporting evidence provided for the indicators listed below. The supporting evidence provided indicated that the achievement of this indicator was as follows:

Indicator	Performance target	Reported achievement	Audited Value
SD1.1 Number of km of gravel roads constructed	30km	30km	24.6km
SD1.2 Number of km of gravel roads maintained	300km	315.1km	354.71km
SD1.4 Number of storm-water facilities upgraded	10	10	14
SD1.6 Number of square metres of paved side walks	10 000m ²	8 361.50m ²	942m ²
SD1.8 Number of households provided with grid electricity	560	808	964
SD1.12 Number of street lights maintained	610	669	2585
SD2.4 Number of roads safety features implemented	5	5	1

Usefulness

SD1.11 Number of street lights upgraded

Reported achievements not consistent with the planned and reported target

23. The reported achievement of 35 street poles planted for the indicator SD1.11 number of street lights upgraded is not consistent with the planned target for this indicator, which was 20 street lights upgraded.

Target is not specific

SD1.5 Number of surface roads maintained

24. The planned target of 11 kilometers of surface roads maintained for the indicator *SD 1.5* number of surface roads maintained is not specific in that it does not clearly identify the nature and required level of performance for the indicator.

SD1.7.2 installation of culverts and bridge approaches complete

25. The planned target of installation of culverts and bridge approaches complete for the indicator *SD 1.7.2* installation of culverts and bridge approaches complete is not specific in that it does not clearly identify the nature and required level of performance for the indicator.

KPA 3 – local economic development

Reliability of reported performance – various indicators

26. The reported achievement in the annual performance report did not agree to the supporting evidence provided for the indicators listed below. I was also unable to obtain sufficient appropriate audit evidence in some instances. The supporting evidence provided indicated that the achievements of these indicators were as follows:

Indicator	Performance target	Reported achievement	Audited value
LED 1.3 Number of village associations assisted with maize production inputs.	40	41	30
LED 3.1 Number of people employed through EPWP	1079	1500	1851
LED 5.2 Number of SMMEs supported	8	7	6

Other matters

27. I draw attention to the matters below.

Achievement of planned targets

28. Refer to the annual performance report on pages ... to ... for information on the achievement of 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 21 to 26 of this report.

Adjustment of material misstatements

29. We identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of KPA2: service delivery and infrastructure development and KPA3: local economic development. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

Report on the audit of compliance with legislation

Introduction and scope

30. 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.
31. The material findings on compliance with specific matters in key legislations are as follows:

Strategic planning and performance

32. The performance management system and related controls were not maintained or were inadequate as it did not describe how the performance planning, monitoring, measurement, review, reporting and improvement processes should be conducted and organised and managed, as required by municipal planning and performance management reg 7(1).

Annual Financial Statements and Annual Report

33. 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 assets, disclosure, expenditure and employee costs 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

34. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
35. Reasonable steps were not taken to prevent irregular expenditure of R136,5 million as disclosed in note 41 to the annual financial statements, as required by section 62(1)(d) of the MFMA.
36. Reasonable steps were not taken to prevent fruitless and wasteful expenditure of R190 530 as disclosed in note 40 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA.

Procurement and contract management

37. Competitive bids were adjudicated by a bid adjudication committee that was not composed in accordance with SCM regulation 29(2). Similar non-compliance was also reported in the prior year.

Consequence Management

38. All unauthorised expenditure amounting to R102,6 million incurred by the municipality in the previous years was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) of the MFMA.
39. All 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.

HR management

40. Job descriptions were not established for some posts in which appointments were made, as required by section 66(1)(b) of the MSA.

Other information

41. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes audit committee's report. The other information does not include the financial statements, the auditor's report and those selected development priorities presented in the annual performance report that have been specifically reported in the auditor's report.
42. Our opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and we do not express an audit opinion or any form of assurance conclusion thereon.
43. In connection with our audit, our 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 our knowledge obtained in the audit, or otherwise appears to be materially misstated.
44. We did not receive the other information prior to the date of this auditor's report. When we do receive and read this information, if we conclude that there is a material misstatement therein, we are 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, we may have to retract this auditor's report and re-issue an amended report as appropriate. However, if it is corrected this will not be necessary.

Internal control deficiencies

45. I considered internal control relevant to my audit of the financial statements, reported performance material and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. 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.

46. The leadership did not take full ownership of the general control environment and did not insist on daily disciplines to ensure efficiency and effectiveness in financial management, service delivery execution and compliance with laws and regulations. Consequently, the correct tone was not set to ensure that officials are held accountable for their actions through a consequence management programme.
47. In addition, the municipality did not fully implement and monitor the audit action plan and, as a result, numerous internal control deficiencies identified in the previous year recurred in the current year.
48. The municipality did not have an effective records management system in place to reliably account for the reporting on financial and performance information. In addition, there was no implementation of monthly controls over daily and monthly reconciliations, as well as inadequate review and monitoring of compliance with laws and regulations.
49. The lack of daily, weekly and monthly financial disciplines and monitoring throughout the financial year resulted in a large number of reconciliations, journals and corrections being performed after year-end. In addition, leadership did not ensure that the financial statements agreed to supporting documentation prior to its submission for audit.
50. The internal audit unit was not effective in its review of internal controls and compliance with laws and regulations. This was largely as a result of the lack of co-operation from management and capacity shortages, in terms of skills and resources in the unit.
51. The impaired functioning of the internal audit unit impacted the effectiveness of the audit committee.

Auditor - General

East London

30 November 2018



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

Annexure – Auditor-general’s responsibility for the audit¹

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected programmes and on the 's compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the financial statements as described in this auditor’s report, I also:
 - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control
 - obtain an understanding of internal control relevant to the audit 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 municipalities’ internal control
 - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by, which constitutes the accounting officer
 - conclude on the appropriateness of the accounting officer’s use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Mbashe Local Municipality’s ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor’s report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of this auditor’s report. However, future events or conditions may cause a municipality to cease continuing as a going concern
 - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation
 - obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group to express an opinion on the financial statements. I am responsible for the direction, supervision and performance of the group audit. I remain solely responsible for my audit opinion

Communication with those charged with governance

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may

reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.