# Report of the auditor-general to the KwaZulu-Natal Provincial Legislature and the council on Umzinyathi District Municipality

## Report on the audit of the financial statements

### Qualified opinion

1. I have audited the financial statements of the Umzinyathi District Municipality set out on pages x to x, which comprise the statement of financial position as at 30 June 2021, 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 notes to the financial statements, including a summary of significant accounting policies.

2. In my opinion, except for the effect and possible effects of the matters described in the basis for qualified opinion section of this auditor's report, the financial statements present fairly, in all material respects, the financial position of the Umzinyathi District Municipality as at 30 June 2021, 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, 2020 (Act No. 4 of 2020) (Dora).

### Basis for qualified opinion

#### Cash and cash equivalents

3. The municipality did not correctly disclose the cash book balances in the notes to the financial statements as required by section 125(a)(ii) of the MFMA. The cash book balances as disclosed in note 7 to the financial statements was overstated by R11,37 million (2019-2020: R2,37 million).

#### Service charges

4. Revenue from the sale of water was incorrectly calculated due to incorrect tariffs being used and unexplainable differences between the amounts per billings reported and the amounts disclosed in the financial statements. I was unable to determine the full extent of the misstatement of the revenue from exchange transactions reported at R74,78 million (2019-2020: R82,81 million) and the related receivables from exchange transactions of R140,53 million (2019-2020: R116,95 million) in the financial statements as it was impracticable to do so. Additionally, there was an impact on the surplus for the period and on the accumulated surplus.

5. I was unable to obtain sufficient appropriate audit evidence to support the free basic services. I was unable to confirm using alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the free basic services stated at R17,06 million (2019-2020: R9,19 million) as per note 21 of the financial statements.

### Contracted services

6. In the prior-year, I was unable to obtain the sufficient appropriate evidence for the contracted services and to confirm the expenditure by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the contracted services expenditure stated at R135,42 million. My audit opinion on the financial statements for the period ended 30 June 2020 was modified accordingly. My opinion on the current year financial statements was also modified because of the possible effect of this matter on the comparability of the contracted services expenditure for the current period.

### General expenditure

7. I was unable to obtain sufficient appropriate audit evidence that payments for general expenditure were in respect of goods and services that were actually received, as the municipality did not have adequate systems to confirm receipt of goods and services before effecting payments. I could not confirm expenditure by alternate means. Consequently, I was unable to determine whether any further adjustments were necessary to the general expenditure stated at R172,02 million as per note 36 of the financial statements.

## Context for the opinion

8. 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.

9. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *International code of ethics for professional accountants (including International Independence Standards)* (IESBA code) as well as other 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.

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

## Emphasis of matters

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

### Material impairment provision – Trade and other receivables from exchange transactions

12. As disclosed in note 6 to the financial statements, the municipality recognised a material provision on the impairment of trade and other receivables from exchange, amounting to R247,90 million (2019-2020: R189,09 million) as the recovery of these amounts were doubtful.

### Material losses – Water distribution

13. As disclosed in note 46 of the financial statement, the municipality had water distribution loss of R33,72 million (2019-2020: R23,78 million) this was mainly due to water leaks caused by aging infrastructure.

### Restatements of corresponding figures

14. As disclosed in note 39 to the financial statements, the corresponding figures for 30 June 2020 were restated as a result of the errors in the financial statements of the municipality at, and for the year ended, 30 June 2021.

## Other matter

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

### Unaudited disclosure notes

16. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion on it.

## Responsibilities of the accounting officer for the financial statements

17. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with 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.

18. 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 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

19. 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.

20. 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

### Introduction and scope

21. 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 on the usefulness and reliability of the reported performance information against predetermined objectives for selected development priority presented in the annual performance report. I performed procedures to identify material findings but not to gather evidence to express assurance.

22. My procedures address the usefulness and reliability of the reported performance information, which must be based on the municipality's approved performance planning documents. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures do not examine whether the actions taken by the municipality enabled service delivery. My procedures do not extend to any disclosures or assertions relating to the extent of achievements in the current year or 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.

23. 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 *basic service delivery and infrastructure development priority* presented in the municipality's annual performance report on pages xx to xx for the year ended 30 June 2021.

24. 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.

25. I did not identify material findings on the usefulness and reliability of the reported performance information for the basic service delivery and infrastructure development priority.

### Other matters

26. I draw attention to the matters below.

#### Achievement of planned targets

27. The annual performance report on pages x to x sets out information on the achievement of planned targets for the year.

### Adjustment of material misstatements

28. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information of the basic service delivery and infrastructure development priority. As management subsequently corrected the misstatements, I did not raise any material findings on the usefulness and reliability of the reported performance information.

## Report on the audit of compliance with legislation

### Introduction and scope

29. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the municipality's compliance with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

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

### Financial statements

31. 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 of property plant and equipment, receivables from exchange transactions, commitments, prior period error, related parties as well as statement of comparison of budget and actual amounts, identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements and the supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

### Expenditure management

32. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R292,55 million, as disclosed in note 53 to annual financial statements, in contravention of section 62(1)(d) of the MFMA.

33. Reasonable steps were not taken to prevent irregular expenditure amounting to R299,92 million as disclosed in note 44 to the financial statements, in contravention of section 62(1)(d) of the MFMA.

### Consequence management

34. Unauthorised expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in contravention of section 32(2)(a) of the MFMA.

35. Irregular expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in contravention of section 32(2)(b) of the MFMA.

36. Fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in contravention of section 32(2)(b) of the MFMA.

### Revenue management

37. An effective system of internal control for revenue was not in place, in contravention of section 64(2)(f) of the MFMA.

### Procurement and contract management

38. 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 by SCM Regulation 17(1)(a) and (c).

39. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, in contravention of SCM Regulation 19(a).

40. The performance of contractors or providers was not monitored on a monthly basis, in contravention of section 116(2)(b) of the MFMA. Similar non-compliance was also reported in the prior year.

41. Some of the commodities designated for local content and production, were procured from suppliers who did not submit a declaration on local production and content in contravention of the 2017 Preferential Procurement Regulation 8(5). Similar non-compliance was also reported in the prior year.

## Other information

42. The 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 and the selected development priority presented in the annual performance report that have been specifically reported in this auditor's report.

43. 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 on it.

44. 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 priority presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

45. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, and 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

46. 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 basis for the qualified opinion and the findings on compliance with legislation included in this report.

47. Management did not implement adequate internal controls for proper and sufficient record keeping to ensure that all the reported financial information was fully supported.

48. Management did not implement adequate controls over monthly reconciliations of some expenditure transactions.

49. Management did not perform adequate reviews and monitoring to ensure accurate reporting of financial information and compliance with legislation.

50. Leadership did not exercise sufficient oversight responsibility regarding the financial reporting, compliance with legislation, and internal controls.

## Material irregularities

51. In accordance with the PAA and the Material Irregularity Regulations, I have a responsibility to report on material irregularities identified during the audit and on the status of the material irregularities reported in the previous year's auditor's report.

### Material irregularities identified during the audit

#### Interest not charged on arrear debtor accounts

52. The municipality did not charge interest on all its arrear accounts for the month of January 2020, as required by section 64(2)(g) of the MFMA. No subsequent billing of this interest has occurred to date and no exemption was granted by council not to charge this interest on arrear accounts. The non-compliance resulted in a likely financial loss to the uMzinyathi District Municipality.

53. The following actions have been taken to resolve the material irregularity:

54. To address the irregularity in current financial year and balances restated on the annual financial statement.

55. The error has been adequately corrected by charging interest to those accounts that were erroneously omitted, this was accounted for as the prior-period error as disclosed in note 39 of financial statements and resulted to the restatements of receivables and interest charges.

### Full and proper records not kept

56. Reasonable steps were not taken in the 2019-2020 financial year to ensure that full and proper records were kept of the financial affairs of the municipality in accordance with any prescribed norms and standards as required by section 62(1)(b) of the MFMA. The non-compliance contributed to a disclaimer of audit opinion as I could not obtain sufficient appropriate audit evidence to support the amounts and disclosures in the financial statements.

57. The lack of full and proper records of the financial affairs of the municipality is likely to result in substantial harm to the public sector institution as the municipality is likely to be unable to discharge its service delivery mandate if these matters are not urgently addressed:

58. The audit report included an overall limitation on property, plant and equipment due to supporting registers not agreeing up to the financial statements and various restatements made on this balance. The lack of records and maintenance directly impacts on the service delivery mandate of the district as it is responsible for all of the infrastructure in the district relating to the provision of water and sanitation services.

59. The audit report included a limitation on water distribution losses. This was due to a lack of proper record keeping to enable consistent measurement and reliable reporting. The lack of records directly impacts on the service delivery mandate of the district who as a water service authority is responsible for the provision of water and sanitation services in the district.

60. The audit report included an overall limitation on revenue from service charges as well as receivables and bad debts written off due to there being a lack of full and proper records maintained by the municipality. The lack of full and proper records directly impacts on the service delivery mandate of the district as this has an impact on the financial sustainability

61. Several other matters which further substantiate the view in point 6 above were also reported in the 2019-2020 audit report under the basis for disclaimer of opinion.

62. The following action have been taken to resolve the material irregularity:

63. Appointment of a service provider to assist with the Fixed asset register (FAR) and relevant Property plant and equipment (PPE) schedules, which will allow a transfer of skills and ensure that these documents are maintained annually.

64. To develop a policy that speaks to water losses and a process of monthly reconciliations and daily reporting on water and chemical inventory to be done and regularly monitoring and oversight is to be maintained.

65. Formalisation of the draft debt impairment policy and implementation.

66. Internal control safeguards, process flows and policies and procedures are to be established and actively monitored to ensure that the risk of re-occurrence of these material irregularities is limited.

67. Significant progress has been made in the implementation of record keeping controls, which already resulted in the prior-year limitations of scope audit findings being resolved and there were no significant limitation of scope identified during the current audit. The accounting officer shall continue putting effort on internal capacity building over record keeping and internal controls instead of over reliance on external service providers.

68. I will follow-up on the implementation of the actions being taken during my next audit.

## Other reports

69. I draw attention to the following engagements conducted by various parties which had, or could have, an impact on the matters reported in the municipality's financial statements, reported performance information, compliance with applicable legislation and other related matters. These reports did not form part of my opinion on the financial statements or my findings on the reported performance information or compliance with legislation.

70. An investigation was conducted by an independent consulting firm, on behalf of the Department of Cooperative Governance and Traditional Affairs. The investigation covered the period 1 July 2015 to 30 June 2017 and related to expenditure for boreholes and debt collection that was not supported by adequate documentary evidence. The final report was tabled to council in the prior year and the recommendations of the investigation are still being implemented.

71. An investigation covering the period 1 July 2014 to 30 June 2018 was conducted by an independent consulting firm on supply chain management irregularities relating to the construction of the disaster management centre. The final report on the outcome of the investigation was tabled to council in the prior year and the recommendations of the investigation are still being implemented.

Auditor-General

Pietermaritzburg

28 February 2022

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 priority 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 relating to events or conditions that may cast significant doubt on the ability of the Umzinyathi District Municipality 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 my 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 operating as a going concern
- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and determine 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 provide the accounting officer with a statement that I have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on my independence and, where applicable, actions taken to eliminate threats or safeguards applied.