

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

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the financial statements of the Jozini Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2014, 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, 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, 2013 (Act No. 2 of 2013) (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 conducting the 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. Because of the matters described in the basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer opinion

Property, plant and equipment

4. The municipality did not review the residual values and useful lives of property, plant and equipment (PPE) in accordance with GRAP 17 *Property, plant and equipment*. Consequently, PPE stated at R212,39 million and its related expenditure was misstated by an undetermined amount. I was not able to determine the correct net carrying amount of PPE, as it was impracticable to do so.

Revenue from non-exchange transactions

5. I was unable to obtain sufficient appropriate audit evidence that management had properly accounted for all grant revenue for the current and prior year, due to the status of the accounting records. I was unable to confirm the grant revenue by alternative means. Consequently, I was unable to determine whether any adjustment to grant revenue stated at R131,13 million and the related unspent conditional grant liability stated at R8,43 million in the financial statements was necessary.



6. The municipality did not recognise all outstanding amounts meeting the definition of revenue, in accordance with GRAP 23 *Revenue from non-exchange transactions*. As the municipality did not maintain adequate records of property rates charged, I was not able to determine the full extent of the misstatement of revenue, as it was impracticable to do so.

Irregular expenditure

7. The municipality made payments in contravention of the supply chain management requirements that were not included in irregular expenditure amounting to R93,04 million in note 27 to the financial statements. As the municipality did not have adequate controls in place and did not maintain complete records and schedules, misstatements were identified during the audit. These misstatements were not adequately adjusted and no evidence was provided that the entire population had been evaluated. I was not able to determine the full extent of the impact on irregular expenditure, as it was impracticable to do so.

Expenditure

8. I was unable to obtain sufficient appropriate audit evidence that management had properly accounted for all expenditure for the current year, due to the status of the accounting records. I was unable to confirm the expenditure by alternative means. Consequently, I was unable to determine whether any adjustment to expenditure stated at R75,14 million in the financial statements was necessary.

Employee Costs

9. System errors resulted in material differences between the payroll system, general ledger, trial balance and the financial statements of the municipality. Consequently, I was unable to confirm whether the financial statements are fairly presented due to the effect of the errors. Furthermore, I was unable to obtain sufficient appropriate audit evidence that management had properly accounted for all employee costs for the current year, due to the status of the accounting records. I was unable to confirm the employee costs by alternative means. Consequently, I was unable to determine whether any adjustment to employee costs stated at R29,73 million in the financial statements was necessary.

Payables

10. The municipality did not recognise all outstanding amounts meeting the definition of a liability, in accordance with GRAP 1 *Presentation of financial statements*. As the municipality did not maintain adequate records of retentions held at year-end. Consequently, retentions of R14,51 million disclosed as part of payables in note 8 to the financial statements was misstated by an undetermined amount. I was not able to determine the full extent of the misstatement of payables, as it was impracticable to do so.

Receivables and impairment

11. Included in trade receivables is an impairment provision of R41,89 million as disclosed in note 2 and 3 to the financial statements, which does not agree to the schedule amounting to R43,07 million. The municipality did not calculate the provision based on the risk profile of each debtor. I was unable to confirm the impairment provision by alternative means. Consequently I was unable to determine whether any adjustment to the trade receivables stated at R6,90 million in the financial statements was necessary.
12. The municipality did not recognise value added tax (VAT) on the accrual basis as required by GRAP 1 *Presentation of Financial Statements*. VAT was incorrectly recognised on the payments basis. As the municipality did not maintain adequate records of VAT, I was not able to determine the full extent of the misstatement of receivables, as it was impracticable to do so.

Commitments

13. I was unable to obtain sufficient appropriate audit evidence that management had properly accounted for all commitments for the current year, due to the status of the accounting records. I was unable to confirm the commitments by alternative means. Consequently, I was unable to determine whether any adjustment to commitments stated at R4,15 million in note 34 to the financial statements was necessary.

Employee benefit obligation

14. I was unable to obtain sufficient appropriate audit evidence that management had properly accounted for the employee benefit obligation, due to the status of the accounting records as information was not provided to support the valuation calculation prepared by the management expert. I was unable to confirm the employee benefit obligation, by alternative means. Consequently, I was unable to determine whether any adjustment to the employee benefit obligation, stated at R1,30 million in the financial statements was necessary.

Disclaimer of opinion

15. Because of the significance of the matters described in the basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

Additional matter

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

Unaudited disclosure notes

17. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

18. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings on the reported performance information against predetermined objectives for selected objectives presented in the annual performance report, non-compliance with legislation as well as internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

19. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected objectives presented in the annual performance report of the municipality for the year ended 30 June 2014:
- KPA2: Improved Service Delivery and Infrastructure Investment on pages x to x
 - KPA3: Sustainable Economic Development on pages x to x
 - KPA5: Municipal Financial Viability and Management on pages x to x
 - KPA6: Spatial Planning and Environmental Management on pages x to x

20. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
21. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned objectives. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the *National Treasury's Framework for managing programme performance information* (FMPPI).
22. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
23. The material findings in respect of the selected objectives are as follows:

Improved Service Delivery and Infrastructure Investment, Sustainable Economic Development, Municipal Financial Viability and Management and Spatial Planning and Environmental Management

Usefulness of reported performance information

Consistency of objectives, indicators and targets

24. Section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000 (MSA) requires the integrated development plan (IDP) to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 100% of the reported objectives, indicators and targets were not consistent with those in the approved IDP. This was due to senior staff at the municipality not being aware of the contents of the IDP, their responsibilities in terms of performance reporting and the lack of understanding and implementation of the performance management system, MSA and the National Treasury Framework for Managing Programme Performance Information (FMPPI).

Measurability of indicators and targets

Performance targets not specific, measurable and time bound and indicators not well defined and verifiable

25. The FMPPI requires the following:
 - Performance targets must be specific in clearly identifying the nature and required level of performance. A total of 100% of the targets were not specific.
 - Performance targets must be measurable. I could not measure the required performance for 100% of the targets.
 - The period or deadline for delivery of targets must be specified. A total of 100% of the targets were not time bound.
 - Performance indicators must be well defined by having clear data definitions so that data can be collected consistently and is easy to understand and use. A total of 100% of the indicators were not well defined.
 - Performance indicator must be verifiable, meaning that it must be possible to validate the processes and systems that produced the indicator. A total of 100% of the indicators were not verifiable.

26. This was due to a lack of proper systems and processes and formal standard operating procedures or documented system descriptions.

Relevance of indicators

Performance indicators not relevant

27. The FMPPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. A total of 100% of the indicators did not relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives as per the five-year IDP. This was because proper performance planning and management practices had not been developed and implemented to provide for the development of performance indicators and targets included in the IDP.

Reliability of reported performance information

Validity, accuracy and completeness

28. The FMPPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations as to the selected indicators and targets I considered necessary to satisfy ourselves as to the reliability of the reported performance information. The auditee's records did not permit the application of alternative audit procedures. This was due to limitations placed on the scope of our work by the absence of information systems, lack of proper record keeping and no employee responsible for managing performance information.

Additional matter

29. I draw attention to the following matter below. This matter does not have an impact on the predetermined objectives audit findings reported above.

Achievement of planned targets

30. Refer to the annual performance report on pages x to x for information on the achievement of the 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 for the selected objectives reported in paragraphs x to x of this report.

Compliance with legislation

31. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Strategic planning and performance management

32. The annual performance report for the year under review did not include a comparison with the previous financial year as required by section 46 (1)(b) of the MSA.

Annual financial statements

33. 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 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 disclaimer audit opinion.

Procurement and contract management

34. Sufficient appropriate audit evidence could not be obtained that goods and services with a transaction value of below R200 000 were procured by means of obtaining the required price quotations, as required by Supply Chain Management (SCM) regulation 17(a) and (c).
35. Sufficient appropriate audit evidence could not be obtained that goods and services of a transaction value above R200 000 were procured by means of inviting competitive bids, as required by SCM regulation 19(a).
36. Invitations for competitive bidding were not always advertised for a required minimum period of days, as required by SCM regulation 22(1) and 22(2).
37. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded only to bidders who submitted 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).
38. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
39. The contract performance and monitoring measures and methods were insufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA.
40. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality did not disclose such interest, as required by SCM regulation 46(2)(e) and the code of conduct for councillors issued in terms of the MSA.

Human resource management and compensation

41. Sufficient appropriate audit evidence could not be obtained that the annual report of the municipality reflected information on compliance with prescribed minimum competencies as required by the Regulations on Minimum Competency Levels regulation 14(2)(b).
42. Sufficient appropriate audit evidence could not be obtained that the competencies of financial and supply chain management officials were assessed in a timely manner in order to identify and address gaps in competency levels as required by the Municipal Regulations on Minimum Competency Levels regulation 13.
43. Sufficient appropriate audit evidence could not be obtained that the municipality submitted a report on compliance with prescribed competency levels to the National Treasury and relevant provincial treasury as required by the Regulations on Minimum Competency Levels regulation 14(2)(a).

Expenditure management

44. Sufficient appropriate audit evidence could not be obtained that payments from the municipality's bank account were approved by the accounting officer and the chief financial officer, as required by section 11(1) of the MFMA.

Conditional grants received

45. Sufficient appropriate audit evidence could not be obtained that the Municipal Infrastructure Grant (MIG), Municipal Systems Improvement Grant (MSIG) and Local Government Financial



Management Grant (LGFMG) allocations, were spent in accordance with the applicable grant framework, section 16(1) of the DoRA.

Consequence management

46. Unauthorised and irregular 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)(ii) of the MFMA.
47. Irregular expenditure was not always recovered from the liable person, as required by section 32(2) of the MFMA.
48. Council certified irregular expenditure as irrecoverable without having conducted an investigation to determine the recoverability of the expenditure, in contravention of section 32(2)(a)(ii) of the MFMA.
49. Allegations of fraud, corruption, favouritism, unfair or irregular practice and failure to comply with the supply chain management system laid against officials were not investigated by the accounting officer, as required by Municipal supply chain management regulation 38(1)(b).

Waste management

50. The municipality operated their waste disposal site without a waste management licence or permit in contravention of section 20(b) of the National Environmental Management: Waste Act, 2008 (Act No. 59 of 2008) (NEMWA) and section 20(1) of the Environmental Conservation Act, 1989 (Act No. 73 of 1989).

Internal control

51. 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 disclaimer of opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

52. The leadership did not implement effective oversight over the review of the financial statements and annual performance report prior to submission for audit. Furthermore, compliance with laws and regulations was not effectively monitored by leadership throughout the financial year.

Financial and performance management

53. Senior management did not implement proper record keeping to ensure that information was accessible and available to support financial and performance reporting. The ineffective monitoring of compliance with laws and regulations and with municipal policies and procedures resulted in errors in daily and monthly processing and reconciling of financial and performance information. These errors were not detected and corrected on a timely basis, resulting in material misstatements in the financial statements and the annual performance report.

Governance

54. The municipality did not effectively implement the recommendations of internal audit and audit committee.



OTHER REPORT

Investigation

55. The municipality performed an investigation which covered the period 1 July 2013 to 30 June 2014. The investigation was initiated based on an allegation of possible misappropriation of the municipality's assets. The outcome of the investigation is expected by January 2015.

Auditor-General
Pietermaritzburg
28 November 2014



AUDITOR-GENERAL
SOUTH AFRICA

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