

Report of the auditor-general to the Free State Legislature and the council on the Metsimaholo Local Municipality

Report on the financial statements

Introduction

1. I have audited the financial statements of the Metsimaholo Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2015, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with 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, 2014 (Act No. 10 of 2014) (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.

Auditor-general's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with International Standards on Auditing. Those standards require that I comply with ethical requirements, and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the municipality's preparation and fair presentation of the financial statements 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. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Metsimaholo Local Municipality as at 30 June 2015 and its financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

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

Restatement of corresponding figures

8. As disclosed in note 40 to the financial statements, the corresponding figures for 30 June 2014 have been restated as a result of errors discovered during 2014-15 in the financial statements of the municipality at, and for the year ended, 30 June 2014.

Irregular expenditure

9. As disclosed in note 48 to the financial statements, the municipality incurred irregular expenditure of R48 211 911 (2014: R65 034 263) during the year under review mainly due to non-compliance with supply chain management requirements.

Material impairments

10. As disclosed in note 5 to the financial statements, a provision for the impairment of debtors amounting to R121 760 402 (2014: R105 858 827) had been made with regard to irrecoverable receivables from non-exchange transactions. In addition, as disclosed in note 6 to the financial statements, a provision for impairment of debtors amounting to R430 760 556 (2014: R347 118 850) has been made with regard to irrecoverable receivables from exchange transactions.

Going concern

11. Note 43 to the financial statements indicate that the municipality has unfavourable indicators in respect of trade payables and receivables. These conditions indicate the existence of an uncertainty that may cast doubt on the municipality's ability to operate as a going concern.

Additional matters

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

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. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

Unaudited supplementary information

14. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon

Report on other legal and regulatory requirements

15. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report findings on the reported performance information against predetermined objectives for the selected key performance areas presented in the annual performance report, compliance with legislation and internal control. The objective of my tests was to identify reportable findings as described under each subheading, but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

16. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected key performance area presented in the annual performance report of the municipality for the year ended 30 June 2015:
 - KPA 1: service delivery and infrastructural development (on pages x to x)
17. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
18. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned key performance area. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information*.
19. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
20. The material findings in respect of the selected key performance area is as follows:

KPA 1 Service delivery and infrastructural development

Usefulness of reported performance information

21. I did not identify material findings on the usefulness of the reported performance information for the selected key performance area KPA 1: service delivery and infrastructural development.

Reliability of reported performance information

22. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. Adequate and reliable corroborating evidence could not be provided for 36,9% of the targets to assess the reliability of the reported performance information. The auditee's records did not permit the application of alternative audit procedures. This was due to limitations placed on the scope of my work by the absence of information systems. **(ISS.32)**

Additional matter

23. I draw attention to the following matter:

Achievement of planned targets

24. Refer to the annual performance report on page(s) x to x and x to x for information on the achievement of the planned targets for the year. This information should be considered in the context of the material findings on the reliability of the reported performance information for the selected key performance area reported in paragraph 21 of this report.

Compliance with legislation

25. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My material findings on compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Annual financial statements, performance and annual reports

26. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the Municipal Finance Management Act. Material misstatements of non-current assets, current assets and disclosure items identified by the auditors in the submitted financial statement were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion. **(ISS.103)**

Expenditure management

27. Money owed by the municipality was not always paid within 30 days or an agreed period, as required by section 65(2)(e) of the MFMA. **(ISS.28, 88)**
28. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA. **(ISS.21)**

Budgets

29. The total unforeseen and unavoidable expenditure incurred exceeded R15 million, in contravention of Municipal Budget and Reporting Regulation 72. **(ISS.100)**

Procurement and contract management

30. Quotations were accepted from prospective providers who are not registered on the list of accredited prospective providers and do not meet the listing requirements prescribed by the SCM policy in contravention of SCM regulation 16(b) and 17(b). **(ISS.101)**
31. Contracts were extended or modified without the approval of a properly delegated official, as required by SCM Regulation 5. **(ISS.101)**
32. Contracts and quotations were awarded to providers whose tax matters had not been declared by the South African Revenue Service to be in order, as required by SCM regulation 43. **(ISS.101)**

Internal control

33. I considered internal control relevant to my audit of the financial statements, the performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on the performance report and the findings on compliance with legislation included in this report.

Leadership

34. The occurrence of material irregular expenditure during the year under review indicates that integrity and ethical values were not adequate to prevent irregular expenditure and to set the standard for sound corporate governance, as they were not prevented by management.
35. Internal policies and procedures for performance information management were not developed, approved and implemented due to a slow response by management on the recommendations in the previous audit report.

Financial and performance management

36. The financial statements were subjected to material corrections resulting from the audit process, which are attributable to weaknesses in the municipality's design and implementation of internal controls for financial management and financial reporting, and weaknesses in the information systems.
37. The municipality did not have a proper system of record management to maintain information that supports the reported performance due to a lack of capacity in the performance information unit.

Other reports

Investigations

38. An independent consulting firm performed an investigation at the request of the municipality, which covered the period 1 July 2012 to 30 June 2014. The investigation was initiated based on an allegation of alleged irregular journal adjustments and write-offs, illegal water connections, possible theft of electrical equipment and other irregularities, alleged irregular processing of transactions on the salary system. The investigations concluded on 2 September 2015 and resulted in disciplinary procedures being instituted against seven employees. These proceedings are currently in progress.

Bloemfontein

30 November 2015



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence