

Auditor-General of South Africa

Amajuba District Municipality - Audit
report 2016-17

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

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Amajuba District Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2017, and the statement of financial performance, statement of changes in net assets, and cash flow statement 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 Amajuba District 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) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) and the Division of Revenue Act of South Africa, 2016 (Act No. 3 of 2016) (DoRA).

Basis for qualified opinion

Service charges

3. The municipality recognised items that did not meet the definition of revenue in accordance with SA Standards of GRAP 9, *Revenue from exchange transactions*. Revenue was not measured at the fair value of the consideration received or receivable, as required by this standard. Additionally, I was unable to obtain sufficient appropriate audit evidence for service charges due to the status of accounting records. Therefore, I was unable to confirm service charges by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to the service charges stated at R26,05 million (2015-16: R24,42 million) in note 18 and consumer debtors stated at R16,45 million (2015-16: R11,89 million) in note 9 to the financial statements.

Inventory

4. I was unable to obtain sufficient appropriate audit evidence for the assumptions used by management to calculate the rate used to measure inventory. Additionally, the municipality did not measure inventory at the lower of cost or net realisable value in accordance with SA Standards of GRAP 12, *Inventory*. As the municipality did not implement a reliable costing system to measure inventory on hand, I was unable to determine the impact on inventory stated at R6,92 million (2015-16: R5,48 million) as disclosed in note 10 to the financial statements as it was impracticable to do so.

Water losses

5. The municipality measured water losses using the rate to measure inventory. I was unable to obtain sufficient appropriate audit evidence for the basis used for calculating the cost of inventory. Consequently, I was unable to determine the value of the adjustment necessary to water losses stated at R21,53 million (2015-16:R19,46 million) in note 45 to the financial statements.

Unspent Conditional grants

6. I was unable to obtain sufficient appropriate audit evidence regarding the unspent conditional grants due to an adjustment passed to restate the opening balance. I was unable to confirm the grant liability by alternative means. Consequently, I was unable to determine whether any adjustment to the accumulated surplus of R590,68 million as disclosed in note 38 to the financial statements and the related unspent conditional grant liability stated at R7,43 million (2015-16: R13,46 million) in note 14 to the financial statements was necessary.

Context 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.

Material uncertainty related to going concern

10. I draw attention to the matter below. My opinion is not modified in respect of this matter.
11. I draw attention to note 38 in the financial statements, which indicates that as of the 30 June 2017 the municipality's current liabilities exceeded its current assets by R39,43 million. This is due to poor history of debtor payment and unfavourable liquidity ratios. This condition, indicate that a material uncertainty exists that may cast significant doubt on the municipality's ability to continue as a going concern. Management plans to improve financial sustainability by implementing cost containment measures in conjunction with revenue enhancement strategies.

Other matter

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

Unaudited disclosure notes

13. 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 thereon.

Responsibilities of accounting officer

14. 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, 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.
15. 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

16. 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.
17. 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

18. 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 identify findings but not to gather evidence to express assurance.
19. 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.

20. 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, objective 1 – basic service delivery on pages x-x presented in the annual performance report of the municipality for the year ended 30 June 2017.
21. 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.
22. The material finding in respect of the usefulness and reliability of the selected objective is as follows:

Objective 1 – Basic Service Delivery

Various indicators – Indicators not well-defined

23. I was unable to obtain sufficient appropriate audit evidence that clearly defined the predetermined nature and required level of performance and method of calculation for the indicators listed below, as required by the Framework for managing programme performance information (FMPPi). This was due to a lack of technical indicator descriptions and formal standard operating procedures. I was unable to test whether these indicators were well-defined by alternative means.

■ Implementation of Buffalo Flats Water Supply Project - Phase 3B: Number of households connected per quarter ■ Municipality Water and Infrastructure Grant - Emadlangeni Rural Water Supply Phase 2: Number of households connected per quarter ■ % completion of the project per quarter ■ Number of boreholes drilled and refurbished per quarter ■ % completion of the project per quarter ■ % water loss reduction per quarter ■ % completion of the project per quarter ■ Number of reports produced per quarter ■ Disaster awareness campaigns held quarterly.

Other matters

24. I draw attention to the matters below.

Achievement of planned targets

25. The annual performance report on pages x to x; x to x includes information on the achievement of planned targets for the year and explanations provided for the under and overachievement of a significant 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 23 of this report.

Adjustment of material misstatements

26. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of basic service delivery. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

Introduction and scope

27. 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.
28. The material findings on compliance with specific matters in key legislation are as follows:

Annual financial statements, performance and annual report

29. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets, current assets, and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements in revenue, debtors, and inventory and water losses resulted in the financial statements receiving a qualified audit opinion.

Consequence management

30. Irregular expenditure 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.

Expenditure management

31. Effective steps were not taken to prevent fruitless and wasteful expenditure of R48 641, as disclosed in note 40 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The disclosed fruitless and wasteful expenditure was caused by penalties incurred for late payments.
32. Effective steps were not taken to prevent irregular expenditure of R303 778, as disclosed in note 41 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The disclosed irregular expenditure was caused by procurement from a supplier whose tax matters had not been declared by the South African Revenue Services to be in order.
33. Money owed by the municipality was not always paid within 30 days as required by section 65(2)(e) of the MFMA.

Revenue Management

34. An effective system of internal control for revenue and debtors was not in place, as required by section 64(2)(f) of the MFMA.
35. An adequate management, accounting and information system which accounts for revenue and debtors was not in place, as required by section 64(2)(e) of the MFMA.

Procurement and Contract Management

36. Bid documentation for procurement of some of the commodities designated for local content and production, did not stipulate the minimum threshold for local production and content as required by Preferential Procurement Regulation (PPR) 9(1).

37. Some commodities designated for local content and production, were procured from suppliers who did not submit a declaration on local production and content as required by PPR 9(1).
38. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by Municipal Supply Chain Management Regulation, 2005 (MSCMR) 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of MSCMR regulation 36(1).
39. Some of the contracts were awarded to providers whose tax matters had not been declared by the South African Revenue Service to be in order, in contravention of SCM regulation 43.

Other information

40. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes the accounting officer's report, the audit committee's report and the mayor's report. The other information does not include the financial statements, the auditor's report thereon and those selected objectives presented in the annual performance report that have been specifically reported on in the auditor's report.
41. 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.
42. 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 objectives presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
43. 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

44. 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

45. Leadership did not adequately oversee and monitor that an action plan developed to address prior year audit findings was actioned timely and accurately, as the action plan was attended to late in the year. This resulted in the same qualification finding on revenue re-occurring in the current year.

46. Leadership did not adequately exercise oversight responsibility to ensure that corrective action is taken for poor performance and that consequence management is applied

Financial and performance management

47. Management did not prepare accurate management accounts in respect of inventory and water losses, as the costing bases were not in line with applicable reporting framework. This is because of the lack of communication between the technical and finance departments.

48. Management did not undertake adequate reviews of registers, reconciliations and schedules supporting information reported on the annual performance report. This was due to slow response in addressing internal control deficiencies identified during the audit.

Other reports

49. I draw attention to the following engagement 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. This report did not form part of my opinion on the financial statements or my findings on the reported performance information or compliance with legislation.

50. The municipality appointed an independent consulting firm in 2012 to conduct an investigation into alleged irregularities on procurement of goods and services covering the period of 1 July 2011 to 30 June 2012. The investigation was still in progress at the date of this report.

Auditor-General

Pietermaritzburg

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 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 council, which constitutes the accounting officer.
 - conclude on the appropriateness of the council, which constitutes 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 Amajuba 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 the auditor’s report. However, future events or conditions may cause the 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 here applicable, related safeguards.

