



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

Auditor-General of South Africa

Mpofana Municipality - audit
report 2015-16

Report of the auditor-general to the KwaZulu-Natal Provincial Legislature and the council on Mpofana Municipality

Report on the financial statements

Introduction

1. I was engaged to audit the financial statements of the Mpofana Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2016, the statement of financial performance, statement of changes in net assets, and cash flow statement and statement of comparison of budget 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, 2015 (Act No. 1 of 2015) (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 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 of opinion

Financial statements submitted without complete and accurate underlying records

4. I was unable to obtain sufficient appropriate audit evidence regarding the financial statements as a whole, as the financial statements were presented for audit purposes without accurate and complete underlying accounting records. I was unable to audit the financial statements by alternative means. Consequently, I was unable to determine whether any adjustment relating to the financial statements as a whole was necessary.

Restatement in corresponding figures

5. I was unable to obtain sufficient appropriate audit evidence for the restatement of the corresponding figures for the financial statements as a whole, as the restatements was made to rectify prior year misstatements, but the restatements could not be substantiated by supporting audit evidence. I was unable to confirm the restatements by alternative means. Consequently, I was unable to determine whether any adjustment to the corresponding figures in financial statements as a whole was necessary.

Property, plant and equipment

6. I was unable to obtain sufficient appropriate audit evidence for the restatement of the corresponding figure of R4,71 million for other property plant and equipment in the financial statements. As described in note 10, the restatement was made to rectify a prior year misstatement, but the restatement could not be substantiated by supporting audit evidence. I was unable to confirm the restatement by alternative means. Consequently, I was unable to determine whether any adjustment to the other property plant and equipment corresponding figure stated at R8,32 million in the financial statements was necessary.

Investment property

7. I was unable to obtain sufficient appropriate audit evidence that disposals of investment property for the prior year had been properly accounted for due to the status of the accounting records. I was unable to confirm the investment property by alternative means. Consequently, I was unable to determine whether any adjustment to investment property stated at R21,2 million.(2015: R19,99 million) disclosed in note 9 to the financial statements was necessary.

Payables from exchange transactions

8. I was unable to obtain sufficient appropriate audit evidence that management had fully accounted for all payables from exchange transactions due to the lack of supporting documentation for the current year's payables. I was unable to confirm the payables by alternative means. Consequently, I was unable to determine whether any adjustment to payables from exchange transactions stated at R31,39 million (2015: R11,87 million) disclosed in note 14 to the financial statements was necessary.

Value-added tax receivable

9. I was unable to obtain sufficient appropriate audit evidence that value-added tax (VAT) for the current year has been properly accounted for, due to the status of the accounting records. I was unable to confirm the VAT by alternative means. Consequently, I was unable to determine whether any adjustment to VAT stated at R2,67 million in the financial statements was necessary.

Prior period errors disclosure

10. I was unable to obtain sufficient appropriate audit evidence for the prior period errors disclosed in note 42, as the supporting information was not provided. I was unable to confirm these disclosures by alternative means. Consequently, I was unable to determine whether any adjustments relating to the prior period errors disclosed in the financial statements were necessary.

Cash flow statement

11. The municipality did not prepare the statement of cash flows in accordance with GRAP 2 Cash Flow Statements. Cash flows from operating activities were misstated as finance costs and changes in working capital were not correctly accounted for. Cash flows from investing activities were materially misstated as a result of invalid movements in investment property. Consequently, cash flows from investing activities was understated by an amount of R4,47 million.

Irregular expenditure

12. The municipality made payments in contravention of the municipal supply chain management (SCM) legislation that were not included in irregular expenditure of R2,1 million as disclosed in note 46 to the financial statements. Adequate systems and controls were not in place to ensure that all irregular expenditure was accounted for. I was not able to determine the full extent of the irregular expenditure as it was impracticable to do so.

Statement of Changes in Net Assets

13. I was unable to obtain sufficient appropriate audit evidence that management had properly accounted for the prior year adjustment of R7,87 million and fair value adjustment of R1,21 million in the statement of changes in net assets. I could not confirm the amounts by alternative means. Consequently, I was unable to determine whether any adjustment to the statement of changes in net assets stated at R74,2 million in the financial statements was necessary.

Expenditure and payables from exchange transactions

14. The municipality did not recognise all outstanding amounts meeting the definition of a liability, in accordance with GRAP 1 *Presentation of financial statements*. The municipality did not maintain adequate records of outstanding payments for goods and services received for the prior year and did not recognise expenditure in the correct accounting period. I was not able to determine whether any adjustments relating payables from exchange transactions and expenditure as it was impracticable to do so, consequentially there is an impact on accumulated surplus.

Aggregation of misstatements

15. The financial statements were materially misstated due to the cumulative effect of numerous individual, uncorrected misstatements in the following items included in the statement of financial position and the statement of financial performance:

- Revenue from service charges, reflected as R51,72 million were understated by R610 000 as a result of incorrect treatment of output VAT. Expenditure as reflected as R32,57 million was overstated by R800 000 as a result of incorrect treatment of input VAT.

In addition, I was unable to obtain sufficient appropriate audit evidence and was unable to confirm the following items by alternative means:

- Fair value adjustment of R1,21 million, Loss on disposal of assets of R70 854 and profit on disposal of assets of R213 545 as included in the statement of financial performance.

Consequently, I was unable to determine whether any further adjustment to these items was necessary.

Electricity losses

16. I was unable to obtain sufficient appropriate audit evidence for the R7,88 million (2015: R6,87 million) disclosed as electricity losses, in note 49 to the financial statements due to inadequate systems and processes for the recording and monitoring of these losses. There were no satisfactory alternative audit procedures that I could perform in this regard. Consequently, I was unable to determine whether any adjustment relating to the electricity losses disclosed in note 49 to the financial statements was necessary.

Disclaimer of opinion

17. 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.

Emphasis of matter

18. I draw attention to matter below.

Going concern

19. As disclosed in note 50 to the financial statements, the municipality did not have sufficient cash resources to realise the unspent conditional grant liability. The unspent conditional grant liability amounted to R19,7 million as per note 18 and the available cash balance amounted to R4,93 million as per note 8.

Additional matter

20. I draw attention to the matter below.

Unaudited disclosure notes

21. 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 financial statements and accordingly I do not express an opinion thereon.

Report on other legal and regulatory requirements

22. 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

23. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the basic service delivery objective presented in the annual performance report of the municipality for the year ended 30 June 2016.
24. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
25. I evaluated the usefulness of the reported performance information to determine whether it 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.
26. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
27. I did not identify any material findings on the usefulness and reliability of the reported performance information for the basic service delivery objective.

Additional matters

28. I identified no material findings on the usefulness and reliability of the reported performance information for the selected objectives, however, I draw attention to the following matters:

Achievement of planned targets

29. The annual performance report on pages x to x includes information on the achievement of the planned targets for the year

Adjustment of material misstatements

30. I identified material misstatements in the annual performance report submitted for auditing on the reported performance information for basic service delivery. As management subsequently corrected the misstatements, I did not raise any material findings on the usefulness and reliability of the reported performance information.

Compliance with legislation

31. I performed procedures to obtain evidence that the municipality 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;

Annual financial statements

32. 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 non-current assets, current assets, revenue, expenditure and disclosure items 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 disclaimer audit opinion.

Procurement and contract management

33. 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).
34. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).
35. Awards were made to providers who are in the service of other state institutions or whose principal shareholders are in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulations 44. Similar awards were identified in the prior year and no effective steps were taken to prevent or combat the abuse of the SCM process in accordance with SCM regulation 38(1).
36. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
37. 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.
38. Sufficient appropriate audit evidence could not be obtained that quotations were awarded to bidders based on points given for criteria that were stipulated in the original invitation for quotations, as required by SCM regulations 21(b) and 28(1)(a) and Preferential Procurement Regulations.

Expenditure management

39. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
40. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.
41. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred, accounted for creditors and for payments made, as required by section 65(2)(b) of the MFMA.

Conditional grants

42. The municipality did not evaluate its performance in respect of programmes funded by the municipal infrastructure grant allocation, as required by section 12(5) of the DoRA.

Revenue management

43. An effective system of internal control for debtors was not in place, as required by section 64(2)(f) of the MFMA.

Asset management and liability management

44. An effective system of internal control for assets and liabilities was not in place, as required by section 63(2)(c) of the MFMA.

Consequence management

45. Unauthorised, irregular and fruitless and wasteful 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.

Internal control

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

Leadership

47. Leadership did not exercise adequate oversight responsibility regarding financial reporting and compliance with laws and regulations. In this regard, leadership did not ensure that policies and procedures as well as action plans were effectively applied and monitored. This was as a result of vacancies in key positions.

Financial management

48. Management did not ensure that regular, accurate and complete financial and performance reports were prepared, which were supported and evidenced by reliable information. This was due to incapacity and key vacancies within the financial management unit.

Governance

49. The risk assessment processes and reviews were not adequate to ensure that key financial and compliance risks were mitigated and responded to in good time by management. Furthermore, the legislative responsibilities of the internal audit and the audit committee were not monitored to ensure that these objectives were met during the year under review.

Other report

50. I draw attention to the following engagement that could potentially impact on the municipality's financial, performance and compliance related matters. My opinion is not modified in respect of this engagement that is in progress.

Investigation

51. The municipality is currently performing an investigation for the 2016-17 period, which was initiated based on an allegation of possible misappropriation of the municipality's assets and financial misconduct during 2016.

Auditor-General

Pietermaritzburg

30 November 2016



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