



AUDITOR-GENERAL
SOUTH AFRICA

The Accounting Officer
Mkhondo Local Municipality
P.O Box 23
Piet Retief
2380

30 November 2017

Reference: 02394REG16/17

Dear Sir

Report of the Auditor-General on the financial statements and other legal and regulatory requirements of Mkhondo Local Municipality for the year ended 30 June 2017

1. The above-mentioned report of the Auditor-General is submitted herewith in terms of section 21(1) of the Public Audit Act of South Africa read in conjunction with section 188 of the Constitution of the Republic of South Africa and section 121(3) of the Municipal Finance Management Act of South Africa (MFMA)
2. We have not yet received the other information that will be included in the annual report with the audited financial statements and have thus not been able to establish whether there are any inconsistencies between this information and the audited financial statements and the reported performance against pre-determined objectives. You are requested to supply this information as soon as possible. Once this information is received it will be read and should any inconsistencies be identified these will be communicated to you and you will be requested to make the necessary corrections. Should the corrections not be made we will amend and reissue the audit report.
3. In terms of section 121(3) of the MFMA you are required to include the audit report in the municipality's annual report to be tabled.
4. Until the annual report is tabled as required by section 127(2) of the MFMA, the audit report is not a public document and should therefore be treated as confidential.
5. Prior to printing or copying the annual report which will include the audit report you are required to do the following:
 - Submit the final printer's proof of the annual report to the relevant senior manager of the Auditor-General of South Africa for verification of the audit-related references in the audit report and for confirmation that the financial statements and other information are those documents that have been read and audited. Special care should be taken with the page references in your report, since an incorrect reference could have audit implications.
 - The signature *Auditor-General* in the handwriting of the auditor authorised to sign the audit report at the end of the hard copy of the audit report should be scanned in when preparing to print the report. This signature, as well as the place and date of signing and the Auditor-General of South Africa's logo, should appear at the end of the report, as in the hard copy that is provided to you. The official logo will be made available to you in electronic format.

6. Please notify the undersigned Senior Manager well in advance of the date on which the annual report containing this audit report will be tabled.
7. Your cooperation to ensure that all these requirements are met would be much appreciated.

Kindly acknowledge receipt of this letter.

Yours sincerely



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Senior Manager: Mpumalanga Business Unit

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Report of the auditor-general to the Mpumalanga Provincial Legislature and the council on the Mkhondo Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Mkhondo Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2017, 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 to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the effects of the matters described in the basis for qualified opinion section of my report, the financial statements present fairly, in all material respects, the financial position of the Mkhondo 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 qualified opinion

Property, plant and equipment

3. In terms of GRAP 17, *Property, plant and equipment*, the municipality should account for all the assets they have control over at the end of the financial year. Contrary to this, the municipality did not maintain proper systems to record and account for all assets. Assets to the value of R54 645 432 could not be physically verified. Unreconciled differences of R10 240 072 arose between the fixed asset registers and the accounting records. Consequently, I was unable to determine whether property, plant and equipment of R1 381 583 488 (2015-16: R1 372 635 401) disclosed in note 10 to the financial statements and the depreciation expense of R70 177 996 (2015-16: R72 299 029) disclosed in note 31 to the financial statements were fairly stated.

Biological assets

4. In terms of GRAP 27, *Agriculture*, the municipality should disclose the amount of a change in fair value less costs to sell due to physical and price changes. Contrary to this, the municipality did not account for all physical changes. Assets to the value of R7 402 304 were not adequately adjusted due to fire damage. Consequently, I was unable to determine whether any further adjustments were necessary to the biological assets of R58 873 012 disclosed in note 8 to the financial statements.

Context for the opinion

5. 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.
6. 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.
7. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Emphasis of matters

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

Material losses

9. As disclosed in note 45 to the financial statements, material losses of R22 591 918 (2015-16: R30 130 496) were incurred as a result of electricity distribution losses, which represented 20% (2015-16: 31%) of the total electricity purchased. Material losses of R129 204 (2015-16: R759 363) were incurred as a result of water distribution losses, which represented 6% (2015-16: 27%) of the total water purchased.

Material impairments

10. As disclosed in note 6 to the financial statements, the receivables balance was significantly impaired. The impairment of consumer debtors amounted to R228 442 973 (2015-16: R168 404 721), which represented 84% (2015-16: 84%) of the total consumer debtors. The contribution to the provision for debt impairment was R60 038 252 (2015-16: R29 265 728).

Other matters

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

Unaudited supplementary schedules

12. The supplementary information set out on pages ... to ... 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

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

Responsibilities of the accounting officer for the financial statements

14. 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.
15. In preparing the financial statements, the accounting officer is responsible for assessing the 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 accounting officer 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

16. 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.
17. 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

18. 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 departments presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
19. 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.
20. 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 departments presented in the annual performance report of the municipality for the year ended 30 June 2017:

Departments	Pages in the annual performance report
Department: technical services	x – x
Department: community services	x – x

21. 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.

22. The material findings in respect of the usefulness and reliability of the selected departments are as follows:

Department: technical services

23. The following indicators were not consistent when compared to the indicators in the approved annual performance plan:

- No. of HHs connected
- Number of ML waste water drained from septic tanks
- Inspected/reported faulty lights attended to by personnel
- Maintenance of 3 intersection
- Number of new request
- Number of graves prepared, closed and paper work processed
- No. of km bulk pipeline constructed/laid
- No. of pump station contracted/laid
- No. of reservoir and elevated tanks constructed
- 15 transformers maintained and oil sampled
- Maintenance of breakers & RMU

24. The following indicators were not well defined or verifiable:

- No. of HHs connected
- Number of HH reticulated
- Lines maintain per KM
- Number of awareness campaign
- Square meters
- Maintenance of breakers & RMU
- No. of bulk meters

25. The following indicators were not presented appropriately, as the measures to improve performance were not disclosed and/or supported:

- Number of awareness campaigns
- Number of MI of treated water
- Number of ML waste water drained from septic tanks
- Number of waste water samples analysed
- Number of water samples analysed

- 20 new street lights installed
- Lines maintain per KM
- Number kilometres of storm water pipes maintained
- Number of Km of gravelled, bladed and levelled roads
- No. of km bulk pipeline constructed/laid
- No. of reservoir constructed. No of tests conducted on the reservoir
- No. of pump station contracted/laid
- No. of river crossing bridges constructed and Km of road
- Km's access road constructed, number of grave space created, km's palisade fence constructed
- No. of relays replaced
- Maintenance of breakers & RMU
- No. of electric testers procured
- No. of bulk meters

26. I was unable to obtain appropriate audit evidence for the reported achievement of the targets due to limitations placed on the scope of my work. I was unable to confirm the reported achievements by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements of the following indicators:

- Number of reviewed & developed operations & maintained manuals, procedures/plans, assets management, water safety plan & W2RAP
- Number of awareness campaigns
- Number of MI of treated water
- MI of treated water
- No. of HHs connected
- Number of ML of waste water treated
- Number of waste water samples analysed
- Number of water samples analysed
- Number of HH reticulated
- 20 new street lights installed
- Inspected/reported faulty lights attended to by personnel
- Lines maintain per KM
- Maintenance of 3 intersection
- Number of awareness campaign
- Number of new request
- Square meters
- Number kilometres of storm water pipes maintained
- Number of Km of gravelled, bladed and levelled roads
- No. of Km of gravel roads bladed/levelled
- Number of graves prepared, closed and paper work processed
- No. of km bulk pipeline constructed/laid
- No. of reservoir and elevated tanks constructed
- No. of pump station constructed
- No. of km bulk pipeline constructed
- % of municipal offices, library and community halls constructed
- 15 transformers maintained and oil sampled
- No. of relays replaced
- Maintenance of breakers & RMU

- No. of bulk meters
- Number of catch pits cleaned

27. The reported achievements for the targets were misstated, as the evidence provided did not agree with the reported achievements as follows:

- Number of water conservation and water demand management programs implemented
- Number of ML waste water drained from septic tanks

Department: community services

28. The following indicators were not consistent when compared to the indicators in the approved annual performance plan:

- No. of streets cleaned
- No. of parks that are cleaned and maintained
- Number of km litter pick
- Waste reports submitted DEA
- No. of greening at eMkhondo
- No. of safety campaigns
- % of learner class conducted
- No. of driver license test conducted
- Number of fire awareness campaigns conducted
- No. road blocks to be conducted
- No. of transport forum meetings conducted
- No. of CSF meetings
- No. of sports tournaments held
- No. of cultural events held
- No. of library outreach programmes conducted
- No. of stakeholder's awareness and clean-up campaigns held

29. The following indicators were not well defined or verifiable:

- No. of new households with refuse collection services
- No. of times recreational facilities are cleaned and maintained
- Number of km litter pick
- Waste reports submitted DEA
- No. of greening at eMkhondo
- No. of CSF meetings
- % training of officials and councillors on fire fighting
- No. of sports tournaments held
- No. of cultural events held
- No. of library outreach programmes conducted
- No. of stakeholder's awareness and clean-up campaigns held

30. The following indicators were not presented appropriately, as the measures to improve performance were not disclosed and/or supported:

- No. of trips for removal of refuse containers in commercial buildings
- No. of times recreational facilities are cleaned and maintained

- % of learner class conducted
- No. of driver license test conducted
- No. of CSF meetings
- % training of officials and councillors on fire fighting

31. I was unable to obtain appropriate audit evidence for the reported achievement of the targets due to limitations placed on the scope of my work. I was unable to confirm the reported achievements by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements of the following indicators:

- No. of trips to collect refuse in serviced areas
- No. of new households with refuse collection services
- No. of trips for removal of refuse containers in commercial buildings
- % of illegal dumping spots identified and cleared
- % compliance with DEA standards
- No. of parks that are cleaned and maintained
- No. of times recreational facilities are cleaned and maintained
- Number of km litter pick
- No. of greening at eMkhondo
- No. of safety campaigns
- % of fire awareness campaigns conducted
- No. road blocks to be conducted
- No. of transport forum meetings conducted
- No. of CSF meetings
- % of revenue generated on abnormal vehicles escorted as per planned escorts and requests
- No. of sports tournaments held
- No. of library outreach programmes conducted
- No. of stakeholder's awareness and clean-up campaigns held

32. The reported achievements for the targets were misstated, as the evidence provided did not agree with the reported achievements as follows:

- Waste reports submitted DEA
- 30 informal businesses to be inspected
- No. of cultural events held

Other matter

33. I draw attention to the matter below.

Achievement of planned targets

34. Refer to the annual performance report on pages x to x and x to x for information on the achievement of planned targets for the year and explanations provided for the under- or overachievement of a number of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 23 to 32 of this report.

Introduction and scope

35. 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.
36. The material findings on compliance with specific matters in key legislation are as follows:

Annual financial statements, performance report and annual report

37. 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 expenditure and financial instruments identified by the auditors in the submitted financial statements were subsequently corrected but the uncorrected material misstatements of biological assets and property, plant and equipment resulted in the financial statements receiving a qualified audit opinion.

Asset management

38. An adequate management, accounting and information system was not in place to account for assets, as required by section 63(2)(a) of the MFMA.
39. An effective system of internal control for assets (including an asset register) was not in place, as required by section 63(2)(c) of the MFMA.

Budget

40. Reasonable steps were not taken to prevent unauthorised expenditure, as required by section 62(1)(d) of the MFMA. The majority of the disclosed unauthorised expenditure was caused by the overspending on votes.

Consequence management

41. All unauthorised expenditure incurred by the municipality was not investigated to determine if any person was liable for the expenditure, as required by section 32(2)(a) of the MFMA.
42. Unauthorised expenditure amounting to R55 100 011 was not authorised through an adjustment budget, as required by section 32(2)(a)(i) of the MFMA.
43. All of the irregular expenditure incurred by the municipality was not investigated to determine if any person was liable for the expenditure, as required by section 32(2)(b) of the MFMA.
44. All of the fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person was liable for the expenditure, as required by section 32(2)(b) of the MFMA.

45. Allegations of theft, fraud or forgery that exceeded R100 000 were not reported to the South African Police Service, as required by section 34(1) of the Prevention and Combating of Corrupt Activities Act of South Africa, 2004 (Act No.12 of 2004).

Expenditure management

46. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
47. Effective steps were not taken to prevent irregular expenditure amounting to R86 744 482, as disclosed in note 44 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The majority of the disclosed irregular expenditure was caused by non-compliance as a result of incorrect procurement and contract management processes.
48. Effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R8 822 975, as disclosed in note 43 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by interest charged on overdue accounts.

Procurement and contract management

49. 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 supply chain management (SCM) regulation 13(c).
50. Quotations were accepted from bidders whose tax matters had not been declared by the South African Revenue Service to be in order, in contravention of SCM regulation 43.
51. Some goods and services with a transaction value above R200 000 were procured without inviting competitive bids, contrary to SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).
52. Some contracts were awarded to providers whose tax matters had not been declared by the South African Revenue Service to be in order, in contravention of SCM regulation 43.
53. Some contracts and quotations were awarded to bidders based on preference points that had not been allocated and/or calculated in accordance with the requirements of the Preferential Procurement Policy Framework Act of South Africa, 2000 (Act No. 5 of 2000) and its regulations.
54. Awards were made to providers who were in the service of other state institutions or whose directors were in the service of other state institutions, in contravention of section 112(j) of the MFMA and SCM regulation 44.

Revenue management

55. A credit control and debt collection policy was not maintained, as required by section 96(b) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) and section 62(1)(f)(iii) of the MFMA.

Other information

56. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report, which includes the audit committee's report. The other information does not include the financial statements, the auditor's report thereon and those selected departments presented in the annual performance report that have been specifically reported on in the auditor's report.
57. 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.
58. 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 development priorities 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.
59. I have read the other information included in the draft annual report and have nothing to report in this regard.
60. I have not yet received the final annual report containing the other information. When I do receive this information, and if I conclude that it contains a material misstatement, I am required to communicate the matter to those charged with governance and to request the other information to 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

61. 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.
62. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

Leadership

63. The accounting officer did not exercise oversight responsibility regarding financial and performance reporting and compliance as well as related internal controls.

Financial and performance management

64. Management did not ensure that controls were implemented over daily and monthly processing and reconciling of transactions.
65. Management did not prepare regular, accurate and complete financial and performance reports that were supported and evidenced by reliable information.

66. Management did not monitor compliance with applicable laws and regulations.

Governance

67. The audit committee and internal audit unit did not have positive impact on the internal control environment, as their recommendations were not implemented effectively.

Auditor-General

Mbombela

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 departments 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 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, where applicable, related safeguards.