



**AUDITOR - GENERAL
SOUTH AFRICA**

Auditing to build public confidence



BLUE CRANE ROUTE LOCAL MUNICIPALITY

Audit Report

For the year ended 30 June 2019



**AUDITOR-GENERAL
SOUTH AFRICA**

Auditing to build public confidence

Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on the Blue Crane Route Municipality

Report on the audit of the financial statements

Opinion

1. I have audited the financial statements of the Blue Crane Route Municipality set out on pages to ..., which comprise the statement of financial position as at 30 June 2019, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Blue Crane Route Municipality as at 30 June 2019, 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 of South Africa, 2018 (Act No. 1 of 2018) (Dora).

Basis for opinion

3. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of this auditor's report.
4. I am independent of the municipality in accordance with sections 290 and 291 of the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* and parts 1 and 3 of the International Ethics Standards Board for Accountants' *International code of ethics for professional accountants (including International Independence Standards)* (IESBA codes) as well as 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 codes.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Emphasis of matters

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

Material losses

7. As disclosed in note 27 to the financial statements, material electricity losses of R11,9 million (2017-18: R9 million) were incurred, which represent 22% (2017-18: 19%) of the total electricity purchased; and material water losses of R3,4 million (2017-18: R5,6 million) were incurred, which represent 30% (2017-18: 48%) of the total water purchased.

Debt impairment

8. As disclosed in note 33 to the financial statements, material losses of R19,4 million (2017-18: R8,9 million) were incurred as a result of the write-off of irrecoverable trade debtors.

Restatement of corresponding figures

9. As disclosed in note 45 to the financial statements, the corresponding figures for 30 June 2018 have been restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2019.

Underspending of conditional grants

10. As disclosed in note 18 to the financial statements, the municipality materially underspent the allocation on conditional grants by R25 million.

Material uncertainty relating to going concern / financial sustainability

11. As disclosed in note 47 to the financial statements, current liabilities exceeded current assets, there were high levels of water and electricity losses, and debt and credit payment ratios were not in the norm. As stated in note 47, these events or conditions, along with the other matters as set forth in note 47, indicate that a material uncertainty exists that may cast significant doubt on the municipality's ability to continue as a going concern.

Other matter

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

Unaudited supplementary schedules

13. The supplementary information set out on pages 70 to 90 does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion on them.

Responsibilities of the 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 Dora, and for such internal control as the accounting authority 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 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's responsibilities for the audit of the financial statements

16. 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.
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

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 priority presented in the annual performance report of the municipality for the year ended 30 June 2019:

Development priorities	Pages in the annual performance report
KPA 2 – basic services and infrastructure 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 development priority are as follows:

KPA 2 – basic service delivery and infrastructure development

KPI: No of water samples taken for chemical bacteriological analysis

23. The planned target for this indicator was not specific in clearly identifying the nature and required level of performance, as it did not provide a breakdown of the target per the different categories of tests to be performed. The planned target referred to 96 water samples taken for chemical and bacteriological analysis, but the reported achievement referred to 102 water samples for bacteriological and 4 chemical analyses.

Various indicators

24. The method of calculation for achieving the planned indicators was not clearly defined for the listed indicators:

- % expenditure on the budget of upgrading of Pearston WWTW
- % expenditure on the budget of Pearston Water Treatment Works
- % expenditure on the budget on upgrading of cookhouse WWTW (phase 3)

25. The systems and processes that should enable reliable reporting of achievements against indicators were not adequately designed, since the method of measurement was based on expenditure instead of progress of the project for the indicators below:

- % expenditure on the budget of upgrading of Pearston WWTW
- % expenditure on the budget of Pearston Water Treatment Works
- % expenditure on the budget on upgrading of cookhouse WWTW (phase 3)

26. The planned targets for the following indicators were not specific in clearly identifying the nature and required level of performance, and were also not measurable:

- % expenditure on the budget of upgrading of Pearston WWTW
- % expenditure on the budget of Pearston Water Treatment Works
- % expenditure on the budget on upgrading of cookhouse WWTW (phase 3)

27. I was unable to obtain sufficient appropriate audit evidence to validate the existence of systems and processes that should enable reliable reporting of actual service delivery against the indicators. This was due to a lack of technical indicator descriptions and formal standard operating procedures or documented system descriptions, since the method of measurement was based on expenditure instead of progress of the project. I was unable to validate the existence of systems and processes by alternative means for the indicators listed below:

- % expenditure on the budget of upgrading of Pearston WWTW
- % expenditure on the budget of Pearston Water Treatment Works
- % expenditure on the budget on upgrading of cookhouse WWTW (phase 3)
- No of water samples taken for chemical bacteriological analysis

KPI: % progress in the upgrade of Somerset East Sportfields (fencing, installation of irrigation system and refurbishment of netball court)

28. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of the target of 70% progress in the upgrade of Somerset East Sportfields. 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 80% as reported in the annual performance report.

Various indicators

29. The measures taken to improve performance against targets that were not achieved as planned were not included in the annual performance report for the indicators below:

- % progress in the construction of ablution facilities and change room at the Pearston sportsfield
- % progress in the construction of ablution facilities and change room at the Somerset East sportsfield

Other matters

30. I draw attention to the matters below.

Achievement of planned targets

31. Refer to the annual performance report on pages 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 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 KPA 2 – basic service delivery and infrastructure 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

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:

Annual financial statements

35. 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.

36. Material misstatements of service charges, bulk purchases and trade receivables from exchange transactions identified by the auditors in the submitted financial statements were subsequently corrected and/or the supporting records provided, resulting in the financial statements receiving an unqualified audit opinion.

Human resource management

37. Senior managers did not sign performance agreements within the prescribed period, as required by section 57(2)(a) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000).

Expenditure management

38. Reasonable steps were not taken to prevent irregular expenditure amounting to R20,9 million, as disclosed in note 51 of the financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by non-compliance with the Supply Chain Management (SCM) Regulations.
39. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R18 million, as disclosed in note 49 to the financial statements, as required by section 62(1)(d) of the MFMA.

Procurement and contract management

40. Some of the invitations for competitive bidding were not advertised for the required minimum period, in contravention of SCM regulation 22(1) and 22(2).
41. Quotations were accepted from bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
42. Sufficient appropriate audit evidence could not be obtained that a contract was awarded in accordance with the legislative requirements.

Consequence management

43. Prior year 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.

Other information

44. The accounting authority is responsible for the other information. The other information comprises the information included in the annual report, which includes the mayor's foreword, executive summary, governance, organisational development performance and financial performance. The other information does not include the financial statements, the auditor's report and the selected development priority presented in the annual performance report that has been specifically reported on in this auditor's report.
45. 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.

46. 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.
47. 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 re-issue an amended report as appropriate; however, if it is corrected this will not be necessary.

Internal control deficiencies

48. 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 findings on the annual performance report and the findings on compliance with legislation included in this report.
49. The municipality did not have sufficient monitoring controls to ensure the proper implementation of the overall process of planning, budgeting, implementation and reporting. This had an impact on the financial and performance management systems, resulting in material misstatements in performance information and non-compliance with legislation.
50. The municipality's system to monitor compliance with applicable legislation was not effective. Non-compliance with legislation and SCM processes could have been prevented had compliance been properly reviewed and monitored. Management also did not timeously monitor adherence to the audit action plan, which resulted in a number of repeat findings.
51. The municipality did not have a proper record management system to maintain information that supported the reported performance in the annual performance report. This included information that related to the collection, collation, verification, storing and reporting of actual performance information.

Other reports

52. I draw attention to the following engagements 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. These reports did not form part of my opinion on the financial statements or my findings on the reported performance information or compliance with legislation.

53. An independent consultant investigated various allegations of possible financial misconduct at the request of the municipality's council, which covered the period 10 December 2018 to 25 January 2019. The investigation concluded on 25 January 2019 but no material findings were identified. The final report was tabled in the council during August 2019.
54. The disciplinary board is investigating an allegation of an incorrect payment resulting from the fraudulent changing of the bank account, which covers the period 23 December to 22 January 2019. The investigation concluded on 22 January 2019 and did not result in any official being found liable and the board recommending the amount be written off. However, the council resolved during March 2019 that the matter should be investigated further.

Auditor-General

East London

29 November 2019



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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 the 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’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

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.