

**REPORT OF THE AUDITOR-GENERAL TO THE KWAZULU-NATAL PROVINCIAL  
LEGISLATURE AND COUNCIL ON NEWCASTLE MUNICIPALITY  
REPORT ON THE FINANCIAL STATEMENTS**

**Introduction**

1. I have audited the financial statements of the Newcastle Municipality set out on pages ... to ..., which comprise, the statement of financial position as at 30 June 2013, 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 Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2012 (Act No. 5 of 2012) (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 qualified audit opinion.

**Basis for qualified opinion**

**Accumulated surplus**

6. I was unable to obtain sufficient appropriate evidence for the correction of prior period errors amounting to R202,22 million which are included in the accumulated surplus of R3,01 billion. Therefore these prior period errors that are included in the accumulated surplus could not be confirmed by alternative means. Consequently I was unable to determine whether any further adjustments to the accumulated surplus balance was necessary.

### **Value-added-taxation (VAT) receivable**

7. I was unable to obtain sufficient appropriate audit evidence regarding the VAT receivable. I was also unable to confirm this amount by alternative means. Consequently, I was unable to determine whether any adjustment relating to the VAT receivable amounting to R47,13 million, as disclosed in note 12 to the financial statements was necessary.

### **Property, infrastructure and equipment**

8. I was unable to obtain sufficient appropriate audit evidence to support completed capital projects amounting to R16,78 million included in the prior year adjustment in note 4 to the financial statements. I was unable to confirm the physical assets by alternative means. Consequently, I was unable to determine whether any adjustment relating to infrastructure assets amounting to R1 billion as disclosed in note 4 to the financial statements was necessary.
9. I was unable to obtain sufficient appropriate audit evidence to support work in progress amounting to R168,66 million included in the prior year adjustment in note 4 to the financial statements. I was unable to confirm the physical assets by alternative means. Consequently, I was unable to determine whether any adjustment relating to the work in progress amounting to R363,80 million as disclosed in note 4 to the financial statements was necessary.
10. I was unable to obtain sufficient appropriate audit evidence to support water infrastructure assets that were transferred to uThukela Water (Pty) Ltd amounting to R22,73 million, as I was not provided with the location and supporting documents of these assets. I was unable to confirm the physical existence of assets by alternative means. Consequently, I was unable to determine whether any adjustment relating to the transfer of the water infrastructure assets amounting to R363,80 million as disclosed in note 4 to the financial statements was necessary.

### **Investment in associated municipal entity: uThukela Water (Pty) Ltd**

11. I was unable to obtain sufficient appropriate audit evidence for transactions included in the prior year adjustment regarding the investment in the associated municipal entity amounting to R21,66 million. I was unable to confirm the prior year adjustments for this investment by alternative means. Consequently, I was unable to determine whether any adjustment relating to the investment in the associated municipal entity amounting to R1 billion as disclosed in note 7 to the financial statements was necessary.

### **Qualified opinion**

12. In my opinion, except for the possible effects of the matters described in the Basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Newcastle Municipality as at 30 June 2013, and its financial performance and cash flows for the year then ended in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA.

### **Emphasis of matters**

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

### **Restatement of corresponding figures**

14. As disclosed in note 35 to the financial statements, the corresponding figures for 30 June 2012 have been restated as a result of an error discovered during 30 June 2013 in the financial statements of the Newcastle municipality at, and for the year ended 30 June 2012.

### **Material losses and impairments**

15. As disclosed in note 28 to the financial statements, material losses to the amount of R16,95 million (42 386 025 kilowatt hours) were incurred as a result of electricity distribution losses, due to transmission losses and illegal connections.
16. As disclosed in note 13 to financial statements, the municipality provided for impairment losses on consumer debtors of R503,87 million, as the recoverability of these amounts are considered doubtful.

### **Irregular expenditure**

17. The municipality incurred irregular expenditure of R55,03 million as disclosed in note 41 to the financial statements, as the expenditure incurred was in contravention of the Municipal Supply Chain Management Regulations (MSCMR).

### **Significant uncertainties**

18. With reference to note 34 to the financial statements, the municipality is a defendant in various lawsuits and there are also uncertainties arising from the dispute declared by the unions as well as pending litigation regarding the wage curve agreement. In this regard, employee job evaluation processes are still in progress for the wage curve dispute. The ultimate outcome of these matters cannot presently be determined and no provision for any liability that may result has been made in the financial statements.

## **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

19. 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**

20. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages ... to ... of the annual report.
21. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the *National Treasury Framework for managing programme performance information (FMPPPI)*.

The reliability of the information in respect of the selected programmes is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).

22. There were no material findings on the annual performance report concerning the usefulness and reliability of the information.

### **Additional matter**

23. Although no material findings concerning the usefulness and reliability of the performance information were identified in the annual performance report, I draw attention to the following matter below.

### **Achievement of planned targets**

24. Of the total number of 222 targets planned for the year, 52 were not achieved. This represents 26% of total planned targets that were not achieved. This was due to lack of effective monitoring of project implementation plans and timely identification of under-performance against service delivery targets.

### **Compliance with laws and regulations**

25. 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:

### **Annual financial statements**

26. 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 non-current assets and accumulated surplus identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements and or supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

### **Procurement and contract management**

27. Awards were made to providers who are persons in the service of the municipality or other state institutions in contravention of section 112(j) of the MFMA and MSCMR 44. Furthermore, the providers failed to declare that he/she was in the service of the municipality, as required by MSCMR 13(c).
28. Bids were not always evaluated by bid evaluation committees which were composed of officials from the departments requiring the goods or services and at least one SCM practitioner of the municipality as required by MSCMR 28(2).
29. Sufficient appropriate audit evidence could not be obtained that contract and quotations were only awarded to providers whose tax matters have been declared to be in order as required by MSCMR 43.

### **Asset management**

30. The accounting officer did not take reasonable steps to ensure that the municipality had and maintained a management and internal control system that accounted for assets as required by section 63(2)(a) and (c) of the MFMA.

### **Expenditure management**

31. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA.

### **Internal control**

32. 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 basis for qualified opinion and the findings on compliance with laws and regulations included in this report.

## **Leadership**

33. The accounting officer did not exercise adequate oversight over financial reporting and compliance as well as internal control. In this regard, the accounting officer did not ensure that the municipality is able to prepare credible financial reports that are supported and evidenced by reliable information.

## **Financial management**

34. The accounting officer did not implement proper processes to communicate timely and relevant information to those charged with governance, in that monthly reporting and reconciliation processes were not at desired levels. In addition records management and review processes were not designed and implemented in a manner to improve accountability and credibility in financial and compliance reporting.

Pietermaritzburg

30 November 2013



**A U D I T O R - G E N E R A L**  
**S O U T H   A F R I C A**

*Auditing to build public confidence*