

Blue Crane Route Local Municipality

Audit Report

For the year ended 30 June 2018

Report of the auditor-general to the Eastern Cape Provincial Legislature and council on Blue Crane Route Municipality

Report on the audit of the financial statements

Opinion

1. I have audited the financial statements of the Blue Crane Route Municipality set out on pages ... to ..., which comprise statement of financial position as at 30 June 2018, and the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget information 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, the financial statements present fairly, in all material respects, the financial position of the Blue Crane Route Municipality as at 30 June 2018, 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 Division of Revenue Act of South Africa, 2017 (Act No.03 of 2017) (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 this 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) 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.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Material uncertainty relating to going concern

6. I draw attention to the matter below. My opinion is not modified in respect of this matter.
7. I draw attention to note 46 to the financial statements, which indicates that current liabilities exceed current assets, net deficits been realised in the current and prior year, high level of water and electricity losses and debt and credit payment ratio's not in the norm. As stated in note 46, these events or conditions, along with the other matters as set forth in note 46, indicate that a material uncertainty exists that may cast significant doubt on the municipality's ability to continue as a going concern.

Emphasis of matters

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

Unauthorised expenditure

9. As disclosed in note 48 to the financial statements, the municipality incurred unauthorised expenditure of R1,6 million (2016-17 R8 million), mainly due to overspending on budget votes.

Irregular expenditure

10. As disclosed in note 50 to the financial statements, the municipality incurred irregular expenditure of R12 million (2016-17 R15,1 million), mainly due to contravention of supply chain management regulations.

Material losses

11. As disclosed in note 27 to the financial statements, the municipality incurred material electricity losses of R9,1 million (2016-2017: R11 million), which represents 19% (2016-17: 22%) of total electricity purchased and material water losses of R5,6 million (2016-17: R6,5 million), which represents 48% (2016-17: 48%) of total water purchased.

Allowance for impairment

12. As disclosed in note 33 to the financial statements, the municipality incurred material losses of R8,9 million (2016-17: R13,4 million), as a result of a write-off of irrecoverable trade debtors.

Restatement of corresponding figures

13. As disclosed in note 44 to the financial statements, the corresponding figures for 30 June 2017 have been restated as a result of errors in the financial statements of the municipality identified at, and for the year ended 30 June 2018.

Other matter paragraph

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

Unaudited supplementary schedules

15. The supplementary information set out on pages 71 to 87 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 on them.

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 GRAP and the requirements of the MFMA, 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 Blue Crane Route 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

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 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 this auditor’s report.

Report on the audit of the annual performance report

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 development priorities 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 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 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
Key performance area (KPA) 2: 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 development priorities are as follows:

KPA 2: basic service delivery and infrastructure development

KPI 23: number of days per week household and business refuse is collected

25. I was unable to obtain sufficient appropriate audit evidence for target, number of days per week on which household and business refuse is collected, that clearly measured the predetermined nature and required level of performance and method of calculation. This was due to a lack of proper systems and processes to ensure that the method of calculation is clearly defined. I was unable to test whether the target for this indicator was clearly defined by alternative means.

KPI 29: number of water samples taken for chemical bacteriological analysis

26. The planned target for this indicator was not specific in clearly identifying the nature and required level of performance as it did not provide a breakdown of the target per the different categories of tests to be performed.

KPI 21: number of kilometres of gravel roads upgraded to paved roads in Nelsig, Khanyiso, Millennium Park, Old location and Bhongweni

27. The planned target for this indicator was not specific in clearly identifying the nature and required level of performance as it did not provide a breakdown of the target per the different areas.

Various indicators

28. I was unable to obtain sufficient appropriate audit evidence to support the measures taken to improve performance for the indicators listed as reported in the annual performance report. This was due to measures not being appropriately disclosed and non-submission of corroborating evidence. I was unable to confirm the reported measures taken by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported measures taken to improve performance:

- KPI 15 - Number of transformers purchased
- KPI 16 – Recloser procured for Somerset East Main substation
- KPI 17 – 4MVA transformer refurbished in SE main substation
- KPI 31 - Number of roadblocks conducted at National roads in BCRM area
- KPI 32 – Number of pounds constructed
- KPI 21 – Number of kilometres of gravel roads upgraded to paved roads in Nelsig, Khanyiso, Millennium Park, Old location and Bhongweni.

Other matters

29. I draw attention to the matters below.

Achievement of planned targets

30. Refer to the annual performance report on pages x to x for 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 of the reported performance information in paragraphs 19 to 22 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 on the key performance area of basic service delivery and infrastructure development. As management subsequently corrected only some of the misstatements, we raised material findings on the usefulness of the reported performance information. Those that were not corrected are reported above.

Report on the 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 on compliance with specific matters in key legislations are as follows:

Annual financial statements

34. 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. Material misstatements identified by the auditors in the submitted financial statement were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.

Human resource management

35. Financial interest was not disclosed by the municipal manager within 60 days from date of appointment, as required by regulation 36(1)(a) on appointment and conditions of employment of senior managers.

36. Financial interest was not disclosed by the senior manager within 60 days from date of appointment, as required by regulation 36(1)(a) on appointment and conditions of employment of senior managers.

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. Reasonable steps were not taken to prevent irregular expenditure amounting to R12 million as disclosed in note 50 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by non-compliance with SCM regulations.
39. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R1,6 million, as disclosed in note 48 of the annual financial statements, as required by section 62(1)(d) of the MFMA.

Asset management

40. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.
41. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Procurement and contract management

42. Some of the goods and services with a transaction value of below R200 000 were procured without obtaining the required number of price quotations, in contravention of SCM regulation 17(a) and (c). Similar non-compliance was also reported in the prior year.
43. Some of the contracts were extended or modified without the approval of a properly delegated official, in contravention of SCM regulation 5. Similar non-compliance was also reported in the prior year.

Other information

44. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes the mayor's foreword, executive summary, governance, organisational development performance and financial performance. 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 the auditor's report.
45. Our opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and we do not express an audit opinion or any form of assurance conclusion thereon.
46. In connection with our audit, our 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 report¹, or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

47. 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

48. 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. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on the key performance area of service delivery and infrastructure development and the findings on compliance with legislation included in this report.
49. The municipality did not have sufficient monitoring controls to ensure the proper implementation of the overall process of planning, budgeting, implementation and reporting and this impacted the financial and performance management systems, resulting in material findings identified on compliance and performance information.
50. The municipality does not have a performance management system in place for employees other than managers directly reporting to the municipal manager. There are also no proper processes in place to ensure that annual declarations are signed by all the employees before the deadline date.
51. The municipality did not properly monitor compliance with the policies as evidenced by material findings on performance information and compliance. Management also did not timeously monitor adherence to the audit action plan, which resulted in a number of repeat findings reported.
52. The municipality did not have a proper record management system to maintain information that supported the reported performance in the annual performance report. This included information that related to the collection, collation, verification, storing and reporting of actual performance information.
53. The financial statements submitted for auditing contained material misstatements, that were subsequently corrected as proper systems of monthly review were not implemented to ensure that misstatements are prevented, detected and corrected timeously. The annual performance report also contained material misstatements due to a lack of proper review, which includes scrutinising and verifying the supporting evidence for each target reported in the annual performance report.

54. The municipality did not have adequate processes in place to detect or prevent non-compliance with laws and regulations, which resulted in material non-compliance findings being reported. More emphasis needs to be placed in the area of adherence with unauthorised, irregular expenditure and compliance with SCM regulations.

Auditor - General

East London

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 Blue Crane Route 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.
 - obtain sufficient appropriate audit evidence regarding the financial information of the municipality to express an opinion on the financial statements. I am responsible for the direction, supervision and performance of the audit. I remain solely responsible for my audit opinion.

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.

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.