

Auditor-General of South Africa

uPhongolo Municipality Audit report 2014-15

Report of the auditor-general to the KwaZulu-Natal Provincial Legislature and the Council on uPhongolo Municipality

Report on the financial statements

Introduction

1. I have audited the financial statements of the uPhongolo Municipality set out on pages xxx to xxx, which comprise, the statement of financial position as at 30 June 2015, the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget information with actual information for the year then ended, as well as 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, 2014 (Act No. 10 of 2014) (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 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

Value Added Tax

6. I was unable to obtain sufficient appropriate audit evidence as to whether Value Added Tax (VAT) and the relevant financial disclosures had been properly recorded and completely accounted for, for all expenditure transactions, due to limitations in the municipality's internal controls over the capturing, claiming and recording of input and output VAT for the current financial year. Consequently, I was not able to determine the full extent of the misstatement of VAT income/expenditure and penalties, as it was impracticable to do so.

Qualified opinion

7. In my opinion, except for the effects of the matter described in the basis for qualified opinion paragraph, the financial statements present fairly, in all material respects, the financial position of the uPhongolo Municipality as at 30 June 2015 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

8. I draw attention to the matters below.

Material losses/impairments

9. As disclosed in note 32 to the financial statements, material electricity losses of R3,93 million (5,40 million kilowatts) (2014: R2,23 million - 3,33 million kilowatts) was incurred as a result of distribution losses.
10. As disclosed in note 5 to the financial statements, the municipality made a material provision for the impairment of receivables from exchange transactions amounting to R51,87 million (2014: R44,49 million) due to poor collection of service debtor accounts.

Report on other legal and regulatory requirements

11. 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 findings on the reported performance information against predetermined objectives for selected objectives presented in the annual performance report, compliance with legislation and 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

12. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the basic service delivery and cross cutting measures objectives, presented in the annual performance report of the municipality for the year ended 30 June 2015.
13. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
14. 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).
15. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
16. The material finding in respect of Objective F: Cross cutting measures is as follows:

Cross cutting measures

Reliability of reported performance information

17. The FMPPI requires municipality's 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. Significantly important targets were not reliable when compared to the source information or evidence provided. This was due to a lack of standard operating procedures and documented system descriptions for the accurate recording of actual achievements.

Basic service delivery

18. I did not identify any material findings on the usefulness and reliability of the reported performance information for Objective A: Basic service delivery.

Compliance with legislation

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

Procurement and contract management

20. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulation 17(a) and (c).

21. Quotations were accepted from prospective providers who are not registered on the list of accredited prospective providers and do not meet the listing requirements prescribed by the SCM policy in contravention of SCM regulations 16(b) and 17(b).
22. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).
23. Invitations for competitive bidding were not always advertised for a required minimum period of days, as required by SCM regulations 22(1) and 22(2).
24. Quotations were awarded to bidders based on points given for criteria that differed from those stipulated in the original invitation for quotations, in contravention of SCM regulations 21(b) and 28(1)(a) as well as the Preferential Procurement regulations.
25. 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, as required by SCM regulation 13(c).
26. Awards were made to providers who are in the service of other state institutions, in contravention of section 112(j) of the MFMA and SCM regulation 44. Similar awards were identified in the prior year and no effective steps were taken to prevent or combat the abuse of the procurement process, in accordance with SCM regulation 38(1).
27. Contracts and quotations were awarded to providers whose tax matters had not been declared by the South African Revenue Service (SARS) to be in order, as required by SCM regulation 43.

Expenditure management

28. Money owing by the municipality was not always paid within 30 days or upon an agreed period, as required by sections 65(2)(e) of the MFMA.
29. Reasonable steps were not taken to prevent unauthorised, irregular as well as fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Value added tax

30. Input VAT was claimed on non-VAT supplier invoices and exempt supplies, contrary to the requirements of section 12 of the Value Add Tax Act of South Africa, 1991 (Act No. 89 of 1991)(VAT Act).
31. VAT 201 returns were not submitted within the timeframes, as prescribed in section 28 of the VAT Act.

32. VAT registration numbers on supplier invoices/quotations did not agree to the SARS e-filing website and the municipality's VAT registration number does not appear on supplier tax invoices, as required by section 20 of the VAT Act.
33. Reasonable steps were not implemented to ensure that input VAT was claimed on valid supplier tax invoices, as required by section 20 of the VAT Act.
34. Output VAT not was not declared on overpayments, as required by section 8(27) of the VAT Act.

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 of the MFMA. Material misstatements of current assets and liabilities 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 supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

Internal control

36. I considered internal control relevant to my audit of the financial statements, performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for qualified opinion, the findings on the performance report and the findings on compliance with legislation included in this report.

Leadership

37. The municipality's oversight processes were not adequate to ensure compliance with SCM processes. Vacancies in the key post of Accounting officer as well as in the finance and SCM sections also contributed to the breakdown in internal control mechanisms.

Financial and performance management

38. The accounting officer did not implement adequate monitoring and evaluation processes to ensure that all requirements of laws and regulations are complied with timeously. Furthermore, due to inadequate monitoring, instances of performance and financial related non-compliance were not identified timeously to implement corrective measures, as was evidenced by the material corrections required to the financial statements and weaknesses in the reported performance information.

Governance

39. The effectiveness of the risk assessment, internal audit function and the audit committee were compromised as management failed to implement the recommendations of internal audit timeously. Furthermore, due to late submission by management, the financial statements and performance information, was not adequately reviewed for accuracy and completeness. This was evidenced by the errors identified during the auditing process.

Investigations

40. Investigations into control deficiencies in the municipality's SCM process were conducted during the year relating to two payments made for goods and services where the goods or services were not received. One case is being investigated by the South African Police services and the other by the municipality's attorneys.
41. Council are investigating a case relating to the salary payments of a section 56 staff member and have finalised another case relating to abuse of municipal resources. The latter case resulted in an official's services being terminated.

Auditor-General

Pietermaritzburg

27 November 2015



Auditing to build public confidence