

Auditor-General of South Africa

uThukela District Municipality

Audit report 2017-18

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

## Report on the audit of the financial statements

### Qualified opinion

1. I have audited the financial statements of the uThukela District Municipality set out on pages' x to x, which comprise the statement of financial position as at 30 June 2018, the statement of financial performance, statement of changes in net assets, the 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 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 uThukela District 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, 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 qualified opinion

#### Revenue and receivables from exchange transaction – service charges

3. The municipality did not recognise all items that met the definition of revenue from exchange transactions in accordance with SA Standard of GRAP 9, *Revenue from exchange transactions*. Revenue from service charges was not accounted for at the fair value of the consideration received or receivable, as required by this standard. The municipality did not maintain adequate records of consumers that had working infrastructure and received services. I was therefore unable to confirm the service charges by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to service charges stated at R169,25 million (2016-17: R158,50) and consumer debtors disclosed at R186,36 million (2016-17: R159,66), in notes 22 and 12 respectively to the financial statements.

#### Water losses

4. I was unable to obtain sufficient appropriate audit evidence for the water losses stated at R161,17 million (2016-17: R127,65 million) in note 55 to the financial statements. This was due to inadequate systems and processes for the recording and monitoring of these losses. I could not confirm the disclosed losses through alternative means. Consequently, I was unable to determine whether any adjustments were necessary to water losses disclosed in the financial statements.

## **Context for the opinion**

5. 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.
6. 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.
7. 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 going concern**

8. I draw attention to the matter below. My opinion is not modified in respect of this matter.
9. Note 45 to the financial statements indicated that as at 30 June 2018 the municipality's current liabilities exceeded its current assets by R97,42 million. In addition, unspent conditional grants of R47,23 million, consumer deposits of R15,04 million, retention creditors of R27,23 million and trust funds of R5,19 million were not cashed backed. These events or conditions, along with other matters as set forth in note 45 to the financial statements, indicate that a material uncertainty exists that may cast significant doubt on the municipality's ability to continue as a going concern.

## **Emphasis of matters**

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

## **Restatement of corresponding figures**

11. As disclosed in note 42 to the financial statements, the corresponding figures for 30 June 2017 were restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2018.

## **Material impairments and losses**

12. As disclosed in note 12 to the financial statements, the municipality recognised a provision for bad debts of R634,76 million (2016-17: R525,30 million) on consumer debtors, as the recoverability of these amounts was doubtful.
13. As disclosed in note 47 to the financial statements, material losses of R13,39 million (2016-17: R32,26 million) were incurred as a result of a write-off of irrecoverable trade debtors.

## **Other matter**

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

## Unaudited disclosure notes

15. 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 the accounting officer for the financial statements**

16. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and Dora, and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

17. 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**

18. 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.

19. 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**

20. 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.

21. 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.

22. 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:

<b>Development priority</b>	<b>Pages in the annual performance report</b>
Development priority 1: Basic services delivery	x – x

23. 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.
24. The material findings in respect of the usefulness and reliability of the selected development priority are as follows:

#### **Percentage of households with access to basic level of water**

25. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of the target: 100% of households with access to basic level of water. 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 reported achievement.

#### **Other matters**

26. I draw attention to the matters below.

#### **Achievement of planned targets**

27. The annual performance report on pages' 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 findings on the usefulness and reliability of the reported performance information in paragraph 25 of this report.

#### **Adjustment of material misstatements**

28. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information of the basic service delivery development priority. 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

29. 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.
30. The material findings on compliance with specific matters in key legislation are as follows:

### Annual financial statements

31. 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 identified by the auditors in the submitted financial statements were not adequately corrected and the supporting records could not be provided subsequently, which resulted in the financial statements receiving a qualified audit opinion.

### Expenditure management

32. Reasonable steps were not taken to prevent unauthorised expenditure of R70,97 million, as disclosed in note 48 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. Most of the unauthorised expenditure was caused by overspending on the approved budget.
33. Reasonable steps were not taken to prevent irregular expenditure of R399,83 million, as disclosed in note 50 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. Most of the irregular expenditure was caused by non-compliance with Municipal Supply Chain Management Regulations GNR 868 30 May 2005 (MSCMR).
34. Money owed by the municipality was not always paid within 30 days or an agreed period, as required by section 65(2)(e) of the MFMA.

### Procurement and contract management

35. Some of the goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations, in contravention of MSCMR 17(a) and (c).
36. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by MSCMR 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of MSCMR 36(1). Similar non-compliance was reported in the prior year.
37. Contracts were awarded to and quotations were accepted from bidders who had not submitted a declaration on whether they are employed by the state or connected to any person employed by the state, as required by MSCMR 13(c).
38. Contracts were awarded to and quotations were accepted from bidders whose tax matters had not been declared by the South African Revenue Service to be in order, in contravention of MSCMR 43.

39. Contracts were awarded to and quotations were accepted from bidders based on points given for criteria that differed from those stipulated in the original invitation for bidding and quotations, in contravention of MSCMR 21(b) and 28(1)(a) and the 2017 Preferential Procurement Regulations (PPR).
40. Some of the contracts were awarded to bidders based on preference points that were not allocated and/or calculated in accordance with the requirements of the Preferential Procurement Policy Framework Act, 2000 (Act No. 5 of 2000) (PPPFA) and its regulations.
41. Some of the contracts were awarded to bidders that had not scored the highest points in the evaluation process, as required by section 2(1)(f) of PPPFA and PPR.
42. 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 2017 PPR 8(2). Similar non-compliance was reported in the prior year. This non-compliance was identified in the procurement processes for the purchase of furniture and other protective clothing.
43. Commodities designated for local content and production were procured from suppliers who had not submitted a declaration on local production and content as required by 2017 PPR. This non-compliance was identified in the procurement processes for the purchase of furniture and other protective clothing.
44. Contracts were extended or modified without the approval of a properly delegated official, in contravention of MSCMR 5.
45. 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.

#### **Utilisation of conditional grants**

46. The Regional Bulk Infrastructure Grant was not spent in accordance with the applicable grant framework, in contravention of section 17(1) of Dora.

#### **Consequence management**

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

#### **Revenue management**

48. An effective system on internal control over revenue and debtors was not in place, in contravention of section 64(2)(f) of the MFMA.
49. Revenue due to the municipality was not calculated on a monthly basis, as required by section 64(2)(b) of the MFMA.



## Other information

50. 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 development priorities presented in the annual performance report that have been specifically reported in this auditor's report.
51. 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.
52. 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 priority presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
53. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information and 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 reissue an amended report as appropriate. However, if it is corrected this will not be necessary.

## Internal control deficiencies

54. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon.
55. 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.
56. Leadership did not provide adequate oversight and monitoring in ensuring that approved policies and action plans are implemented to fully address prior year findings on the financial statements, predetermined objectives and compliance with legislation. Furthermore, consequence management was not effectively implemented for non-performance and slow responses in addressing and implementing recommendations and transgressions reported.
57. Senior management did not implement proper record management processes and systems for the maintenance of documents supporting both the annual financial statements and reported performance. Additionally, procurement and contract management requirements were not complied with and monitored.
58. Furthermore, controls and processes over the preparation of the financial statements and the annual performance report were not effectively implemented by senior management to ensure that they were accurately prepared and supported by reliable and credible information.



## Other reports

59. 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.

### Investigation

60. The municipality's legal team is currently investigating an allegation of possible misappropriation of the municipality's assets, which covers the period from 1 July 2016 to 30 June 2017.

*Auditor - General SA*  
Pietermaritzburg

30 November 2018



AUDITOR - GENERAL  
SOUTH AFRICA

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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 development priority 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 municipality 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 operating 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**

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.

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.