

REPORT OF THE AUDITOR-GENERAL TO THE KWAZULU-NATAL PROVINCIAL LEGISLATURE AND THE COUNCIL ON NQUTHU MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Nquthu Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2012, the statement of financial performance, statement of changes in net assets and the cash flow statement for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting Officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Local Government: Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2011 (Act No. 6 of 2011) (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.

Auditor-General's responsibility

3. My responsibility is to express an opinion on the financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the *General Notice* issued in terms thereof and International Standards on Auditing. 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.
4. 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 municipality'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 municipality'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.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Nquthu Municipality as at 30 June 2012, 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 DoRA.

Emphasis of matters

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

Irregular expenditure

8. As disclosed in note 46 to the financial statements, the municipality incurred irregular expenditure of R3,101million due to not following the Municipal Supply Chain Management procedures.

Significant uncertainties

9. As disclosed in note 37 to the financial statements, the municipality is a defendant in four lawsuits, of which the timing and outcome of the litigations cannot presently be determined and no provision for any liability that may result has been made in the financial statements.

Material losses

10. As disclosed in note 49 to the financial statements, the municipality incurred material electricity distribution losses amounting to R2,600 million (11,114 million kilowatt hours) during the year.

Material impairments

11. As disclosed in note 11 to the financial statements, the municipality provided for an impairment allowance of R6,242 million on consumer debtors as the recoverability of these amounts were considered doubtful.

Additional 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 xx to xx do 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 thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

14. In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

15. I am unable to report findings on the usefulness and reliability of the annual performance report, as it was not prepared, as required by section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) and 121(3)(c) of the MFMA.

Compliance with laws and regulations

16. I performed procedures to obtain evidence that the municipality has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the *General Notice* issued in terms of the PAA are as follows:

Procurement and contract management

17. Contracts and quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, contrary to the requirements of regulation 13(c) of the Local Government: Municipal Supply Chain Management Regulations of 30 May 2005.

Annual financial statements, performance and annual report

18. The accounting officer did not make public the council's oversight report on the 2010-2011 annual report within seven days of its adoption, as required by section 129(3) of the MFMA.

19. The annual performance report for the financial year under review was not prepared, as required by section 46 of the MSA and section 121(3)(c) of the MFMA.

20. 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 disclosure items identified by the auditors were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.

Conditional grants

21. Monthly budget statements did not include the extent of compliance with conditions of the allocation, as required by section 12(2)(b) of the DoRA.

Audit committee

22. The audit committee did not advise council, the accounting officer and management staff on matters relating to risk management and accounting policies, as required by section 166 of the MFMA.

Internal audit

23. Internal audit did not advise the accounting officer or report to the audit committee, on matters relating to accounting procedures and loss control, as required by section 165 of the MFMA.

Budgets

24. Expenditure was incurred in excess of the amounts provided for in certain votes of the approved budget, contrary to the requirements of section 15 of the MFMA.

Strategic planning and performance management

25. The municipality did not comply with section 41 of the MSA, as it did not:

- set appropriate key performance indicators as a yardstick for measuring performance, including outcomes and impact, with regard to the municipality's development priorities and objectives set out in its integrated development plan.
- set measurable performance targets with regard to each development priority and objective.
- monitor performance, with regard to each of those development priorities and objectives and against the key performance indicators and targets set.
- measure and review performance at least once per year, with regard to each of those development priorities and objectives and against the key performance indicators and targets set.
- take steps to improve performance with regard to those development priorities and objectives where performance targets are not met.

INTERNAL CONTROL

26. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

27. Management did not exercise effective oversight over policies and procedures regarding budgets, supply chain and performance management to enable and support the understanding and execution of internal control objectives, processes and responsibilities.

Financial and performance management

28. An effective system for monitoring compliance has not been established to prevent non-compliance with laws and regulations.
29. Management did not implement effective controls over the preparation, review and reconciliation of financial records as well as the reporting of performance against predetermined objectives. Consequently, internal controls were unable to prevent and detect material misstatements in the annual financial statements.

Governance

30. The audit committee and internal audit did not completely fulfil their responsibilities for the year.

Pietermaritzburg

30 November 2012



**AUDITOR - GENERAL
SOUTH AFRICA**

Auditing to build public confidence