



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

REPORT OF THE AUDITOR-GENERAL TO THE NORTH WEST PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE MOSES KOTANE DEVELOPMENT AGENCY (SOC) LTD

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the Moses Kotane Development Agency (SOC) Ltd, which comprise the statement of financial position as at 30 June 2011, and the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information as set out on pages [XX] to [XX]

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and in the manner required by the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Companies Act of South Africa, 2008 (Act No. 71 of 2008). This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor-General's responsibility

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 (Act No. 108 of 1996), section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and section 300 of the Companies Act, my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with International Standards on Auditing and *General Notice 1111 of 2010* issued in *Government Gazette 33872 of 15 December 2010*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Basis for adverse opinion

Property, plant and Equipment

6. I was unable to verify the completeness, existence and valuation of property, plant and equipment of R105 104 (2010: R178 073) disclosed in the statement of financial position. The limitation is due to inadequate descriptions and details on the asset register to enable me to verify the completeness, existence and valuation of these assets. The municipality's records did not permit the application of alternative audit procedures regarding property, plant and equipment.
7. The entity did not annually review the residual values and useful lives of property, plant and equipment as required by SA Standards of GRAP, GRAP 17, *Property, plant and equipment*. The municipality's records did not permit the performance of alternative audit procedures. Consequently, I was unable to obtain sufficient appropriate audit evidence to verify the valuation of property, plant and equipment of R105 104 (2010: R178 073) disclosed in the statement of financial position and note 2 of the financial statements as well as the accuracy, occurrence and completeness of the depreciation expense of R72 969 (2010: R77 299) as disclosed in the statement of financial performance and note 2 of the financial statements.
8. SA Standards of GRAP, GRAP 17, *Property, Plant and Equipment* require that an item that meets the definition of property, plant and equipment be recognised at cost less accumulated depreciation. As reported in the prior year assets of R15 077 were incorrectly classified as operating expenditure instead of capitalised as property, plant and equipment. This error has not been corrected and consequently property, plant and equipment of R105 104 (2010: R178 073) disclosed in the statement of financial position is understated by R15 077.

Revenue

9. I was unable to obtain sufficient appropriate audit evidence for revenue of R2 000 in respect of recoupment. The municipal entity's records did not permit the application of alternative audit procedures for these revenue items. Consequently, I was unable to verify the occurrence, accuracy and classification of this amount included in revenue of R2 001 as disclosed in the statement of financial performance.
10. As reported in the prior year, my opinion on the corresponding figures of R199 397 relating to the revenue from sales of goods, rental income of R27 936 and grants of R612 179 were modified. Sufficient appropriate audit evidence to substantiate the revenue could not be provided for audit. The municipal entity's records did not permit the application of alternative audit procedures regarding these revenue transactions. Consequently, I was unable to verify the occurrence, accuracy and classification of these corresponding amounts.
11. As reported in the prior year, my opinion on the corresponding figure in terms of revenue grants was modified. Expenditure payments of R3 229 613 made by the Moses Kotane Local Municipality on behalf of the Moses Kotane Development Agency was not recognised as revenue and expenditure as required by the SA Standards of GRAP, GRAP 23, *Revenue from non-exchange transactions*. Consequently, both the corresponding for revenue and the corresponding figure for expenditure are understated by R3 229 613.

Liabilities

12. As reported in the prior year, my opinion on the corresponding figure of R612 179 for advances and R123 669 for trade payables as disclosed in the corresponding figures of the 2010 financial statements was modified. Sufficient appropriate audit evidence to substantiate the advances and trade payables could still not be provided for audit. The entity's records did not permit the application of alternative audit procedures regarding these advances and trade payables. Consequently, I was unable to verify the completeness, existence and valuation of these corresponding amounts.
13. As reported in the prior year sufficient appropriate audit evidence to substantiate the movements amounting to R123 669 in trade payables could not be provided. Sufficient appropriate audit evidence can still not be provided and the municipal entity's records did not permit the application of alternative audit procedures regarding the movements in payables.

Consequently, I am unable to verify the valuation and completeness of trade payables disclosed as R0 for both the prior year and current year.

14. Provision was not raised in the current and prior year financial statements for the *accrued leave pay as required by SA Statements of GRAP, GRAP 19 Provisions, Contingent liabilities and Contingent assets*. Sufficient appropriate evidence was not available to calculate the extent of the misstatement. Consequently, I was unable to verify the completeness of liabilities as disclosed in the statement of financial position.

Employee cost

15. As reported in the prior year, my opinion on the corresponding figure of R71 438 as disclosed in note 9 of the financial statements was modified in respect of personnel cost. The municipal entity's records did not permit the application of alternative audit procedures. Consequently, I did not obtain all the evidence I considered necessary to verify the occurrence, accuracy and classification of employee cost.
16. Salaries of R180 772 paid by the Moses Kotane Local Municipality on behalf of the Moses Kotane Development Agency was not recognised as revenue and expenditure as required by the SA Standard of GRAP, GRAP 23, *Revenue from non-exchange transactions*. Consequently, revenue employee costs and related party transactions are understated by R180 772.

Operating Expenditure

17. As reported in the prior year, my opinion on the corresponding figure of R70 675 included in general expenses of R72 207 disclosed in note 7 of the financial statements was modified. The entity's records did not permit the application of alternative audit procedures regarding these expenses. Consequently, I did not obtain all the evidence I considered necessary to verify the occurrence, accuracy and classification of this expenditure.

Related party transactions

18. As reported in the prior year, my opinion on the corresponding figure of R618 281 disclosed in note 15 of the financial statements was modified. The municipal entity's records did not permit the application of alternative audit procedures to substantiate these related party transactions. Consequently, I was unable to verify the occurrence, accuracy and valuation, and completeness of the corresponding amount disclosed for related party transactions.
19. International Public Sector Accounting Standard, IPSAS 20, *Related party disclosures* requires the disclosure of all transactions with related parties. As reported in the prior year, expenditure amounting to R3 229 613 in respect of payments made by the Moses Kotane Local municipality on behalf of the municipal entity was not recognized as related party transactions.

Going Concern

21. On 29 July 2010 the Council took a resolution to suspend the operating activities of the Moses Kotane Development Agency (SOC) Ltd and to dissolve the board of directors. As at 30 June 2011 the operating activities of the entity had significantly declined and on 1 July 2010, the employees of the entity were also officially transferred to the Moses Kotane Local Municipality. This indicates a material uncertainty that may cast significant doubt on the entity's ability to continue as a going concern and therefore it may be unable to realise its assets and discharge its liabilities in the normal course of operations. The financial statements and notes thereto do not disclose this fact.

Irregular and fruitless and wasteful

22. As reported in the prior year, my opinion on the corresponding figure for irregular expenditure was modified due to the unavailability of sufficient appropriate audit evidence incurred during 2009 to verify whether operating expenditure of R780 534 was made in terms of the municipality's SCM policy. Consequently, I was unable to verify the occurrence, accuracy and valuation and completeness of irregular expenditure.

23. As reported in the prior year, my opinion on the corresponding figure of fruitless and wasteful expenditure was modified. Fruitless and wasteful expenditure of R113 142 identified in the prior year (2009), was still not disclosed in the notes to the financial statements for both the prior year and current year. Consequently the closing balance for fruitless and wasteful expenditure is understated with R113 142.

Adverse Opinion

24. Because of the significance of the matters described in the basis for adverse opinion paragraphs, the financial statements do not present fairly the financial position of the Moses Kotane Development Agency (SOC) Ltd as at 30 June 2011 and its financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of the MFMA and the Companies Act.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

25. In accordance with the PAA and in terms of *General Notice 1111 of 2010*, issued in *Government Gazette 33872 of 15 December 2010*, I include below my findings on the material non-compliance with laws and regulations applicable to the municipal entity.

Predetermined objectives

26. I was unable to conduct the audit of performance against predetermined objectives as the municipal entity did not submit the annual performance report as required by section 46 of the Municipal Systems Act of South Africa 2000 (Act No. 32 of 2000) (MSA) and section 121(4)(d) of the MFMA.

Compliance with laws and regulations

Strategic planning and performance management

27. The accounting officer of the municipal entity did not, by 20 January assess the performance of the entity during the first half of the financial year, taking into account the targets set in the service delivery agreement, business plan or other agreement with the entity's parent municipality as required by section 88(1)(a) of the MFMA.
28. The accounting officer of the municipal entity did not submit the results of the assessment on the performance of the municipality during the first half of the financial year to the parent municipality of the entity as required by section 88(1)(b) of the MFMA.

Budgets

29. The board of directors did not approve the annual budget by 31 May, 30 days before the start of the financial year, as required by section 87(4) of the MFMA.

Annual Financial Statements

30. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements identified by the auditors were not adequately corrected, which resulted in the financial statements receiving an adverse audit opinion.
31. The accounting officer did not submit the annual financial statements of the municipal entity for auditing, within two months after the end of the financial year as required by section 126(2)(b) of the MFMA.
32. Late submission of the annual financial statements to the Auditor-General for auditing was not appropriately addressed by the Mayor and municipal council of the parent municipality as per the requirements of section 133(1) of the MFMA.
33. The accounting officer did not prepare and include an assessment of the performance against any measurable performance objectives set, in terms of the service delivery agreement or other agreement between the entity and its parent municipality as required by section 121(4)(d) of the MFMA.

Audit Committees

34. No audit committee was in place as required by section 166(1) of the MFMA.

Internal Audit

35. The municipal entity did not have an internal audit unit in place as required by section 165(1) of the MFMA.

Expenditure Management

36. The accounting officer did not take reasonable steps to prevent irregular expenditure and fruitless and wasteful expenditure, as required by section 95(d) of the MFMA.

INTERNAL CONTROL

37. In accordance with the PAA and in terms of *General Notice 1111 of 2010*, issued in *Government Gazette 33872 of 15 December 2010*, I considered internal control relevant to my audit, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters reported below are limited to the significant deficiencies that resulted in the basis for adverse opinion and the findings on compliance with laws and regulations included in this report.

Leadership

38. Management's philosophy and operating style does not promote effective control over reporting, as evidenced by inappropriate implementation and monitoring of action plans to address prior year audit findings. The accounting officer does not exercise oversight over reporting and compliance with laws and regulations and internal control

Financial and performance management

39. Management did not implement proper record keeping in a timely manner to ensure that complete, relevant and accurate information is accessible and available to support financial and performance reporting. Sufficient controls were not implemented over daily and monthly processing and reconciling of transactions.

Governance

40. The Council did not implement good governance principles over the operations of the municipal entity, which includes establishment of the internal audit function and the audit committee and oversight over compliance with laws and regulation.

Auditor-General

Rustenburg

20 April 2012



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