

# **King Sabata Dalindyebo 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 on the King Sabata Dalindyebo Local Municipality

## Report on the audit of the financial statements

### Qualified opinion

1. I have audited the financial statements of the King Sabata Dalindyebo 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 information with actual information 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 possible effects of the matter described in the basis for qualified opinion section of this report, the financial statements present fairly, in all material respects, the financial position of the King Sabata Dalindyebo 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 of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2017 (Act No. 3 of 2017) (Dora).

### Basis for qualified opinion

#### Inventory

3. I was unable to obtain sufficient appropriate audit evidence for inventories as the inventory listing provided did not agree to the amount disclosed in the financial statements. I was not able to confirm by alternative means which balance could be relied on. Consequently, I was unable to determine whether any adjustments to inventory of R15,3 million as disclosed in note 3 to the financial statements were necessary.

### 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.

## **Material uncertainty relating to financial sustainability**

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

## **Financial sustainability**

8. I draw attention to note 55 to the financial statements which indicates that the municipality is experiencing financial difficulties in that its current liabilities exceed its current assets. The events or conditions disclosed in note 55 together with other matters set forth in the same note indicate that material uncertainty exists that may cast significant doubt on the municipality's ability to continue to fund its existing level of operations.

## **Emphasis of matters**

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

## **Significant uncertainty**

10. As disclosed in note 42 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, however disclosure has been made in the financial statements for any liabilities that may result.

## **Impairment loss**

11. As disclosed in note 4 and 5 to the financial statements, cumulative debt impairments of R265,1 million (2016-17: R218,6 million) and R232,2 million (2016-17: R180,4 million) were made to receivables from exchange and non-exchange transactions respectively.

## **Irregular expenditure**

12. As disclosed in note 46 to the financial statements, the municipality has accumulated R889,5 million (2016-17: R1,06 billion) irregular expenditure that has not been recovered, written off or condoned. Irregular expenditure of R297 million (2016-17: R56,9) million incurred during the current year is included in the amount disclosed.

## **Unauthorised expenditure**

13. As disclosed in note 43 to the financial statements, the municipality has accumulated R473,7 million (2016-17: R374,7 million) unauthorised expenditure that has not been recovered, written off or condoned. Unauthorised expenditure of R98,9 million (2016-17: R21 million) incurred during the current year is included in the amount disclosed.

## **Fruitless and wasteful expenditure**

14. As disclosed in note 44 to the financial statements, the municipality incurred fruitless and wasteful expenditure of R17,5 million (2016-17: R12,2 million) during the current year.

## Restated corresponding figures

15. As disclosed in note 54 to the financial statements, the corresponding figures for 30 June 2017 were restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2018.

## Other matter

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

## Unaudited disclosure notes

17. 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 we do not express an opinion thereon.

## Responsibilities of the accounting officer for the financial statements

18. 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.

19. 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

20. 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.

21. 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

22. 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.

23. My procedures addressed 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.
24. 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 priority presented in the annual performance report of the municipality for the year ended 30 June 2018:

Development priorities	Pages in the annual performance report
Basic service delivery and infrastructure (Technical service and Human settlement)	xx
Local Economic Development	xx

25. 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.
26. The material findings in respect of the usefulness and reliability of the selected development priorities are as follows

**Development priority: Basic services and Infrastructure (Technical service and Human settlement)**

**Strategic objective was not consistent when compared with the planned strategic objective**

27. The strategic objective, approved in the service delivery and budget plan includes an objective relating to *Reduce Hazardous substances related fatalities (deaths) by 2022*. However, the objective was not reported in the annual performance report.

**Measures taken to improve performance not disclosed**

**Various indicators**

28. The measures taken to improve performance against the following targets were not included in the annual performance report.

Indicator	Target
Maintain and repair 50 000m <sup>2</sup> of urban roads by June 2018	50 000m <sup>2</sup> surface roads repaired and maintained
Maintain 800km of gravel roads by June 2018	800km of gravel roads maintained
Electrify 1 781 households by June 2018	1781 households electrified

### Comparison between performance of the year under review and previous year

29. A comparison between the planned and reported performance of the year under review and previous year was not included for any of the indicators in the annual performance report.

### Reliability

#### Various indicators

30. The municipality reported that it had achieved the planned targets for the indicators set out in the table below, however the reported achievements were not supported by the evidence provided. As a result, the reported achievements of the below indicators are misstated.

Performance indicator	Planned target	Reported achievement	Audited Value
<b>Technical services</b>			
Construction of 2 Community Halls by June 2018	2 Community Halls constructed by June 2018	Achieved	1 community hall
Refurbish 21km of overhead in Zamakulungisa and Vulindlela Heights by December 2018	Refurbishment complete	Achieved	14 km refurbished
Construction of 6 km of 66kv overhead lines by December 2018	Construction complete	Achieved	2,48 km completed
<b>Human Settlement and Community Services</b>			
No. of new urban households receiving refuse collection service	Increased refuse collection services by 16,000 rural and urban households by June 2018	Achieved	0
No of peri-urban areas cleaned by co-operatives	Mthatha West, Payne, Ngcwanguba, Vidgesville & Qweqwe	Achieved	0

Performance indicator	Planned target	Reported achievement	Audited Value
No. of job opportunities created – EPWP	Implement Working For The Coast Programme	Achieved	0
Kei Rail. Servicing of 537 sites	537 serviced sites	Achieved	Could not confirm actual amount serviced

## Development priority: Local economic development

### Usefulness

#### Measures taken to improve performance not disclosed

31. The measures taken to improve performance against the target for the indicator *Provide capacity building for 200 local enterprise and community members by 2017-18* were not included in the annual performance report.

#### Comparison between performance of the year under review and previous year

32. A comparison per the indicators below between the performance of the year under review and previous year was not included for any of the indicators in the annual performance report.

#### Various indicators

33. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of the 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 as reported in the annual performance report.

Indicator	Target
Create 500 EPWP work opportunities by June 2018.	500 job opportunities created by June 2018
Number of workers employed during 17/18 in the following sector: Agriculture (arable and grazing land) by June 2018 Woolclip - R130 000 Citrus Pendu Merchandised Forestry	400 jobs
Manufacturing (agro-processing) by LED projects	100 jobs in Manufacturing
Number of informal traders supported	Support/capacitate 360 traders

Indicator	Target
Develop support programmes for informal traders by 17/18	4 support programmes for informal traders
Provide capacity building for 200 local enterprise and community members by 17/18	200 local enterprises and community members

### Other matter

34. I draw attention to the matter below.

### Achievement of planned targets

35. Refer to the annual performance report on pages ... to ... for information on the achievement of planned targets for the year and explanations provided for the under/ over achievement of a significant number of targets. 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 32 of this report.

## Report on the audit of compliance with legislation

### Introduction and scope

36. 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.

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

### Conditional grants

38. Performance in respect of programmes funded by the Integrated National Electrification Programme (INEP) and Municipal Infrastructure Grant (MIG) was not evaluated, as required by section 12(5) of the DoRA.

### Consequence management

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

### Strategic Planning

40. 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).



41. The IDP did not include the key performance indicators and targets as required by section 26 (c) of the MSA and municipal planning and performance management regulation 2.

#### **Annual report and annual financial statements**

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

#### **Expenditure management**

43. Monies owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
44. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R98,9 million as disclosed in note 43 to the annual financial statements, as required by section 62(1)(d) of the MFMA.
45. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R17,5 million as disclosed in note 44 to the annual financial statements, as required by section 62(1)(d) of the MFMA.
46. Reasonable steps were not taken to prevent irregular expenditure amounting to R297,5 million as disclosed in note 45 to the annual financial statements, as required by section 62(1)(d) of the MFMA.

#### **Human resource management and compensation**

47. The municipality's systems and procedures to monitor, measure and evaluate staff performance were not developed and adopted, as required by section 67(1)(d) of the MSA.

#### **Asset Management**

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

#### **Procurement and contract management**

49. 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).
50. 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. Similar non-compliance was also reported in the prior year.
51. Competitive bids were adjudicated by a bid adjudication committee that was not composed in accordance with SCM regulation 29(2). This non-compliance was identified by management in the procurement processes for 24 contracts.

52. 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).

### Other information

53. 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. 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 this auditor's report.
54. 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.
55. 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.
56. If, based on the work I have performed, I conclude that there is a material misstatement in this other information, I am required to report that fact. I have nothing to report in this regard.

### Internal control deficiencies

57. 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.
- There was slow progress in the implementation of the audit intervention plan of the municipality to adequately address issues raised in the prior year. Material non-compliance issues have been identified due to a lack of management oversight over the compliance of the applicable laws and regulations and policies by the municipality.
  - There was an inadequate control environment at the municipality with ineffective daily and monthly processing and reconciliation of transactions in property, plant and equipment, as well as inventory and certain disclosure items. Misstatements existed in the submitted financial statements for items that were not identified by the municipality's system of internal control which were corrected during the audit process.

### Other report

58. I draw attention to the following engagement conducted by an external party 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.

### Investigation

59. Subsequent to year end, an investigation was commenced by the Special Investigation Unit (SIU) into a matter that arose in previous years, including costs incurred for the funeral of former president Nelson Mandela. This investigation is still in progress.

*Auditor-General*

Auditor-General

East London

30 November 2018



AUDITOR-GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*

## **Annexure – Auditor-general's responsibility for the audit**

60. 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 development priorities and on the municipality's compliance with respect to the selected subject matters.

### **Financial statements**

61. 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 King Sabata Dalindyebo 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

### **Communication with those charged with governance**

62. 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.

63. 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.