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**AUDITOR - GENERAL  
SOUTH AFRICA**

# **Engcobo Local Municipality**

## **Audit Report**

For the year ended 30 June 2018

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

## Report on the audit of the financial statements

### Qualified opinion

1. I have audited the financial statements of the Engcobo Local Municipality set out on pages ... to... , which comprise, 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 the 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, except for the effects of the matters described in the basis for qualified opinion section of this auditor's report the financial statements present fairly, in all material respects, the financial position of the Engcobo Local Municipality as at 30 June 2018, 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, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2016 (Act No 3 of 2016) (DoRA).

### Basis for qualified opinion

#### Contracted services

3. I was unable to obtain sufficient appropriate audit evidence for Contracted services, as the journal processed to repairs and maintainance and work in progress accounts could not be substantiated by supporting documentation. I could not confirm that the journal was necessary by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to Contracted services stated at R13,492 million.

### Context for the opinion

4. 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.
5. 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.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

## **Emphasis of matters**

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

### **Irregular Expenditure**

8. As disclosed in note 47 to the financial statements, the municipality incurred irregular expenditure of R12,4 million (2017: R10,8 million), as it did not follow a proper tender process.

### **Impairment loss**

9. As disclosed in note 10 to the financial statements, debt impairment of R4,4 million (2017: R5,9 million) was made to receivables from non-exchange transactions.

### **Restatement of corresponding figures**

10. As disclosed in note 42 to the financial statements, the corresponding figures for 30 June 2017 have been restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2018.

### **Reclassification of corresponding figures**

11. As disclosed in note 43 of the financial statements, comparative figures have been reclassified to be in line with MSCOA requirements, this has resulted in reclassification of comparative figures for Contracted Services, Repairs and Maintenance and General Expenses.

## **Other matter**

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

### **Unaudited disclosures**

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

## **Responsibilities of accounting officer for the financial statements**

14. 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 the 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.

15. In preparing the financial statements, the accounting officer is responsible for assessing the Engcobo Local 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

16. My objectives are to obtain reasonable assurance about whether the financial statements 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.
17. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.

## Report on the audit of the annual performance report

### Introduction and scope

18. 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.
19. 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.
20. 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 2018:

Key Performance Areas	Pages in the annual performance report
KPA 3 – Basic Service Delivery	x – x
KPA 2 – Local Economic Development	x – x

21. 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.

22. The material findings in respect of the usefulness and reliability of the selected key performance areas priorities are as follows:

### KPA 3 Basic Service Delivery

23. I was unable to obtain sufficient appropriate audit evidence to support the reported achievement of the following targets. This was due to inadequate technical descriptions and proper performance management systems and processes that predetermined how the achievement would be measured, monitored and reported. I was unable to confirm the reported achievement of the indicators by alternative means. Consequently, I was unable to determine whether any adjustments were required to the achievements as reported in the annual performance report.

Indicator number	Indicator description	Achievement
TS 30	Number of kms of gravel roads bladed as per approved maintenance plan by June 2018	Not achieved, 34.85 km
TS 31	Number of kms of gravel roads fully maintained/processed as per approved maintenance plan by June 2018	Not achieved, 28.1kms completed
TS 27	% completion of construction of 200 Ngcobo Street Lights, Ward 11 by June 2018	Not Achieved, 142 Street lights have been completed instead of 200 (71% Completion)

24. I was unable to obtain sufficient appropriate audit evidence to support the measures taken to improve performance against target as reported in the annual performance report. This was due to limitations placed on the scope of my work. I was unable to confirm the reported measures taken by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported measures taken to improve performance.

Indicator number	Indicator description	Reasons for corrective/ Measurement Source
TS 30	Number of kms of gravel roads bladed as per approved maintenance plan by June 2018	The plant has got no enough capacity , the municipality will ensure that the plant is serviced timeously in the next financial year
TS 31	Number of kms of gravel roads fully maintained/processed as per approved maintenance plan by June 2018	The plant has got no enough capacity , the municipality will ensure that the plant is serviced timeously in the next financial year
TS 23	% completion of construction of Sports Facilities in Ward 1 and 2	The projected was affected by the stopping of Funds by MIG, Constant spending on MIG project, the project will be completed in the next financial year 18/19



## KPA 2 Local Economic Development

25. I was unable to obtain sufficient appropriate audit evidence for the reported achievements of the following indicators relating to this KPA. This was due to limitations placed on the scope of my work. I was unable to confirm the reported achievements by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements in the annual performance report of the indicators listed below:

Indicator number	Indicator description	Reported achievement
IPED 4	% completion of construction of 1 Feedlot in Sinqumeni ward 20 by June 2018	Not Achieved, There is about 35% work that has been done.
IPED 8	% completion of 2 Boreholes in Zabasa ward 19 by June 2018	Not Achieved, There were delays with water pumps and outsourced some of the work(80% Completed)

### Indicator: Number of inputs purchased for 10 SMMEs in Transido by June 2018 (IPED 17)

26. I was unable to obtain sufficient appropriate audit evidence that clearly defined the predetermined source information and method of collection to be used when measuring the actual achievement for the indicator as the performance measure is not defined so that data can be collected consistently as the method of counting is not clear between the number of SMME's or inputs.

### Other matters

27. I draw attention to the matters below.

### Achievement of planned targets

28. Refer to the annual performance report on pages x to x; x to x 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 23 to 26 of this report.

### Adjustment of material misstatements

29. 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 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:

#### **Annual Financial Statements and annual report**

32. 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 and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected, but the supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

33. The oversight report adopted by the council on the 2016/17 annual report was not made public, as required by section 129(3) of the MFMA.

#### **Strategic planning and performance management**

34. The SDBIP was revised during the year without approval of the council following approval of an adjustments budget, as required by section 54(1)(c) of the MFMA.

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

#### **Asset management**

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

#### **Procurement and Contract Management**

37. Contracts were awarded to bidders that did not score the highest points in the evaluation process, as required by section 2(1)(f) of Preferential Procurement Policy Framework Act and Preferential Procurement Regulations.

38. The contract performance and monitoring measures and methods were not sufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA.

#### **Other information**

39. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report and those selected key performance areas presented in the annual performance report that have been specifically reported in this auditor's report.

40. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.



41. 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 key performance areas presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
42. The other information I obtained prior to the date of this auditor's report is the draft annual report which includes mayor's foreword and municipal managers overview, and the audit committee report is expected to be made available to us after 30 November 2018.
43. If, based on the work I have performed on the other information that I obtained prior to the date of this auditor's report, I conclude that there is a material misstatement of this other information, I am required to report that fact. No material inconsistencies were identified.
44. When I do receive and read the audit committee report, 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 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 information 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 basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.
  - Leadership did not take full ownership of the general control environment and the daily disciplines to ensure efficiency and effectiveness in financial management, service delivery execution and compliance with legislation, hence material findings and deficiencies were identified in all the audits performed.
  - The municipality did not implement proper record keeping to ensure that accounting records are accurate, complete and supported by adequate supporting documentation, this is evidenced by material misstatements identified in the financial statements and annual performance report submitted for audit. In addition, compliance with legislation was not monitored adequately throughout the year, resulting in numerous material findings on compliance with legislation
  - Supporting documentation was not readily available for audit purposes as most request for information (RFI) were submitted after the three day turnaround time or after the closure of communication of audit findings (COAF), which resulted in delays in the audit process.

## Other reports

46. I draw attention to the following engagement conducted by various parties that had, or could have, an impact on the matters reported in the municipality's financial statements, reported performance information, compliance with applicable legislation and other related matters. This report did not form part of my opinion on the financial statements or my findings on the reported performance information or compliance with legislation.

## Pending investigations

47. With reference to note 40 to the financial statements, for the 2013/2014 financial year, the municipality discovered alleged fraud committed by municipal employees. The case was reported to the South African Police Services (SAPS) and the Hawks for investigation. The matter is currently ongoing at the high court. Based on legal advice the municipality is of the opinion that it can recover a portion of the lost funds.

*Auditor - General*

East London

30 November 2018



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## Annexure – Auditor-general’s responsibility for the audit

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 key development areas and on the Municipality’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 municipality’s internal control
  - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by 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 Engcobo 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 consolidated 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.