

Auditor-General of South Africa

Umzinyathi District Municipality

Audit report 2017-18

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

Report on the audit of the financial statements

Adverse opinion

1. I have audited the financial statements of the Umzinyathi District Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2018, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget with actual 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, because of the significance of the matters described in the basis for adverse opinion section of this auditor's report, the financial statements do not present fairly, in all material respects, the financial position of the Umzinyathi District Municipality as at 30 June 2018, and its financial performance and its cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2017 (Act No. 3 of 2017) (Dora).

Basis for adverse opinion

Infrastructure assets

3. The municipality did not recognise all items of infrastructure assets in accordance with SA Standards of GRAP 17, *Property, plant and equipment*. Assets completed were reported as one asset in the fixed asset register and not componentised to allow each asset to be separately identifiable for physical verification. I was unable to determine the impact of this misstatement on infrastructure assets stated at R952,65 million (2016-17: R919,02 million) in note 7 to the financial statements, as it was impracticable to do so.

Value-added tax (VAT) receivable

4. The municipality's VAT receivable balance was overstated due to the municipality's financial system duplicating certain VAT transactions. Consequently, I was unable to determine whether any further adjustment was necessary to the VAT receivable balance, stated at R15,19 million in note 4 to the financial statements.

Trade payables

5. The municipality did not recognise all trade payables from exchange transactions in accordance with SA Standards of GRAP 104, *Financial instruments*. Consequently, I was unable to determine whether any further adjustments were necessary to trade payables stated at R66,22 million (2016-17: R8,61 million) as stated in note 13 to the financial statements.

Expenditure

6. I was unable to obtain sufficient appropriate audit evidence for general expenditure and contracted services due to the status of the accounting records. Supporting documentation did not contain adequate information to determine whether all the expenditure was properly recorded. Consequently, I was unable to determine whether any further adjustments were necessary to general expenses stated at R63,39 million (2016-17: R120,05 million) and contracted services stated at R196,37 million.

Revenue from exchange transactions

7. The municipality did not recognise all revenue from service charges in accordance with SA Standards of GRAP 9, *Revenue from exchange transactions*. The amount of the kilolitres of water that the municipality billed the consumers did not agree to the actual meter readings. I was unable to determine the impact of this misstatement, as it was impracticable to do so for the sale of water amount stated at R57,51 million (2016-17: R33,76 million) in note 19 and consumer debtors stated at R254,09 million (2016-17: R196,27 million) in note 5 to the financial statements. Additionally, there was a resultant impact on the surplus for the period and the accumulated surplus at year-end.

Restatement of corresponding figure - water losses

8. I was unable to obtain sufficient appropriate audit evidence for the restatement of the corresponding figure for water losses. As described in note 50 to the financial statements, the restatement was made to rectify a previous 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 was necessary to the water losses figure stated at R23,16 million in the financial statements.

Context for the opinion

9. 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 auditor's report.
10. I am independent of the 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.
11. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my adverse opinion.

Emphasis of matters

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

Material losses – water

13. As disclosed in note 50 to the financial statements, material water losses of R21,72 million were incurred. Technical and non-technical losses amounted to 6,89 million kilolitres and were due to burst pipes in the reticulation system due to ageing infrastructure and illegal connections.

Unauthorised expenditure

14. As disclosed in the statement of comparison of budget with actual information, the municipality materially overspent its budget by R176,63 million mainly due to overspending, resulting in unauthorised expenditure being incurred.

Other matter

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

Unaudited disclosure notes

16. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion on it.

Responsibilities of the accounting officer for the financial statements

17. 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.

18. In preparing the financial statements, the accounting officer is responsible for assessing the Umzinyathi District 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 appropriate governance structure 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

19. 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.

20. 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

21. 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 development priorities presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
22. 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 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.
23. 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 development priorities presented in the annual performance report of the municipality for the year ended 30 June 2018:

Development priorities	Pages in the annual performance report
KPA 2 – basic service delivery and infrastructure investment	xx – xx
KPA 3 – local economic development	xx – xx

24. 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.

25. The material findings in respect of the usefulness and reliability of the selected development priorities are as follows:

Development priority 2 – basic service delivery and infrastructure investment

Various indicators

26. The reported targets in the annual performance report were not consistent with those approved in the integrated development plan (IDP), as the IDP did not include targets for the following indicators:

Indicator description	Target per integrated development plan	Target per annual performance report
Percentage of compliance to quality standards for the waste water treatment works	N/A	75%
Percentage of compliance to quality standards for drinking water	N/A	80%
Turnaround time to attend to water and sanitation related incidents	N/A	3-6 hours
Volumes of water purified and distributed	N/A	10 087 368
Percentage reduction of non-revenue water	War on leaks	1%

Various indicators

27. The measures taken to improve performance against targets for the following indicators were not included in the annual performance report:

Indicator description	Planned target	Actual target
Number of households to be provided with access to water within RDP standards	966	404
Number of households provided with sanitation facilities	2 700	1 319
Percentage of compliance to quality standards for the waste water treatment works	75%	41%
Volumes of water purified and distributed	10 087 368	0
Percentage reduction of non-revenue water	1%	0%

Various indicators

28. The municipality did not have an adequate record keeping system to enable reliable reporting on the achievement of the indicators listed below. As a result, I was unable to obtain sufficient appropriate audit evidence in some instances; while in other cases, the supporting evidence provided did not agree to the reported achievements. Based on the supporting evidence that was provided, the achievement of these indicators was different to the reported achievement in the annual performance report. I was also unable to further confirm the reported achievements by alternative means. Consequently, I was unable to determine whether any further adjustments were required to the reported achievements for the indicators listed below.

Indicator description	Reported achievement
Number of households to be provided with access to water within RDP standards	404
Number of households provided with sanitation facilities	1 319
Percentage of compliance to quality standards for drinking water (SANS 241)	96%
Percentage of compliance to quality standards for the waste water treatment works	41%
Turnaround time to attend to water and sanitation related incidents	3-6 hours
Volumes of water purified and distributed	0

Development priority 3 – local economic development

Various indicators

29. The targets approved in the IDP were inconsistent with the targets reported in the annual performance report.

Indicator description	Target per integrated development plan	Target per annual performance report
Date of adoption of LED strategy	30 December 2017	30 June 2018
Number of SMME /informal economy programmes /supported project.	Not included	1
No of farmer production support units (FPSU) supported	Not included	1
Number of tourism structures supported with grant	Not included	1
Number of jobs created through municipality's LED initiatives including capital projects.	Not included	957

Number of project phases completed for tourism signage

30. The indicator approved in the IDP was not reported in the annual performance report.

Various indicators

31. The following indicators were not specific in clearly identifying the nature and the required level of performance.

Indicator description
Number of SMME /informal economy programmes /supported project.
No of farmer production support units (FPSU) supported
Number of tourism structures supported with grant

Number of project phases completed for tourism signage

32. The indicator and target approved in the IDP was not reported in the annual performance report and no evidence was obtained to confirm that the change had been approved.

Date of adoption of the LED strategy

33. The target approved in the IDP was 30 December 2017. However, the target was changed to 30 June 2018 and no evidence was obtained to confirm that the change had been approved.

Number of jobs created through municipality's LED initiatives

34. The measures taken to improve performance against target of 957 and actual of 0 were not included in the annual performance report.

Various indicators

35. The reported achievement in the annual performance report did not agree to the supporting evidence provided for the indicators listed below. The supporting evidence provided indicated that the achievements of these indicators were as follows:

Indicator description	Reported achievement	Audited value
Date of adoption of LED strategy	30 June 2018	20 September 2018
No. of jobs created through municipality's LED initiatives including capital projects.	0	24
Number of tourism structures supported with grant	1	2
Number of SMME /informal economy programmes /supported project.	1	3

Other matter

36. I draw attention to the matter below.

Achievement of planned targets

37. The annual performance report on pages xx to xx includes information on the achievement of 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 in paragraphs 28 to 39 of this report.

Report on the audit of compliance with legislation

Introduction and scope

38. 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.

39. The material findings on compliance with specific matters in key legislation are as follows:

Financial statements

40. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA.
41. Material misstatements identified by the auditors in the submitted financial statements were not adequately corrected and/or the supporting records could not be provided subsequently, which resulted in the financial statements receiving an adverse audit opinion.

Expenditure management

42. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
43. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The majority of the disclosed irregular expenditure was caused by non-compliance with municipal supply chain management (SCM) regulations.

Asset management

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

Revenue management

45. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.
46. I was unable to obtain sufficient appropriate audit evidence that accounts for charges for municipal services were prepared on a monthly basis, as required by section 64(2)(c) of the MFMA.

Consequence management

47. 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)(b) of the MFMA.

Strategic planning and performance management

48. The local community was not consulted on the drafting of the IDP, as required by section 29(1)(b)(ii) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) and municipal planning and performance regulation 15(1)(a)(i).
49. The IDP was not developed or adopted by the council after the start of its elected term, as required by section 25(1) of the MSA.

Conditional grants

50. Performance in respect of programmes funded by the regional bulk infrastructure, water services infrastructure and rural transport services infrastructure grants was not evaluated, as required by section 12(5) of Dora.

Procurement and contract management

51. Sufficient appropriate audit evidence could not be obtained that contracts were awarded in accordance with the legislative requirements, due to an inadequate filing system.
52. Some goods and services with a transaction value below R200 000 were procured without obtaining the required price quotations, in contravention of SCM regulations 13(c) (GNR 868 of 30 May 2005) and 17(a) and (c).
53. Sufficient appropriate audit evidence could not be obtained that goods and services with a transaction value above R500 000 were procured by inviting competitive bids and/or that deviations were only approved by the accounting officer if it was impractical to invite competitive bids, as required by SCM regulations 19(a) and 36(1).
54. Sufficient appropriate audit evidence could not be obtained 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).
55. Sufficient appropriate audit evidence could not be obtained 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 of South Africa, 2000 (Act No. 5 of 2000).
56. Sufficient appropriate audit evidence could not be obtained that all extensions or modifications to contracts were approved by a properly delegated official, as required by SCM regulation 5.
57. Awards were made to service providers who were in the service of other state institutions or whose directors / principal shareholders were in the service of other state institutions, in contravention of section 112(j) of the MFMA and SCM regulation 4.

Other information

58. 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 those selected development priorities presented in the annual performance report that have been specifically reported in this auditor's report.
59. 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.
60. 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 development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
61. If, based on the work I have performed, I conclude that there is a material misstatement in this other information, I am required to report that fact.

62. The other information I obtained prior to the date of this auditor's report are the mayor's foreword and the municipal manager's overview, while the audit committee's report is expected to be made available to me after 30 November 2018.
63. If, based on the work I have performed on the other information that I obtained prior to the date of this auditor's report, I conclude that there is a material misstatement of this other information, I am required to report that fact.
64. When I do receive and read the report of the audit committee, 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

65. 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 on it.
66. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the adverse opinion, the findings on the performance report and the findings on compliance with legislation included in this report.
67. The leadership did not adequately exercise oversight responsibility over the preparation and review of the financial statements and the annual performance report.
68. There has also been an increase in the vacancy levels and instability in key management positions, which resulted in a lack of proper supervision, reviews as well as monitoring of the implementation of the audit action plan.
69. Management did not ensure that monthly information was reconciled for infrastructure assets, revenue and receivables to ensure the quality of monthly management information and ultimately the year-end financial statements.
70. Management did not adequately monitor and review the performance information to ensure that it was well defined and agreed to supporting information.
71. There was also inadequate ongoing monitoring of compliance with the applicable laws and regulations.

Other reports

72. 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

73. An investigation in terms of section 106 of the MFMA was conducted by an independent consulting firm, on behalf of the Department of Cooperative Governance and Traditional Affairs. The investigation covered the period 1 July 2015 to 30 June 2017 and related to expenditure for boreholes and debt collection that was not supported by adequate documentary evidence. The municipality is awaiting the release of the final report.
74. An investigation covering the period 1 July 2014 to 30 June 2018 is being conducted by an independent consulting firm at the request of the municipality. The firm is looking into value for money on expenditure and whether supply chain processes were followed relating to the construction of the municipality's disaster management centre. The investigation is currently in progress.

Auditor-General
Pietermaritzburg

30 November 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 development priorities 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 this 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 Umzinyathi District 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 this auditor’s report. However, future events or conditions may cause a municipality to cease continuing 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.