

Report of the auditor-general to the Western Cape Provincial Parliament and the council on the Kannaland Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Kannaland municipality set out on pages 3 to 88, which comprise the statement of financial position as at 30 June 2017, and the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion section of my report, the financial statements present fairly, in all material respects, the financial position of the Kannaland municipality as at 30 June 2017, and its financial performance and cash flows for the year then ended in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP), the requirements of the Division of Revenue Act of South Africa, 2016 (Act No. 3 of 2016 (DoRA) and the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA).

Basis for qualified opinion

Contingent liabilities

3. I was unable to obtain sufficient appropriate audit evidence for contingent liabilities as disclosed in note 49 to the financial statements, as not all external legal confirmations were received. I was unable to confirm by alternative means whether all contingent liabilities were recorded. Consequently, I was unable to determine whether any adjustments to contingent liabilities stated at R1,7 million in note 49 to the financial statements were necessary.

Property, plant and equipment

4. I was unable to obtain sufficient appropriate audit evidence for the impairment of other assets within property plant and equipment as disclosed in note 11 to the financial statements, as assets that were in poor condition were not assessed for impairment in accordance with GRAP 26 *Impairment of cash-generating assets*. I was unable to determine by alternative means the impact thereof on the net carrying amount of property, plant and equipment stated at R311,5 million in the financial statements, depreciation and amortisation stated at R10,6 million in the financial statements, impairment loss stated at R3,5 million in the financial statements and the surplus for the year stated at R7,8 million in the financial statements as it was impracticable to do so.

Taxes

5. I was unable to obtain sufficient appropriate audit evidence for the restatement of the corresponding figure for Value Added Tax(VAT) as disclosed in note 10 to the financial statements. The restatement was made to rectify a previous year misstatement, however restatement could not be substantiated by appropriate supporting audit evidence. I was unable to confirm the restatement by alternative means. Consequently, I was unable to determine whether any adjustments to the Taxes (VAT receivable) stated at R3 342 792 (2015-16: R981 946(VAT payable)) and any other accounts in the financial statements were necessary.

Irregular expenditure

6. I was unable to obtain sufficient appropriate audit evidence that all instances of irregular expenditure were disclosed in note 40.3 to the financial statements as the municipality did not maintain accurate and complete records for irregular expenditure. I was unable to confirm by alternative means that all irregular expenditure was recorded. Consequently, I was unable to determine whether any further adjustments to irregular expenditure stated at R 99,4 million (2015-16: R63,5 million) in note 40.3 to the financial statements were necessary.

Basis for the opinion

7. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of my report.
8. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) together with the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
9. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Emphasis of matters

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

Restatement of corresponding figures

11. As disclosed in note 34 to the financial statements, the corresponding figures for 30 June 2016 have been restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2017.

Material impairments

12. As disclosed in note 27 to the financial statements, an impairment of R10 million (2015-16: R7 million) was provided for on receivables from non-exchange transactions.
13. As disclosed in note 27 to the financial statements, an impairment of R17,3 million (2015-16: R14,3 million) was provided for on receivables from exchange transactions.

Material underspending of conditional grants

14. As disclosed in note 22,7 and 22,8 to the financial statements, the municipality underspent its conditional grants by R10,2million (2015-16: R8,9 million).

Material losses – water

15. As disclosed in note 40.4 to the financial statements, material water losses to the amount of R4,8 million, (2015-16: R3,4 million was incurred which represents 32.8% (2015-16: 26%) of total water purchased.

Other matters

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

Unaudited supplementary schedules

17. The supplementary information set out on pages 89 to 92 did 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.

Unaudited disclosure notes

18. 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.

Responsibilities of the accounting officer

19. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with SA Standards of GRAP and the requirements of the MFMA and 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.
20. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the accounting officer either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

21. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

22. A further description of my responsibilities for the audit of the financial statements is included in the annexure to the auditor's report.

Report on the audit of the annual performance report

Introduction and scope

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 material findings on the reported performance information against predetermined objectives for selected key performance areas presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
24. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators/measures included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
25. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected key performance areas presented in the annual performance report of the municipality for the year ended 30 June 2017:

Key performance area	Pages in the annual performance report
Key Performance Area 1: To provide access to reliable infrastructure that will contribute to a better quality of life for Kannaland citizens	10-14
Key Performance Area 7: To strive towards a financially sustainable municipality	28-41

26. I performed procedures to determine whether the reported performance information was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and 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 following key performance areas:
- Key Performance Area 1: To provide access to reliable infrastructure that will contribute to a better quality of life for Kannaland citizens
 - Key Performance Area 7: To strive towards a financially sustainable municipality.

Other matters

28. I draw attention to the matters below.

Achievement of planned targets

29. Refer to the annual performance report on pages 10 to 41 for information on the achievement of planned targets for the year and explanations provided for the under / overachievement of a number of targets.

Adjustment of material misstatements

30. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of Key Performance Area 7: To strive towards a financially sustainable municipality. As management subsequently corrected the misstatements, I did not raise any material findings on the usefulness and reliability of the reported performance information.

Report on audit of compliance with legislation

Introduction and scope

31. In accordance with the PAA and the general notice issued in terms thereof I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

32. The material findings on compliance with specific matters in key legislations are as follows:

Annual financial statements and annual performance report

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 qualified audit opinion.

34. The annual financial statements were not submitted for auditing within two months after the end of the financial year, as required by section 126(1)(a) of the MFMA.

35. The council failed to adopt an oversight report containing the council's comments on the annual report within the prescribed timelines, as required by section 129(1) of the MFMA.

36. The oversight report adopted by the council on the 2015-16 annual report was not made public, as required by section 129(3) of the MFMA.

Strategic planning and performance management

37. Amendments to the IDP were made without consultation with the district municipality as required by Regulation 3(6)(a) of the Municipal Planning and Performance Management Regulations, 2001.

Budget management

38. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R 24,7 as disclosed in note 40.1 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was as a result of spending in excess of the budget.
39. Unforeseen and unavoidable expenditure incurred by the municipality was not approved by the mayor as required by section 29(1) of the MFMA.

Expenditure management

40. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
41. Effective steps were not taken to prevent irregular expenditure amounting to R 35,9 million as disclosed in note 40.3 to the financial statements, as required by section 62(1)(d) of the MFMA. The full extent of the irregular expenditure could not be quantified as indicated in the basis for qualification paragraph. The majority of the disclosed irregular expenditure was caused by non-compliance with the Municipal Supply Chain Management Regulations, 2005.
42. Effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R2.1 million as disclosed in note 40.2 to the financial statements, as required by section 62(1)(d) of the MFMA. The majority of the fruitless and wasteful expenditure was caused by late payments of pay as you earn, VAT returns that were not submitted within the legislated time frames and the abuse of the acting allowance policy.

Grant management

43. The Municipal Infrastructure Grant allocation, was not spent in accordance with the applicable grant framework, in contravention of section 17(1) of the DoRA.

Human resource management

44. Municipal manager failed to disclose financial interests within 60 days from date of appointment, as required by Regulation 36(1)(a) of the Regulations on Appointment and Conditions of Employment of Senior Managers, 2014.

Procurement and contract management

45. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by Municipal Supply Chain Management Regulations, 2005 (SCM) regulations 17(a) and (c). Similar non-compliance was also reported in the prior year.
46. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).
47. Quotations were accepted from prospective providers who were not on the list of accredited prospective providers and did not meet the listing requirements prescribed by the SCM policy, in contravention of SCM regulations 16(b) and 17(b).

48. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2) (b) of the MFMA. Similar non-compliance was also reported in the prior year
49. Quotations were accepted from 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).
50. Some awards were made to providers who were in the service of other state institutions, in contravention of section 112(j) of the MFMA and SCM regulation 44. Similar non-compliance was reported in the previous year and the municipality did not take disciplinary action against the suppliers or officials involved.
51. Quotations were accepted from providers whose tax matters had not been declared by the South African Revenue Service to be in order, in contravention of SCM regulation 43. Similar non-compliance was also reported in the prior year.

Consequence management

52. Unauthorised 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) of the MFMA.
53. 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)(b) of the MFMA.
54. 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)(b) of the MFMA.

<h3>Other information</h3>

55. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report thereon and those selected key performance areas presented in the annual performance report that have been specifically reported on in the auditor's report.
56. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
57. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected key performance areas presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
58. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and re-issue an amended report as appropriate, however, if it is corrected this will not be necessary.

Internal control deficiencies

59. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

Leadership

60. Leadership did not provide adequate oversight regarding the implementation of action plans to address prior year audit findings and internal control deficiencies which has resulted in repeat audit findings in the area of financial reporting, the report on pre-determined objectives and compliance with laws and regulations. Sufficient oversight over the processes for the preparation of the underlying supporting schedules in support of the financial statements and annual performance report did not occur resulting in numerous material misstatements in the financial statements and the annual performance report. Leadership furthermore did not facilitate the implementation of adequate compliance monitoring processes resulting in numerous non-compliance findings being reported with key applicable legislation.

Financial and performance management

61. Management did not put adequate processes in place to ensure that a credible set of financial statements and annual performance report, in compliance with the reporting frameworks, are prepared as the internal review procedures were inadequate to identify and correct material misstatements in the financial statements and performance report and underlying records before submitting for audit. This was mainly due to the processes implemented for the preparation and finalisation of the financial statements and annual performance report being inadequate and quarterly financial statements and performance reports not being prepared to ensure the credibility of the financial statements and the annual performance report.
62. Deficiencies in review processes and the ineffective implementation of compliance monitoring controls to ensure compliance with key applicable legislation resulted in non-compliance with the MFMA and other applicable legislation and unauthorised, and fruitless and wasteful expenditure being incurred.

Governance

63. The municipality did not implement effective systems of risk management to achieve the objectives of a strengthened internal control environment and mitigate the risks of material misstatements in the financial statements and annual performance report and in non-compliance with the prescribed reporting frameworks. The audit committee was ineffective and there was no internal audit to provide adequate oversight over financial and performance reporting and compliance with laws and regulations as well as to ensure the implementation of internal controls regarding the reliability and integrity of financial and performance information, and evaluation of compliance with laws and regulations in the areas of expenditure and supply chain management.

Other reports

64. I draw attention to the following engagements conducted by various parties that had, or could have, an impact on the matters reported in the municipality 's financial statements, reported performance information, compliance with applicable legislation and other

related matters. These reports did not form part of my opinion on the financial statements or my findings on the reported performance information or compliance with legislation.

Investigations finalised

65. The Provincial Fraud Investigating Unit conducted an investigation into alleged fraud occurring at the municipality. The investigation was completed with recommendations made to the provincial government and the municipal manager to address the matters raised.

Investigations in progress

66. The Directorate for Priority Crime Investigation (Hawks) is conducting an investigation into alleged fraud at the municipality. The investigation is ongoing and is still in progress at the date of this report.

Auditor-General

Cape Town

21 February 2018



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence

Annexure – Auditor-general's responsibility for the audit

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected key performance areas and on the municipality's compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the financial statements as described in the auditor's report, I also:
 - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
 - obtain an understanding of internal control relevant to the audit 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.
 - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer.
 - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the municipality's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of the auditor's report. However, future events or conditions may cause a municipality to cease to continue as a going concern.
 - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

Communication with those charged with governance

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and where applicable, related safeguards.