



Report of the auditor-general to the North West provincial legislature and the council on the Madibeng Local Municipality

Report on the financial statements

Introduction

1. I was engaged to audit the financial statements of the Madibeng Local Municipality as set out on pages XX to XX, which comprise the statement of financial position as at 30 June 2016, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts 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 these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA standards of GRAP), the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA), 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 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

Cash and cash equivalents

4. I was unable to obtain sufficient appropriate audit evidence for cash and cash equivalents as the municipality could not provide adequate substantiating records for the unreconciled difference between the municipality's cash book and bank statement balances for the current and prior year. Furthermore, I identified reconciling items of R126 510 882 that have not been captured in the financial system. I was unable to confirm the cash and cash equivalents by alternative means. Consequently, I was unable to determine whether any adjustments relating to cash and cash equivalents of R65 626 995 (2015: R58 957 539) and the bank overdraft of R94 862 046 disclosed in the statement of financial position and note 12 to the financial statements or any other accounts affected, were necessary.

Revenue from exchange transactions

5. The municipality did not adequately account for revenue from service charges in accordance with GRAP 9 *Revenue from exchange transactions* due to an inadequate billing process. I was unable to confirm the revenue from service charges by alternative means. Consequently, I was unable to determine the full extent of this misstatement of revenue from service charges of R636 380 735 disclosed in note 22 and consumer receivables of R196 115 791 disclosed in note 11 to the financial statements.

Revenue from non-exchange transactions

6. I was unable to obtain sufficient appropriate audit evidence for property rates revenue of R292 796 357, due to discrepancies identified in the valuation roll and the billing system as well as an inadequate billing process. I was unable to confirm the property rates revenue by alternative means. Consequently, I was unable to determine whether any adjustments relating to property rates revenue of R292 796 357 recognised in the statement of financial performance and receivables from non-exchange transactions of R110 679 138 recognised in the statement of financial position, were necessary.

Bulk purchases

7. I was unable to obtain sufficient appropriate audit evidence for bulk purchases of electricity of R362 104 042 and water of R122 816 063 disclosed in note 36 to the financial statements, due to a lack of proper substantiating accounting records. I was unable to confirm these bulk purchases by alternative means. Consequently, I was unable to determine whether any adjustment relating to bulk purchases of R515 693 414 recognised in the statement of financial performance, was necessary.

Distribution losses

8. I was unable to obtain sufficient appropriate audit evidence for bulk electricity and water distribution losses due to an inadequate billing process and the limitation on the testing of bulk purchases. The extent of these distribution losses could not be confirmed by alternative means. Consequently, I was unable to determine whether any adjustments relating to electricity distribution losses of R310 187 118 and water distribution losses of R130 386 620 disclosed in note 50 to the financial statements, were necessary.

Irregular expenditure

9. Section 125 of the MFMA requires the disclosure of irregular expenditure incurred. The municipality made payments of R28 766 166 (2015: R15 400 014) in contravention of the supply chain management requirements, which were not included in the irregular expenditure disclosed. In addition, I was unable to obtain sufficient appropriate audit evidence to confirm that awards of R50 668 401 (2015: R95 673 054) were made in terms of the supply chain management requirements. As the municipality did not quantify the full extent of the irregular expenditure, it was impracticable to determine the resultant understatement of irregular expenditure of R762 462 954 disclosed in note 47 to the financial statements.

Aggregation of immaterial uncorrected misstatements

10. I was unable to obtain sufficient appropriate audit evidence regarding the following items recognised in the statement of financial performance, which had a cumulative effect on the financial statements:
 - Repairs and maintenance of R7 833 393 included in the disclosed total of R115 829 481.
 - Contracted services of R6 901 143 included in the disclosed total of R129 059 580.



- Grants and subsidies paid of R1 785 808 included in the disclosed total of R22 609 654.
- General expenditure of R14 125 284 included in the disclosed total of R183 709 099.

11. I was unable to confirm these items by alternative means. Consequently, I was unable to determine whether any adjustments to these items, were necessary.

Disclaimer of opinion

12. 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 matters

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

Unauthorised and fruitless and wasteful expenditure

14. As disclosed in note 45 to the financial statements, unauthorised expenditure of R796 321 559 incurred in the current year and R1 169 383 204 in respect of prior years, had not yet been dealt with in accordance with section 32 of the MFMA.

15. As disclosed in note 46 to the financial statements, fruitless and wasteful expenditure of R7 330 977 incurred in the current year and R8 033 260 in respect of prior years not yet been dealt with in accordance with section 32 of the MFMA.

Restatement of corresponding figures

16. As disclosed in note 41 to the financial statements, the corresponding figures for 30 June 2015 have been restated as a result of an error discovered during 2016 in the financial statements of the Madibeng Local Municipality at, and for the year ended 30 June 2015.

Significant uncertainty

17. As disclosed in note 39 to the financial statements, the municipality is the defendant in a number of civil claims. The municipality is opposing these claims. The ultimate outcome of these matters cannot presently be determined and hence no provision for any liability that may result, has been made in the financial statements.

Material losses and impairments

18. As disclosed in note 28 to the financial statements, debt impairment of R159 241 289 and bad debts written off of R69 512 132, were incurred.

19. As disclosed in note 32 to the financial statements, material losses of R19 330 166 were incurred as a result of impairment of assets.

Going concern

20. As disclosed in note 43 to the financial statements, the Madibeng Local Municipality had a deficit for the year of R645 132 206 and, as of 30 June 2016, the municipality's current liabilities exceeded its current assets by R175 854 364. These conditions indicate the existence of a material uncertainty that may cast doubt on the municipality's ability to operate as a going concern.

Additional matter

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

Unaudited supplementary schedules

22. The supplementary information set out on pages XX to XX does 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

23. 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 key development areas 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

24. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected key performance areas (KPA) presented in the annual performance report of the municipality for the year ended 30 June 2016:

- KPA 2: Basic service delivery presented under objectives 1 – 7 on pages XX to XX
- KPA 3: Local economic development presented under objective 8 on pages XX to XX

25. I evaluated the usefulness of the reported performance information to determine whether it was consistent with the planned key performance areas. 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).

26. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.

27. The material findings in respect of the selected key performance areas are as follows:

KPA 2: Basic service delivery

Usefulness of reported performance information

28. Section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) requires the service delivery budget implementation plan (SDBIP) 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 objectives, 29% of the indicators and 24% of the targets reported on, were not consistent with those in the approved SDPIB.

29. Section 54(1)(c) of the MFMA determines that the SDBIP adopted by the municipal council may be amended only if the council approves an adjustments budget. Changes to SDBIP in the year have to be made in accordance with the process as prescribed in section 28 of the MFMA. Material changes were made to the indicators and targets in the annual performance report, without adoption by the municipal council.

30. The FMPPI requires that indicators be well defined and verifiable and targets be specific, measurable and time bound:

- A total of 27% of the indicators were not well defined.



- A total of 100% of the indicators were not verifiable.

Reliability of reported performance information

31. The FMPPI 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 I considered necessary to satisfy myself as to the reliability of the reported performance information.

KPA 3: Local economic development

Usefulness of reported performance information

32. Section 41(c) of the MSA requires the SDBIP 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 objectives, 32% of the indicators and 47% of the targets reported on, were not consistent with those in the approved SDBIP.

33. Section 54(1)(c) of the MFMA determines that the SDBIP adopted by the municipal council may be amended only if the council approves an adjustments budget. Changes to the SDBIP in the year have to be made in accordance with the process as prescribed in section 28 of the MFMA. Material changes were made to the indicators and targets in the annual performance report, without adoption by the municipal council.

34. The FMPPI requires that indicators be well defined and verifiable and targets be specific, measureable and time bound:

- A total of 32% of the indicators were not well defined.
- A total of 100% of the indicators were not verifiable.

Reliability of reported performance information

35. The FMPPI 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. The reported performance information was not valid, accurate and complete when compared to the source information or evidence provided.

Additional matter

36. I draw attention to the following matter:

Achievement of planned targets

37. Refer to the annual performance report on page XX to XX 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 key performance areas reported in paragraphs XX to XX of this report.

Compliance with legislation

38. 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 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

39. The performance management system and related controls were inadequate as it did not describe and present the processes of performance planning, monitoring, measurement, review, reporting and improvement and how it is conducted, organised and managed, as required by section 38 of the MSA and regulation 7 of the Municipal planning and performance management regulations.
40. The performance management policies and procedures did not provide for steps of improvement where performance targets were not met, as required by section 41(1)(d) of the MSA.
41. Revisions to the SDBIP were not approved by the council as required by section 54(1)(c) of the MFMA.

Financial statements, performance and annual reports

42. 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 on non-current assets, current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records provided, but the uncorrected material misstatements and supporting records that could not be provided, resulted in the financial statements receiving a disclaimer opinion.
43. The 2014-15 annual report was not tabled in the municipal council within seven months after the end of the financial year, as required by section 127(2) of the MFMA.

Procurement and contract management

44. I could not obtain sufficient appropriate audit evidence that goods and services with a transaction value below R200 000 were procured using price quotations as required by SCM regulation 17(a) and (c).
45. I could not obtain sufficient appropriate audit evidence that goods and services with a transaction value above R200 000 were procured by inviting competitive bids, as required by SCM regulation 19(a).
46. I could not obtain sufficient appropriate audit evidence that deviations approved by the accounting officer were only if it was impractical to invite competitive bids, as required by SCM regulations 36(1).
47. I could not obtain sufficient appropriate audit evidence that bid specifications are unbiased and allowed all potential suppliers to offer their goods or services, as required by SCM regulation 27(2)(a).
48. I could not obtain sufficient appropriate audit evidence that invitations for competitive bidding were advertised for a required minimum period of days, as required by SCM regulations 22(1) and 22(2).
49. Sufficient appropriate audit evidence could not be obtained that bids were 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 SCM regulation 28(2).
50. I could not obtain sufficient appropriate audit evidence that contracts were awarded to bidders based on points given for criteria that were stipulated in the original invitation for bidding and quotations, as required by SCM regulations 21(b) and 28(1)(a) and the Preferential Procurement Regulations.
51. I could not obtain sufficient appropriate audit evidence that bid adjudication committees were always composed in accordance with SCM regulation 29(2).

52. I could not obtain sufficient appropriate audit evidence to determine whether awards were made to bidders other than those recommended by the bid evaluation committee as required by SCM regulation 29(5)(b).
53. I could not obtain sufficient appropriate audit evidence that the preference point system was applied in all procurement of goods and services above R30 000, as required by section 2(a) of the Preferential Procurement Policy Framework Act (PPPFA) and SCM regulation 28(1)(a).
54. I could not obtain sufficient appropriate audit evidence that contracts were awarded to suppliers based on preference points that were allocated and calculated in accordance with the requirements of the PPPFA and its regulations.
55. I could not obtain sufficient appropriate audit evidence obtained that contracts were awarded to bidders that scored the highest points in the evaluation process, as required by of section 2(1)(f) of PPPFA.
56. I could not obtain sufficient appropriate audit evidence that contracts were awarded only to bidders who submitted a declaration on whether they were employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
57. I could not obtain sufficient appropriate audit evidence that contracts were only extended or modified after tabling the reasons for the proposed amendment in the council of the municipality, as required by section 116(3) of the MFMA.
58. I could not obtain sufficient appropriate audit evidence that all extensions or modifications to contracts were approved by a properly delegated official, as required by SCM regulation 5.
59. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
60. The contract performance and monitoring measures and methods were insufficient to ensure effective contract management, in contravention of section 116(2)(c) of the MFMA.
61. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e).
62. Persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e).
63. I could not obtain sufficient appropriate audit evidence that contracts were only awarded to providers whose tax matters had been declared by the South African Revenue Service to be in order, as required by SCM regulation 43.

Expenditure management

64. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
65. I could not obtain sufficient appropriate audit evidence that payments from the municipality's bank account were approved by the accounting officer, the chief financial officer or a properly authorised official, as required by section 11(1) of the MFMA.
66. Reasonable steps were not taken to prevent unauthorised, irregular and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Revenue management

67. Revenue due to the municipality was not calculated on a monthly basis, as required by section 64(2)(b) of the MFMA.

Consequence management

67. 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.

Environmental management

68. The municipality did not exercise its legislative and executive authority of managing, monitoring and enforcing environmental related bylaws to promote a safe and healthy environment as required by sections 11(3)(l) and (m) of the MSA.

69. The municipality operated its wastewater treatment facility without a license in contravention of section 24(2)(a) of the National Environmental Management Act, 1998 (Act No. 107 of 1998) (NEMA) and section 22(1)(b) of the National Water Act, 1998 (Act No. 36 of 1998) (NWA).

70. The municipality's operational activities at its waste disposals sites and wastewater treatment facilities contravened or failed to comply with the requirements of a waste management license or the norms and standards as prescribed by sections 67(1)(f) and (h) of the NEMWA and sections 151(1)(c) and (i) of the NWA.

71. The municipality's waste management and disposal activities contravened or failed to comply with the requirements of section 28(1) of the NEMA, section 19 of the NWA and sections 16(1)(c) and (d) and 26(1)(b) of the NEMWA.

Internal control

72. I considered internal control relevant to my audit of the financial statements, the 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, the findings on the annual performance report and the findings on compliance with legislation included in this report.

Leadership

73. Leadership did not exercise adequate oversight responsibility regarding financial and performance reporting, compliance with key laws and regulations and related internal controls. Furthermore, the action plan to address prior year audit findings was not adequately implemented and monitored as numerous instances of repeat audit findings were identified which negatively impacts on the assurance level provided by leadership.

Financial and performance management

74. Management did not fully implement effective controls to ensure that information in the financial statements and the report on predetermined objectives were reliable before submission for audit. This was mainly evident in the limitation on bank reconciliations and the fact that the municipality could not provide evidence in support and information presented in the report on predetermined objectives. Furthermore, various instances of non-compliance with legislation were identified.

Governance

75. Although the municipality had a functioning audit committee and internal audit, recommendations by the internal audit and audit committee to address internal control deficiencies were not adequately implemented by the municipality, resulting in the internal control environment over performance reporting and compliance with laws and regulations being ineffective.



Other reports

76. 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 are in progress.

Investigation

77. An investigation by an independent firm on fraudulent payments made from the municipal bank account was still on-going at the reporting date.

Rustenburg

30 November 2016



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence