

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

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Oudtshoorn Municipality set out on pages 3 to 78, which comprise the statement of financial position as at 30 June 2017, the statement of financial performance, statement of changes in net assets, statement of cash flows and statement of comparison of budget information 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 Oudtshoorn Municipality as at 30 June 2017, and its financial performance and cash flows for the year then ended in accordance with the South African Standards of General Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act, 2003 (Act. No 56 of 2003) (MFMA) and the Division of Revenue Act, 2016 (Act No. 3 of 2016) (DoRA).

Basis for qualified opinion

Contingent liabilities

3. I was unable to obtain sufficient appropriate audit evidence to confirm whether all contingent liabilities were disclosed, as not all external confirmations were received. I was unable to confirm the contingent liabilities by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to contingent liabilities, stated at R546 654 in note 49 to the financial statements.

Property plant and equipment - Other assets

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 not all municipal assets included on the asset register were assessed for impairment in accordance with GRAP 26. I was unable to confirm by alternative means the effect of not adequately considering the impairment. Consequently, I was unable to determine whether any adjustment was necessary to other assets, stated at R14 million in note 11 to the financial statements. In addition, there may also be a resultant impact on impairments and the surplus for the year.

Water distribution losses

5. I was unable to obtain sufficient appropriate audit evidence to confirm whether water distribution losses were correctly disclosed in note 41.4 to the financial statements, as the Oudtshoorn bulk water meter was damaged for a significant part of the year. I was unable to confirm the water distribution losses by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to water distribution losses, stated at R513 026 in note 41.4 to the financial statements.

Context for the opinion

6. 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 this report.
7. I am independent of the Oudtshoorn Municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) and 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.
8. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Material uncertainty relating to going concern/financial sustainability

9. I draw attention to the matter below. My opinion is not modified in respect of this matter.
10. I draw attention to note 46.1 to the financial statements, which indicates that the statement of financial position as at 30 June 2017 indicates that Oudtshoorn Municipality's current liabilities exceeded its current assets by R32,6 million (2015-16: R78,8 million). These conditions, along with other matters as set forth in note 46.1 to the financial statements, indicate that a material uncertainty exists that may cast significant doubt on the municipality's ability to operate as a going concern.

Emphasis of matters

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

Restatement of corresponding figures

12. As disclosed in note 36 to the financial statements, the corresponding figures for 30 June 2016 have been restated as a result of errors discovered during the 2016-17 financial year in the financial statements of the Oudtshoorn Municipality at, and for the year ended, 30 June 2017.

Material impairments

13. As disclosed in note 17 to the financial statements, an impairment of R51,9 million (2015-16: R60,3 million) was provided for on receivables from exchange transactions.
14. As disclosed in note 18 to the financial statements, an impairment of R23,3 million (2015-16: R22,1 million) was provided for on receivables from non-exchange transaction.

Material underspending of the conditional grant

15. As disclosed in note 9 to the financial statements, the municipality underspent its conditional grants by R7,1 million (2015-16: R16,5 million).

Material underspending of the capital budget

16. As disclosed in the statement of comparison of budget information for the year ended 30 June 2017, the municipality underspent its capital budget by R7,3 million (2015-16: R21,1 million).

Other matter

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

Unaudited supplementary schedules

18. The supplementary information set out on pages 79 to 82 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

19. 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 for the financial statements

20. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the 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.
21. 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 there is an intention 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

22. 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 the 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 aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
23. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.

Report on the audit of the annual performance report

Introduction and scope

24. 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 objectives presented in the annual performance report. I performed procedures to raise findings but not to gather evidence to express assurance.
25. 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.

26. 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 objectives presented in the annual performance report of the municipality for the year ended 30 June 2017:

Objectives	Pages in the annual performance report
Infrastructure investment/ basic services	6 – 15

27. I performed procedures to determine whether the reported performance information was properly presented and whether performance 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.
28. The material finding in respect of the usefulness and reliability of the selected objective is as follows:

Infrastructure investment/ basic services

29. I was unable to obtain sufficient appropriate evidence regarding the Infrastructure investment/ basic services objective, which clearly defined the predetermined source information, evidence and method of collection to be used when measuring the actual achievement for the indicators and targets, as required by the Framework for managing programme performance information (FMPPI). This was due to a lack of formal standard operating procedures or documented system descriptions. I was unable to confirm the usefulness and reliability of the reported performance information by alternative means.

Other matter

30. I draw attention to the matter below.

Achievement of planned targets

31. Refer to the annual performance report on pages 6 to 15 for information on the achievement of planned targets for the year and explanations provided for the under/overachievement of a number of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraph 29 of this report.

Introduction and scope

32. 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 raise findings but not to gather evidence to express assurance.
33. The material findings on compliance with specific matters in key legislations are as follows:

Strategic planning and performance management

34. A performance management system was not established or adopted as required by section 38(a) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) and municipal planning and performance management regulation 8.
35. The performance management system and related controls were not maintained or were inadequate as they did not describe how the performance planning, monitoring, measurement, review and reporting processes should be conducted, organised and managed, as required by municipal planning and performance management regulation 7(1).

Expenditure management

36. Money owed by the municipality was not always paid within 30 days, as required by section 65(2) (e) of the MFMA.
37. Effective steps were not taken to prevent irregular expenditure amounting to R280,6 million as disclosed in note 41.3 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure disclosed was caused by non-compliance with the Municipal Supply Chain Management Regulation.
38. Effective steps were not taken to prevent fruitless and wasteful expenditure, as required by section 62(1) (d) of the MFMA. The majority of the fruitless and wasteful expenditure disclosed was caused by the political instability during the administrative period where invoices were not paid to suppliers within 30-days.

Asset management

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

Procurement and contract management

40. 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).
41. 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). Similar non-compliance was also reported in the previous year.
42. The preference point system was not applied in all procurement of goods and services above R30 000 as required by section 2(a) of the Preferential Procurement Policy Framework Act 5 of 2000 and SCM regulation 28(1) (a).
43. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2) (b) of the MFMA.
44. 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.
45. 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).

Annual financial statements and annual report

46. 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 expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and/or 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.
47. 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.

Other information

48. 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 and the selected objective presented in the annual performance report that have been specifically reported in the auditor's report.
49. 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.

50. 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 objective presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
51. If, based on the work I have performed, I conclude that there is a material misstatement of this other information, I am required to report that fact.
52. I have nothing to report in this report.

Internal control deficiencies

53. 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

54. Although there were improvements in the control environment, leadership did not provide adequate oversight regarding the implementation of action plans to address the prior year audit findings which resulted in repeat findings in the areas of the financial reporting, the report on predetermined objectives and compliance to laws and regulations. Leadership did not in all instances facilitate the implementation of adequate compliance monitoring processes resulting in non-compliance findings being reported on key legislation. Furthermore, leadership should ensure that the municipality is capacitated with sufficient skilled resources to manage the gap in capacity constraints.

Financial and performance management

55. Management did not establish adequate processes to ensure that a credible set of financial statements were prepared which resulted in a qualified audit opinion.
56. The performance management unit did not ensure that all key performance indicator owners are equipped with the necessary knowledge in order to ensure that all key performance indicator processes are supported by documentation which verifies the process. Due to the lack of standard operating procedures for indicators and targets, no review processes were in place to ensure that monthly/quarterly and annual reporting was valid, accurate and complete.
57. Deficiencies in the review processes and the ineffective implementation of compliance monitoring controls to ensure compliance with key applicable legislation resulted in the non-compliance with the MFMA and other applicable legislation and irregular expenditure being incurred.

Governance

58. The municipality did not implement effective risk management and governance to strengthen the internal control environment. The risk manager post was vacant and no approved fraud prevention plan was implemented.
59. The audit committee was not independent and did not provide adequate oversight over the financial and performance reporting and compliance with laws and regulations.
60. The internal audit did not provide the necessary assurance, as they were not sufficiently resourced and capacitated.

Other reports

61. 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 in progress

62. The directorate of priority crime investigation was conducting investigations on transgressions which aspired from the Special Investigation Unit report (2015-16). The investigation was still in progress at the reporting date.

Auditor-General

Cape Town
30 November 2017



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 the selected objective 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.