

# Report of the auditor-general to the Northern Cape provincial legislature and the council on Karoo Hoogland Local Municipality

## Report on the financial statements

### Introduction

1. I have audited the financial statements of the Karoo Hoogland Municipality set out on page 8 to 69, which comprise the statement of financial position as at 30 June 2015, the statement of financial performance, statement of changes in net surplus, cash flow statement and Actual versus budget 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 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 qualified audit opinion.

## Basis for qualified opinion

### Property Plant and equipment

6. I was unable to obtain sufficient appropriate audit evidence regarding property, plant and equipment, as the municipality did not have adequate systems in place. I could not confirm this by alternative means. Consequently, I was unable to determine whether any adjustment to property, plant and equipment stated at R281 533 256 (2014: R282 295 835) in the financial statements was necessary.

### Commitments

7. During 2014, I was unable to obtain sufficient appropriate audit evidence regarding the amount of R12 098 528 disclosed in the current year financial statements and I could not confirm this by alternative means. My opinion on the current period's financial statements is also modified because of the possible effect of this matter on the comparability of the current period's figures.

### Taxes

8. During 2014, I could not obtain sufficient appropriate audit evidence for an unexplained difference of R854 436 between the amount per the general ledger and the VAT returns. This could not be confirmed by alternative means. Consequently I was unable to determine whether any adjustment to taxes stated at R796 491 was necessary. My opinion on the current period's financial statements is also modified because of the possible effect of this matter on the comparability of the current period's figures.

### Fruitless and wasteful expenditure

9. During 2014, the municipality did not include particulars of fruitless and wasteful expenditure in the notes to the financial statements as required by section 125(2)(d) of the MFMA. The municipality incurred expenditure that was made in vain and that would have been avoided had reasonable care been exercised which were not disclosed as fruitless and wasteful expenditure, resulting in fruitless and wasteful expenditure being understated by R193 618. My opinion on the current period's financial statements is also modified because of the possible effect of this matter on the comparability of the current period's figures.

### Cash flow statement

10. During 2014, I was unable to obtain sufficient appropriate audit evidence to determine whether the cash flow statement and the related notes were fairly stated. Taking into account the misstatements and scope limitations identified in the financial statements, as set out in this report, I was unable to practically quantify the misstatements in the cash flow statement and notes thereto. Consequently, I was unable to determine the correctness of the cash flow statement and related notes.

## **Qualified opinion**

11. 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 the Karoo Hoogland Municipality as at 30 June 2015 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**

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

## **Restatement of corresponding figures**

13. As disclosed in note 48 to the financial statements, the corresponding figures for 30 June 2014 have been restated as a result of an error discovered during 30 June 2015 in the financial statements of the municipality at, and for the year ended, 30 June 2014

## **Material losses**

14. As disclosed in note 36.5 to the financial statements, a material loss of R677 838 (10.45%) was incurred as a result of the distribution of electricity.

## **Material impairments**

15. As disclosed in note 15 and 16 to the financial statements, a significant provision for the impairment of receivables from exchange transactions and non-exchange transactions was recognised which constitutes 54% of the total receivables from exchange transactions and non-exchange transactions balance respectively.

## **Contingent liabilities**

16. With reference to note 46 to the financial statements, the municipality was summoned for the unlawful suspension of senior officials. The ultimate outcome of the matter cannot presently be determined and no provision for any liability that may result has been made in the financial statements.

## **Additional matters**

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

## **Unaudited supplementary schedules**

18. The supplementary information set out on appendixes A and B 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.

## **Unaudited disclosure notes**

19. 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.

## **Report on other legal and regulatory requirements**

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 findings on the reported performance information against predetermined objectives for selected development objectives 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**

21. I am unable to report on the usefulness and reliability of the performance information, as the annual performance report of the municipality was not prepared as required by section 46 of the Municipal Systems Act and section 121(3)(c) of the MFMA.

## **Compliance with legislation**

22. 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:

## **Strategic planning and performance management**

23. The municipality did not develop and adopt appropriate systems (policies) and procedures to monitor, measure and evaluate performance of staff in contravention of MSA sec 67(d).

## **Financial statements, performance and annual reports**

24. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA.
25. Material misstatements identified by the auditors in the submitted financial statements were not adequately corrected and the supporting records could not be provided subsequently, which resulted in the financial statements receiving a qualified audit opinion.

## **Audit committees**

26. An audit committee was not in place, as required by section 166(1) of the MFMA.
27. A performance audit committee was not in place and the audit committee was not used to fulfil the performance audit committee function, as required by Municipal Planning and Performance Management regulation 14(2)(a).

## **Internal audit**

28. An internal audit unit was not established, as required by section 165(1) of the MFMA.

## **Procurement and contract management**

29. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM Regulation 17(a) & (c).
30. Bids were not always evaluated by bid evaluation committees which were composed of at least one SCM practitioner of the municipality as required by SCM Regulation 28(2).
31. Contracts and quotations were awarded to bidders based on points given for criteria that differed from those stipulated in the original invitation for bidding and quotations, in contravention of SCM Regulations 21(b) and 28(1)(a) and the Preferential Procurement Regulations.
32. Bid adjudication was not always done by committees which were composed in accordance with SCM Regulation 29(2).
33. The preference point system was not applied in all procurement of goods and services above R30 000 as required by section 2(a) of the Preferential Procurement Policy Framework Act and SCM Regulation 28(1)(a).
34. Contracts and quotations were awarded to bidders based on preference points that were not calculated in accordance with the requirements of the Preferential Procurement Policy Framework Act and its Regulations.
35. 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).
36. Contracts were extended without tabling the reasons for the proposed amendment in the council of the municipality, as required by section 116(3) of the MFMA.
37. Contracts were extended without the approval of a properly delegated official, as required by SCM Regulation 5.

## **Human resource management and compensation**

38. The annual report of the municipality did not reflect information on compliance with prescribed minimum competencies as required by the Regulations on Minimum Competency Levels Regulation 14(2)(b).

## **Expenditure management**

39. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
40. 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.

## **Asset and liability management**

41. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

## **Consequence management**

42. 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 section 32(2) of the MFMA.
43. The condoning of irregular expenditure was not approved by the appropriate relevant authority, in accordance with the requirements of sections 1 and 170 of the MFMA.
44. Authorisation of unauthorised expenditure was not done through an adjustment budget, as required by section 32(2)(a)(i) of the MFMA.

## **Internal control**

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

## **Leadership**

46. The accounting officer did not exercise oversight responsibility over the preparation of the financial statements, the report on predetermined objectives, compliance with laws and regulations, and internal control. The leadership did not implement processes to ensure that reviews took place before information was submitted. This was evidenced by the material misstatements in the financial statements, non-compliance with laws and regulations and internal control deficiencies noted throughout the audit process.
47. Senior management did not adhere to internal controls, which resulted in various instances of irregular and unauthorised expenditure being incurred and other material misstatements in the financial statements, not detected by management.
48. Management is in process to establish, update and communicate policies and procedures to enable and support the understanding and execution of internal control objectives, processes, and responsibilities within the municipality.

## Financial and performance management

49. Material misstatements were made in the financial statements as these were not accurate and complete, because senior management did not detect misstatements during the review process. This indicates that there were weaknesses in internal control with regard to the review process of the financial statements. Furthermore, the financial statements were not sufficiently reviewed for completeness and accuracy prior to submission for auditing.
50. There were deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations.
51. The supply chain management unit of the municipality did not always function effectively. The necessary procedures were not always followed.
52. Specific training interventions are needed in the municipality to enable finance staff members to understand and implement the GRAP Financial Reporting Framework effectively in order to fully meet the disclosure requirements of these standards.

## Governance

53. Appropriate a risk management activity was not implemented to ensure that regular risk assessments, including consideration of IT risks and fraud prevention, are conducted and that a risk strategy to address the risks is developed and monitored.
54. The accounting officer did not ensure that there is an adequately resourced and functioning internal audit unit that identifies internal control deficiencies and recommends corrective action effectively
55. The audit committee did not promote accountability and service delivery through evaluating and monitoring responses to risks and providing oversight over the effectiveness of the internal control environment, including financial and performance reporting and compliance with laws and regulations.

Kimberley

30 November 2015



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*