

# Report of the auditor-general to the Provincial Legislature and the Council for the Merafong City Local Municipality

## Report on the audit of the financial statements

### Opinion

1. I have audited the financial statements of the Merafong City Local Municipality set out on pages xx... to xx..., which comprise the appropriation statement, the statement of financial position as at 30 June 2018, the statement of financial performance, statement of changes in net assets, and cash flow statement and the 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, the financial statements present fairly, in all material respects, the financial position of the Merafong City Local 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 the Division of Revenue Act, 2017 (Act No. 3 of 2017) (Dora).

### Basis for the 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 auditor's 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) and 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. As disclosed in note 45 in the financial statements, which indicates that the municipality incurred a net loss of R161 738 076 during the year ended 30 June 2018 and, as of that date the municipality's current liabilities exceeded its current assets by R357 316 675. As stated in note 45, these events or conditions, along with other matters as set forth in note 45, 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.

## Material impairments

9. As disclosed in note 12 to the financial statements, the consumer debtors balance has been significantly impaired. The allowance for impairment of consumer debtors amounts to R1 247 339 948 (2016-17: R940 805 836) which represents 87.6% (2016-17: 82.8%) of total consumer debtors. The contribution to the provision for debt impairment was R327 263 309 (2017-16: R263 761 962).

## Material losses

10. As disclosed in note 53 to the financial statements, material water losses amounting to R55 338 580 (2016-17: R42 485 098) were incurred, which represents 47.06% (2016-17: 43.32%) of the total water purchased. Technical losses amounted to R43 416 340 (2016-17: R33 332 034). Non-technical losses amounted to R11 922 240 (2016-17: R9 153 063) and are mainly due to deterioration of water reticulation system, burst pipes and unauthorised consumption.
11. As disclosed in note 53 to the financial statements, material electricity losses amounting to R73 812 581 (2016-17 R60 778 294) were incurred, which represent 33.86% (2017-16: 24.81%) of total electricity purchased. Technical losses amounted to R62 461 378 (2017-16: R51 431 557). Non-technical losses amounted to R11 351 203 (2017-16: R9 346 736) and are due to unauthorised consumption, tampering and faulty meters.

## Material uncertainties

12. With reference to note 39 to the financial statements, the municipality is the defendant in various lawsuits. The outcome of these matters cannot presently be determined, and/ or reliably measured, therefore no provision for any liabilities that may result was made in the financial statements.

## Other matter

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

## Unaudited disclosure notes

14. 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 we do not express an opinion thereon.

## Responsibilities of the accounting officer for the financial statements

15. 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.
16. In preparing the financial statements, the accounting officer is responsible for assessing the Merafong City Local 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**

17. 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 financial statements.
18. 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**

19. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected goal presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
20. 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.
21. 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 goal presented in the annual performance report of the municipality for the year ended 30 June 2018:

<b>Goal</b>	<b>Pages in the annual performance report</b>
Goal1: Basic service delivery	x – x

22. 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.

23. I did not raise any material findings on the usefulness and reliability of the reported performance information for the following goal:

- Goal1: Basic Service Delivery

### **Other matters**

24. I draw attention to the matters below.

#### Achievement of planned targets

25. Refer to the annual performance report on pages.... to ... for information on the achievement of planned targets for the year.

#### Adjustment of material misstatements

26. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of Goal 1: Basic service delivery. 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**

27. 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.

28. The material findings on compliance with specific matters in key legislations are as follows:

#### Expenditure management

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

30. Effective steps were not taken to prevent irregular expenditure amounting to R22 456 631 as disclosed in note 48 to the annual financial statements, as required by section 62(1)(d) of the MFMA. All of the irregular expenditure was caused by contravention of regulation 19(a), due to competitive bidding processes and regulation 36(1) on deviation process.

31. Effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R24 680 024, as disclosed in note 47 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. All of the disclosed fruitless and wasteful expenditure was caused by late payments to suppliers which incurred penalties and interest.

## Asset Management

32. Investment on VBS Mutual Bank was not made in accordance with the municipality investment policy as required by municipal investment regulation 3(3).
33. Funds were invested in VBS Mutual bank, in contravention of municipal investment regulation 6.

## Other information

34. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes the directors' report, the audit committee's report. The other information does not include the financial statements, the auditor's report and those selected goal presented in the annual performance report that have been specifically reported in this auditor's report.
35. 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.
36. 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 goal presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
37. If based on the work I have performed, I conclude that there is a material misstatement in this other information, I am required to report that fact. I have nothing to report in this regard.

## Internal control deficiencies

38. 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 annual performance report and the findings on compliance with legislation included in this report.
39. The accounting officer did not exercise adequate oversight responsibility regarding compliance with certain laws and regulations and performance reporting. Furthermore, action plans to address prior year audit findings were not in all instances adequately monitored which resulted in a number of repeat findings on non-compliance with certain laws and regulations.
40. Senior management did not adequately monitor controls in place to ensure that compliance with certain laws and regulations were adhered to.
41. Senior management did not prepare regular, accurate and complete performance reports that were supported and evidenced by reliable information.

## Other reports

42. I draw attention to the following engagements conducted by various parties that 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.

## Investigations

43. There are currently investigations in progress that are being conducted by the municipality and the Gauteng Department of Finance. These investigations were initiated based on non-compliance with the SCM regulations and the municipal investment regulations. These investigations were still in progress at the reporting date.

*Auditor - General*

Johannesburg

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 goal 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 authority’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 Merafong City Local Municipality 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 entities or business activities within the group to express an opinion on the consolidated financial statements. I am responsible for the direction, supervision and performance of the group 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.