



# Report of the auditor-general to the North West provincial legislature and the council on the Maquassi Hills Local Municipality

## Report on the financial statements

### Introduction

1. I have audited the financial statements of the Maquassi Hills Local Municipality set out on pages XX to XX, which comprise the statement of financial position as at 30 June 2016, the 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, 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 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, 2015 (Act No. 1 of 2015) (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 entity'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 entity'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 qualified audit opinion.

## **Basis for qualified opinion**

### **Trade and other payables from exchange transactions**

6. I was unable to obtain sufficient appropriate audit evidence for trade and other payables from exchange transactions due to the status of the accounting records. In addition, interest on other financial liabilities was duplicated resulting in trade and other payables from exchange transactions and finance cost expense being overstated by R1 583 792 .I could not confirm the trade and other payables by alternative means. Consequently, I was unable to determine whether any further adjustments relating to trade and other payables from exchange transactions of R150 421 442 as disclosed in note 13 to the financial statements was necessary.

### **Service charges**

7. The municipality did not recognise all service charges as required by SA standards of GRAP 9 *Revenue from exchange transactions* and GRAP 1 *Presentation of financial statements*. As the municipality did not maintain adequate records of services rendered, I was unable to determine the full extent of the understatement of sale of water as it was impracticable to do so. Consequently, I was unable to determine whether any adjustments relating to revenue from sale of water of R45 764 027 as disclosed in note 19 of the financial statements and trade and other receivables from exchange transactions of R9 326 175 as disclosed in note 10 to the financial statements were necessary.

### **Irregular expenditure**

8. Section 125 of the MFMA requires the disclosure of irregular expenditure incurred. I was unable to obtain sufficient appropriate audit evidence to confirm that awards of R7 471 328 were made in terms of the supply chain management requirements. In addition, the municipality made payments of R936 862 in contravention with the supply chain management requirements which were not included in irregular expenditure disclosed. The municipality's records did not permit the application of alternative procedures. Consequently, I was unable to determine whether any further adjustment relating to irregular expenditure of R170 838 050 as disclosed in note 43 to the financial statements was necessary.

## **Qualified opinion**

9. In my opinion, except for the effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of Maquassi Hills Local Municipality as at 30 June 2016 and its financial performance and cash flows for the year then ended, in accordance with the SA standards of GRAP and the requirements of the MFMA and the DoRA.

## **Emphasis of matters**

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

### **Restatement of corresponding figures**

11. As disclosed in note 46 to the financial statements, the corresponding figures for 2015 have been restated as a result of errors discovered during 2016 in the financial statements of the





## Unauthorised expenditure

12. As disclosed in note 41 to the financial statements, unauthorised expenditure of R40 034 602 was incurred in the current year and the unauthorised expenditure in respect of prior years of R368 403 193 had not yet been dealt with in accordance with section 32 of the MFMA.

## Fruitless and wasteful expenditure

13. As disclosed in note 42 to the financial statements, fruitless and wasteful expenditure of R2 351 520 was incurred in the current year and the fruitless and wasteful expenditure in respect of prior years of R679 032 had not yet been dealt with in accordance with section 32 of the MFMA.

## Material losses

14. As disclosed in note 47 to the financial statements, material electricity and water losses to the amount of R3 099 495 (2015: R115 112) and R40 211 611 (2015: R40 407 503) were incurred.

## Going concern

15. Note 39 to the financial statements indicates that the municipality has experienced difficulties in settling its current liabilities. These conditions indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern.

## Additional matters

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

## Unaudited disclosure notes

17. 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 schedules

18. 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

19. 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 selected key performance area 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**

20. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected key performance area (KPA) presented in the annual performance report of the municipality for the year ended 30 June 2016:
  - KPA1: Service delivery and infrastructure development on pages 23 to 32
21. 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 objectives. 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 (FMPPi).
22. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
23. The material findings in respect of the selected KPA are as follows:

### **KPA1: Service delivery and infrastructure development**

#### **Usefulness of reported performance information**

24. Section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) requires the integrated development plan (IDP) to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 30% reported objectives were not consistent with those in the IDP.

#### **Reliability of reported performance information**

25. The FMPPi requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure reliable reporting of actual achievements against planned objectives, indicators and targets. The reported achievements against planned targets of 40% of the indicators were not reliable when compared to the source information.

#### **Additional matter**

26. I draw attention to the following matter:

#### **Achievement of planned targets**

27. Refer to the annual performance report on page 23 to 32 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 usefulness and reliability of the reported performance information for the selected key performance area reported in paragraphs 24 to 25 of this report.

## **Compliance with legislation**

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







## **Strategic planning and performance management**

29. The amendments to the IDP was not adopted by the council only after consultation with the district and taking into account all comments received as required by regulation 6 of the Municipal planning and performance management regulations.
30. The performance management system was not in line with the priorities, objectives, indicators and targets contained in its IDP as required by section 38(a) of the MSA and Municipal planning and performance management regulation 7(2)(g).
31. Key performance indicators in respect of each of the development priorities and objectives were not set out in the IDP, as required by section 41(1)(a) of the MSA and regulations 1 and 9(1)(a) of the Municipal planning and performance management regulations.
32. The performance management system and related controls were inadequate as it did not describe and represent the processes of performance monitoring and review and how it is conducted, organised and managed, as required by sections 38 of the MSA and regulation 7 of the Municipal planning and performance management regulations.

## **Annual financial statements, performance and annual reports**

33. 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, current liabilities, revenue, expenditure 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 resulted in the financial statements receiving a qualified audit opinion.
34. The 2014-15 annual report was not published for the local community to submit representations in connection with the annual report, as required by section 127(5)(a) of the MFMA.
35. The oversight report adopted by the council on the 2014-15 annual report was not made public, as required by section 129(3) of the MFMA.
36. The annual performance report for the year under review did not include the performance of each external services provider and a comparison with the previous financial year as required by section 46 (1)(a) of the MSA.

## **Expenditure management**

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

## **Procurement and contract management**

39. Sufficient appropriate audit evidence could not be obtained to confirm that all contracts were awarded in accordance with the legislative requirements and a procurement process which is fair, equitable, transparent and competitive, as the municipality did not provide all documentation to provide evidence of a competitive bidding process.
40. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulations 17(a) & (c).
41. Contracts and quotations were awarded to 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).





42. Awards were made to 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 44. Similar awards were identified in the previous year and no effective steps were taken to prevent or combat the abuse of the SCM process, as required by SCM regulation 38(1).
43. Contracts were awarded to providers whose tax matters had not been declared to be in order by the South African Revenue Service, in contravention of SCM regulation 43.

## **Revenue management**

44. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.
45. Revenue due to the municipality was not calculated on a monthly basis, as required by section 64(2)(b) of the MFMA.

## **Consequence management**

46. Unauthorised, irregular and fruitless and wasteful expenditure, incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in accordance with the requirements of sections 32(2)(a) and (b) of the MFMA.
47. Council did not always approve the terms of reference of each investigation as required by regulation 6(1) of the Municipal regulations on financial misconduct procedures and criminal proceedings.

## **Liability management**

48. An adequate management, accounting and information system which accounts for liabilities was not in place, as required by section 63(2)(a) of the MFMA.

## **Environmental management**

49. The municipality did not exercise its legislative and executive authority of managing, monitoring and enforcing environmental related bylaws to promote a safe and healthy environment as required by section 11(3)(l) and (m) of the MSA.
50. The municipality operated its wastewater treatment facility's without a license in contravention of section 24(2)(a) of the National Environmental Management Act, 1998 (Act No. 107 of 1998) (NEMA) and section 22(1)(b) of the National Water Act, 1998 (Act No. 36 of 1998) (NWA). The municipality's operational activities at its waste disposal sites and wastewater treatment facility contravened or failed to comply with the requirements of a waste management license or the norms and standards as prescribed by sections 67(1)(f) and (h) of the National Environmental Management Waste Act, 2008 (Act No. 59 of 2008) (NEMWA) and sections 151(1)(c) and (i) of the NWA.
51. The municipality's waste management and disposal activities contravened and failed to comply with the requirements of section 28(1) of the NEMA, section 19 of the NWA and sections 16(1)(c) and (d) and 26(1)(b) of the NEMWA.

## **Internal control**

52. I considered internal control relevant to my audit of the financial statements, the annual performance report and compliance with legislation. 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**

53. Action plans did not adequately address prior year audit findings and policies and procedures implemented did not enable and support the understanding and execution of internal control objectives, processes, and responsibilities. The establishment of a culture of honestly, ethical business practices and good governance requires urgent intervention. Leadership failed to appoint sufficient appropriately skilled staff in key positions within the finance unit and the training and development initiatives failed to address the underlying deficiencies that caused matters to be reported on repeatedly.

## **Financial and performance management**

54. The accounting officer did not ensure that adequate monitoring controls were implemented to ensure that reliable financial and performance reports were collated throughout the year as part of his periodic reporting responsibilities. The disinclination to implement preventative internal control measures to address prior year audit findings pertaining to financial and performance reporting and non-compliance with laws and regulation is evident. Management's inability to address repetitive findings relating to supply chain management regulations could be indicative of financial misconduct.

## **Governance**

55. The audit committee and the internal audit unit were not functioning for the majority of the financial year and the impact of the lack of appropriate monitoring and oversight is evident from the audit findings on financial and performance reporting and non-compliance with laws and regulation.

## **Other reports**

56. I draw attention to the following engagement that could potentially impact on the municipality's financial performance and compliance related matters. My opinion is not modified in respect of these engagements that are in progress.

## **Investigations**

57. An investigation was initiated by Presidential Proclamation and is conducted by the Special Investigations Unit (SIU) on allegations of supply chain management irregularities. The investigation was not yet finalised on date of this report.
58. An investigation was initiated by Accounting Officer and is conducted by the Hawks on allegations of supply chain management irregularities. The investigation was not yet finalised on the date of this report.
59. An investigation was initiated by Accounting Officer and is conducted by South African Police Service (SAPS) on allegations of supply chain management irregularities. The investigation was not yet finalised on the date of this report.





*Auditor General*

Rustenburg  
30 November 2016



AUDITOR-GENERAL  
SOUTH AFRICA

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