

Auditor-General of South Africa

Ugu District Municipality

Audit report 2017-18

Report of the auditor-general to the KwaZulu-Natal Provincial Legislature and the council on Ugu District Municipality

Report on the audit of the consolidated and separate financial statements

Adverse opinion

1. I have audited the consolidated and separate financial statements of the Ugu District Municipality set out on pages ... to ..., which comprises the consolidated and separate statement of financial position as at 30 June 2018, the consolidated and separate 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 consolidated and separate financial statements, including a summary of significant accounting policies.
2. In my opinion, because of the significance of the matters described in the basis for adverse opinion section of this auditor's report, the consolidated and separate financial statements do not present fairly, in all material respects, the financial position of the Ugu District Municipality as at 30 June 2018, and its financial performance and its 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 of South Africa, 2017 (Act No. 3 of 2017) (Dora).

Basis for adverse opinion

Property, plant and equipment

3. The municipality did not properly account for infrastructure assets in accordance with GRAP 17: *Property, plant and equipment* as the municipality did not maintain an effective system of internal control for assets. Consequently, property, plant and equipment stated at R3,99 billion (2016-17: R3,91 billion) in note 11 to the consolidated and separate financial statements is materially misstated. There was also a resultant impact on depreciation and impairment.

Revenue and receivables from exchange transactions

4. The municipality did not account for revenue from exchange transactions in accordance with GRAP 9, *Revenue from exchange transactions* due to inadequate internal controls in the billing and estimation. I was also unable to obtain sufficient appropriate audit evidence for adjustments to revenue and receivables from exchange transactions. I was unable to confirm these journals by alternative means. Consequently, I was unable to determine whether further adjustments were necessary to service charge revenue stated at R325,34 million (2016-2017: R314,58 million) in note 22 and the related receivables from exchange transactions stated at R114,66 million (2016-17: R85,46 million) in note 8 to the consolidated and separate financial statements. Additionally, there was a resultant impact on the surplus and the accumulated surplus.

Receivables from non-exchange transactions

5. The municipality recognised items that did not meet the definition of revenue in accordance with GRAP 23, *Revenue from non-exchange transactions*. Consequently, receivables from non-exchange transactions stated at R99,98 million (2016-17: R33,42 million) in note 6 to the consolidated and separate financial statements are overstated. In addition, the municipality did not consider the receivables from non-exchange transactions in the computation of the allowance for impairment of receivables. Additionally, there was a resultant impact on the surplus and the accumulated surplus.

Payables from exchange transactions

6. The payables from exchange transactions were not recognised in accordance with GRAP 104, *Financial instruments* as there were discrepancies identified in amounts disclosed in the consolidated and separate financial statements and the underlying records. Consequently, payables from exchange transactions stated at R178,50 million in note 15 to the consolidated and separate financial statements are overstated by an unknown amount.

Value added tax payable (VAT)

7. I was unable to obtain sufficient appropriate audit evidence for VAT payable disclosed in the statement of financial position as the municipality did not maintain accurate and complete records. I could not confirm the amounts by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to VAT stated at R18,28 million in note 17 to the consolidated and separate financial statements.

Commitments

8. I was unable to obtain sufficient appropriate audit evidence for commitments, as the municipality did not maintain accurate and complete records of the contractual information used to determine commitments. I could not confirm the amounts by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to commitments stated at R569,77 million (2016-17: R666,37 million) in note 43 to the consolidated and separate financial statements.

Irregular expenditure

9. The municipality did not have adequate systems and controls to ensure irregular expenditure incurred was recorded correctly. This resulted in irregular expenditure being misstated by an unknown amount. In addition, I was unable to obtain sufficient appropriate audit evidence for the amounts disclosed. I could not confirm the irregular expenditure by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to irregular expenditure stated at R132,53 million in note 52 to the consolidated and separate financial statements.

Water losses

10. I was unable to obtain sufficient appropriate audit evidence for water losses, as the municipality did not maintain sufficient appropriate audit evidence for the water stock levels. I could not confirm the amounts by alternative means. Consequently, I was unable to determine whether

any adjustment was necessary to water losses stated at R30,50 million in note 53 to the consolidated and separate financial statements.

Context for the opinion

11. 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 consolidated and separate financial statements section of this auditor's report.
12. 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.
13. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my adverse opinion.

Going concern

14. I draw attention to the matter below. My opinion is not modified in respect of this matter.
15. I draw attention to note 48 in the consolidated and separate financial statements, which indicates that, as of 30 June 2018 the municipality's current liabilities exceeded its current assets by R3,11 million. There was also a significant decrease in the municipality's cash balance.

Other matters

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

Unaudited supplementary schedules

17. The supplementary information set out on pages XX to XX does not form part of the consolidated and separate financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion on them.

Unaudited disclosure notes

18. 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 consolidated and separate financial statements. This disclosure requirement did not form part of the audit of the consolidated and separate financial statements and, accordingly, I do not express an opinion on it.

Responsibilities of the accounting officer for the consolidated and separate financial statements

19. The accounting officer is responsible for the preparation and fair presentation of the consolidated and separate 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 consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.

20. In preparing the consolidated and separate 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 consolidated and separate financial statements

21. My objectives are to obtain reasonable assurance about whether the consolidated and separate 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 the assurance engagement conducted in accordance with the relevant assurance standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if they could reasonably be expected to influence the relevant decisions of users taken on the basis of the reported performance information.
22. A further description of my responsibilities for the audit of the consolidated and separate financial statements is included in the annexure to this auditor's report.
23. 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 of the consolidated and separate financial statements in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.

Report on the audit of the annual performance report

Introduction and scope

24. 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 priority presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
25. 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.

26. 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 priority	Pages in the annual performance report
<i>Development priority 1: Basic service delivery</i>	x – x

27. 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.
28. The material finding in respect of the usefulness and reliability of the selected development priority are as follows:

Percentage compliance to water tankering programme

29. The municipality did not maintain adequate records to support the achievement of the indicator to enable reliable reporting on achievement of targets. As a result, I was unable to obtain sufficient appropriate audit evidence for the reported achievement of 84%. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any further adjustments were required to the reported achievement.

Other matters

30. I draw attention to the matters below.

Achievement of planned targets

31. The annual performance report on page x to x; includes information on the achievement of planned targets for the year. This information should be considered in the context of the material finding on the usefulness and reliability of the reported performance information in paragraph 29 of this report.

Adjustment of material misstatements

32. 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. 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.

Introduction and scope

33. 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.
34. The material findings on compliance with specific matters in key legislation are as follows:

Consolidated and separate financial statements

35. The consolidated and separate 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, current liabilities, revenue and disclosure items identified by the auditors in the submitted consolidated and separate financial statements were not adequately corrected and the supporting records could not be provided subsequently, which resulted in the consolidated and separate financial statements receiving an adverse audit opinion.

Expenditure management

36. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R243,82 million, as required by section 62(1)(d) of the MFMA, which is disclosed in note 50 to the consolidated and separate financial statements. The majority of the unauthorised expenditure was caused by lack of proper planning.
37. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The expenditure disclosed does not reflect the full extent of the irregular expenditure, which could not be quantified as indicated in the basis for adverse opinion paragraph. The majority of the disclosed irregular expenditure was caused by the non-adherence to municipal supply chain management regulations.
38. Reasonable steps were not taken to prevent fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA, which is disclosed in note 51 to the consolidated and separate financial statements. The majority of the disclosed fruitless and wasteful expenditure was caused by late settlement of invoices which attracted interest.
39. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
40. Expenditure was incurred in excess of the approved budget, in contravention of section 87(8) of the MFMA.

Revenue management

41. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.

Assets management

42. Capital assets were disposed of without the municipality having in a meeting open to the public, decided on whether the assets were still needed to provide the minimum level of basic municipal services and considered the fair market value of the assets and the economic and community value to be received in exchange for the assets, as required by section 14(2)(a) and 14(2)(b) of the MFMA.
43. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Consequence management

44. Some of the unauthorised expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) of the MFMA.
45. Some of the irregular expenditure incurred by the municipality were not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.
46. Some of the 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.

Procurement and contract management

47. Some of the goods and services with a transaction value below R200 000 were procured without obtaining the required price quotations, in contravention with municipal supply chain management regulation 17(a) and (c). Similar non-compliance was also reported in the prior year.
48. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by municipal supply chain management regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of municipal supply chain management regulation 36(1). Similar non-compliance was also reported in the prior year.
49. The performance of some of the contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA. Similar non-compliance was also reported in the prior year.
50. Some of the contracts were extended or modified without the approval of a properly delegated official, in contravention of municipal supply chain management regulation 5. Similar non-compliance was also reported in the prior year.
51. Some of the bid documentation for procurement of commodities designated for local content and production, did not stipulate the minimum threshold for local production and content as required by the preferential procurement regulation 8(2). Similar non-compliance was also reported in the prior year.

Other information

52. 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 consolidated and separate 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.
53. My opinion on the consolidated and separate 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.
54. 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 consolidated and separate financial statements and the selected development priority presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
55. 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.
56. I have nothing to report in this regard.

Internal control deficiencies

57. I considered internal control relevant to my audit of the consolidated and separate financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it.
58. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the adverse opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.
59. Leadership did not exercise effective oversight and monitoring over financial and performance reporting and compliance with legislation.

60. Management did not implement controls to regularly update, validate and reconcile financial and performance records. Consequently, management did not ensure that the consolidated and separate financial statements and the annual performance report were supported by accurate and reliable information.

Auditor-General
Pietermaritzburg

14 December 2018



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence

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 consolidated and separate financial statements, and the procedures performed on reported performance information for selected development priority and on the municipality’s compliance with respect to the selected subject matters.

Consolidated and separate financial statements

2. In addition to my responsibility for the audit of the consolidated and separate financial statements as described in this auditor’s report, I also:
 - identify and assess the risks of material misstatement of the consolidated and separate 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 consolidated and separate 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 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 consolidated and separate financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the consolidated and separate 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 consolidated and separate financial statements, including the disclosures, and whether the consolidated and separate financial statements represent the underlying transactions and events in a manner that achieves fair presentation

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.