

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

Report on the audit of the financial statements

Opinion

1. I have audited the financial statements of the Metsimaholo Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2017, 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, the financial statements present fairly, in all material respects, the financial position of the Metsimaholo Local 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 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, 2016 (Act No. 3 of 2016) (Dora).

Basis for opinion

3. 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.
4. 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.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Material uncertainty related to going concern

6. I draw attention to note 44 to the financial statements, which indicates that the municipality's current liabilities exceeded its current assets by R10 457 393. In addition, the municipality owed Eskom R38 734 074 (2016: R26 449 491) and the water board R11 135 456 (2016: R10 720 677) as at 30 June 2017. These conditions, along with other matters as set forth in note 44, indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern and to meet its service delivery objectives.

Emphasis of matters

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

Irregular expenditure

8. As disclosed in note 48 to the financial statements, irregular expenditure of R18 302 949 (2016: R19 380 908) was incurred due to non-compliance with SCM requirements. In addition, the full extent of irregular expenditure is still in the process of being determined.

Restatement of corresponding figures

9. As disclosed in note 40 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 losses

10. As disclosed in note 32 to the financial statements, The municipality incurred water distribution losses of R4 836 143 (2016: R3 270 901) mainly due to leakages, burst water pipes, line losses, tampering and theft.

Material impairments

11. As disclosed in note 5 to the financial statements, consumers and other receivables from non-exchange transactions were impaired by R141 639 600 (2016: R136 692 289). In addition, as disclosed to in note 6 to the financial statements receivable from exchange transactions were impaired by R642 331 750 (2016: R522 427 485).

Other matters

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

Dissolution of the municipal council

13. The municipal council was dissolved in the current year due to the failure to approve the 2017-18 budget which was due on 30 June 2017. In terms of the section 139(4) of the Constitution of South Africa, 1996 (Act No. 108 of 1996), the executive council appointed an administrator until a new council has been declared elected.

Unaudited disclosure notes

14. 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, as contained in note xx to the financial statements, did not form part of the audit of the financial statements and, accordingly, I do not express opinion on it.

Unaudited supplementary information

15. The appropriation statement 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 this statement and, accordingly, I do not express an opinion on it.

Responsibilities of the accounting officer for the financial statements

16. 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.
17. In preparing the financial statements, the accounting officer is responsible for assessing the Metsimaholo Local 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 there is no realistic alternative but to do so.

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

18. 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 the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
19. 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

20. 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 area presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
21. 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.

22. 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 area 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 |
|--|--|
| KPA 1: Basic service delivery and infrastructure development | x – x |

23. 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.
24. The material findings in respect of the usefulness and reliability of the selected key performance area are as follows:

Key performance area 1: Basic service delivery and infrastructure development

Indicator 1.9 percentage of reported water leaks repaired.

25. The municipality did not have an adequate performance management system to maintain records to enable reliable reporting on achievement of targets. Sufficient appropriate audit evidence could not be provided in some instances. In other cases, the evidence provided did not agree with the recorded achievements which resulted in a misstatement of the target achievement reported as the evidence provided indicated that it was 64,6percentage and not 88percentage. I was also unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any further adjustments were required to the reported achievements.

Various indicators

26. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of the indicators listed below. This was due to actual achievement not reported. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements.

| Indicator | Reported achievement |
|---|----------------------|
| 2.6 Percentage of reported sewer blockages attended to in time (within 48hours) | Target achieved |
| 2.7 Percentage compliance with the green drop quality accreditation system | Target not achieved |
| 3.7 Percentage electricity distribution losses minimised | Target achieved |

| | |
|---|---------------------|
| 3.8 Number of hours/ percentage of reported outages responded to in time | Target not achieved |
| 3.9 Number of hours / percentage of reported industrial outages responded to in time | Target achieved |
| 3.10 Number of months/ percentage of reported faulty street and high mast lights responded to in time | Target achieved |

Various indicators

27. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of the indicators listed below. This was due to the unavailability of supporting documentation. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements.

| Indicator | Reported achievement |
|--|----------------------|
| 1.1 Number of HHs with access to potable water in formalised areas (yard metered connection) | 51893 |
| 1.2 Number of HHs provided with new metered yard connections | 1601 |
| 2.1 Number of HHs with access to decent sanitation | 51893 |
| 2.2 Number of households provided with sewer house connections | 1601 |
| 2.3 Percentage planned sewer pump stations constructed in Gortin | 88percentage |
| 3.1 Number of HHs with access to basic electricity in formal areas | 51088 |
| 3.2 Number of HHs provided with new metered stand connections in formal areas | 3213 |
| 11.1 Number of/ percentage of households with access to basic refuse removal services (removal at least once a week) | 50 000=100percentage |
| 11.2 Percentage of formal businesses receiving a daily refuse removal service | 100percentage |

Various indicators

28. The reported achievements of the indicators listed below were misstated, as the evidence provided did not agree with the reported achievements as follows:

| Performance indicator | Reported achievement | Audited value |
|--|----------------------|----------------|
| 1.8 Percentage minimisation of water distribution loss | 23percentage | 27.9percentage |
| 1.12 Number of/ percentage of zonal meters installed | 5=100percentage | 5=45percentage |

Other matters

29. I draw attention to the matters below.

Achievement of planned targets

30. Refer to the annual performance report on pages xx to xx for information on the achievement of planned targets for the year and explanations provided for the under/overachievement of a significant number of targets. This information should be considered in the context of the disclaimer of opinions expressed on the usefulness and reliability of the reported performance information in paragraph of this report.

Adjustment of material misstatements

31. 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 1: basic service delivery and infrastructure development. 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 included in the basis for disclaimer of opinion paragraphs.

Report on audit of compliance with legislation

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 identify findings but not to gather evidence to express assurance.

33. The material findings in respect of the compliance criteria for the applicable subject matters are as follows:

Annual financial statements and annual report

34. 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 property plant and equipment identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently.

35. The 2015-16 annual report was not tabled in the municipal council within seven months after the end of the financial year, as required by section 127(2) of the MFMA.

Asset management

36. Capital assets were transferred without the approval of the council and the accounting officer, as required by section 14(2)(a) of the MFMA.

Expenditure management

37. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA
38. Effective steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA.

Procurement and contract management

39. Some of the goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations, in contravention of SCM regulation 17(a) and (c). Similar non-compliance was also reported in the prior year.
40. Sufficient appropriate audit evidence could not be obtained that some of the 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).
41. Sufficient appropriate audit evidence could not be obtained that quotations were only accepted from bidders whose tax matters had been declared by the South African Revenue Service to be in order, as required by SCM regulation 43.
42. 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). Similar non-compliance was also reported in the prior year.
43. One of the competitive bids was adjudicated by a bid adjudication committee that was not composed in accordance with SCM regulation 29(2). This non-compliance was also reported in the prior year.
44. One contract was made to bidders other than those recommended by the bid evaluation committee as required by SCM regulation 29(5)(b). Similar non-compliance was also reported in the prior year.
45. An award was made to a provider whose directors principal shareholders were in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulation 44.

Consequence management

46. Irregular expenditure incurred by the municipality were not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.
47. The 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 integrated development plan (IDP) was not adopted by the council after the start of its elected term, as required by section 25(1) of the Municipal System Act, 2000 (Act No. 32 of 2000) (MSA).

Human resource management

49. Appropriate systems and procedures to monitor, measure and evaluate performance of staff were not developed and adopted as required by section 67(1)(d) of the Municipal System Act, 2000 (Act No. 32 of 2000).

Other information

50. The Metsimaholo Local Municipality's 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 KPAs presented in the annual performance report that have been specifically reported on in the auditor's report.
51. 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.
52. 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 KPAs presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work I have performed on the other information 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.
53. I did not receive the other information prior to the date of this auditor's report. When I do receive 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 re-issue my auditor's report amended as appropriate.

Internal control deficiencies

54. 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 findings on the annual performance report and the findings on compliance with legislation included in this report.
55. Management did not always take timely and adequate action to address weaknesses in the reporting on financial and performance management and predetermined objectives due to a lack of monitoring and supervision, which resulted in material adjustments and audit report matters.
56. Management did not interpret the SCM regulations requirements correctly in the supply chain management section, which resulted in non-compliance with applicable legislation and further the occurrence of irregular expenditure.

57. Consequence management was not applied effectively as the council did not investigate instances of irregular and fruitless and wasteful expenditure to determine whether any person was to be held liable for the expenditure as the council did not appoint a committee to investigate the expenditure before it was written off.
58. Senior management did not ensure that supporting documentation for some indicators and targets were kept and that the reported information is consistent, valid, accurate and complete. As a result, issues were reported in the audit report that could have been prevented.
59. Inadequate monitoring of the financial statements compilation process as well as a lack of skills and review by municipal officials resulted in material adjustments to the financial statements that could have been prevented.
60. Management did not regularly review and monitor management's compliance with laws and regulations and internally designed policies and procedures. As a result, significant non-compliance issues were noted that could have been prevented.
61. Internal audit did not adequately review and verify the information reported in the annual financial statements and performance report submitted for auditing. This resulted in various matters to be adjusted and corrected in the audit report that could have been prevented.
62. Insufficient coordination between directorates and lack of processes and controls to ensure compliance with the supply chain management requirements resulted in the occurrence of irregular expenditure.

Auditor-General
Bloemfontein

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 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 Metsimaholo Local 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 here applicable, related safeguards.

