

Report of the auditor-general to the Free State Legislature and the council on the Mangaung Metropolitan Municipality

Report on the financial statements

Introduction

1. I have audited the financial statements of the Mangaung Metropolitan Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2016, the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget and actual amounts 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 the South Africa Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2015 (Act No. 1 of 2015) (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 the 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 the 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 entity'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 entity'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. The municipality did not apply the principles of GRAP 17 *Property, plant and equipment*, in determining the values at which infrastructure assets were recognised and in assessing the remaining useful lives of assets. As a result, the cost price and accumulated depreciation of infrastructure assets as disclosed in note 13 to the financial statements were overstated by R83 615 716 (2015: R65 570 999) and R16 881 062 (2015: R39 657 109), respectively. Additionally, the accumulated surplus was overstated by R66 734 654 (2015: R25 913 890). Consequently, the disclosure of the prior period error as contained in note 57.41 to the financial statements was also misstated.
7. The municipality did not transfer the expenditure of all completed capital projects to the value of the appropriate class of property, plant and equipment. This resulted in the overstatement of assets under construction included in property, plant and equipment as disclosed in note 13 to the financial statements by R121 285 028. In addition, I was unable to obtain sufficient appropriate audit evidence to support assets under construction. This was due to adjustments processed by management for the transfer of completed projects to the relevant class of property, plant and equipment that could not be supported by audit evidence. I was unable to confirm the value of assets under construction by alternative means. Consequently, I was unable to determine whether further adjustments to assets under construction stated at R1 478 084 988 (2015: R1 063 373 918) in the financial statements were necessary.

Qualified opinion

8. In my opinion, except for the possible 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 Mangaung Metropolitan Municipality as at 30 June 2016 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 DoRA.

Emphasis of matters

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

Restatement of corresponding figures

10. As disclosed in note 57 to the financial statements, the corresponding figures for 30 June 2015 have been restated as a result of errors discovered during 2015-16 in the financial statements of the municipality at, and for the year ended, 30 June 2015.

Handwritten initials

Material losses

11. As disclosed in notes 6, 7 and 8 to the financial statements, material losses were incurred as a result of the write-off of consumer and other receivables of R249 534 738 (2015: R86 431 274).
12. As disclosed in note 64 to the financial statements, the municipality incurred material water distribution losses of R146 392 570 (2015: R173 394 547), mainly due to burst water pipes, leakages and unmetered sites.

Material impairments

13. As disclosed in notes 5, 6, 7 and 8 to the financial statements, management provided for the impairment of consumer and other receivables to the value of R2 315 444 976 (2015: R2 078 606 189).

Unauthorised expenditure

14. As disclosed in note 61 to the financial statements, the municipality incurred unauthorised expenditure of R654 710 007 (2015: R987 132 533) in 2015-16 due to expenditure that exceeded the limits provided for in the votes of the approved budget.

Material underspending of conditional grants

15. As disclosed in note 22 to the financial statements, the municipality has materially underspent on conditional grants by R106 083 319 (2015: R107 483 829). The underspending was mainly due to the grant conditions not being met at year end for the telecom and postal service grant, the neighbourhood development grant and the urban settlement development grant.

Additional matter

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

Unaudited disclosure notes

17. 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.

Unaudited supplementary information

18. The appropriation statement set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited this statement and, accordingly, I do not express an opinion on it.

Ma C

Service delivery

19. Included in the cost of buildings, as disclosed in note 13 to the financial statements, is capital expenditure amounting to R351 906 448 (2015: R351 906 448) that relates to the intermodal public transport facility. The construction of this facility has been finalised but the facility is not fully utilised. This is due to disagreements between the taxi industry and the council which the council has not been able to resolve.

Report on other legal and regulatory requirements

20. In accordance with the Public Audit Act, 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 of selected key performance areas 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 them.

Predetermined objectives

21. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information of the following selected key performance areas presented in the annual performance report of the municipality for the year ended 30 June 2016:
 - Key performance area: Spatial development and the built environment on pages x to x
 - Key performance area: Eradication of bucket system, VIP toilets in Mangaung, Botshabelo and Thaba Nchu, roads, ageing infrastructure, focus on the basics, building solar farm, power plant feasibility study, safety and security on pages x to x
 - Key performance area: Human settlements on pages x to x
 - Key performance area: Public transport on pages x to x
22. I evaluated the usefulness of the reported performance information to determine whether it was consistent with the planned key performance areas. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (FMPPi).
23. I 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 selected key performance areas are as follows:

Key performance area: Spatial development and the built environment

25. I did not raise any material findings on the usefulness and reliability of the reported performance information for this key performance area.

Key performance area: Eradication of bucket system, VIP toilets in Mangaung, Botshabelo and Thaba Nchu, roads, ageing infrastructure, focus on the basics, building solar farm, power plant feasibility study, safety and security

Reliability of reported performance information

26. The FMPPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure reliable reporting of actual achievements against planned objectives, indicators and targets. Adequate and reliable corroborating evidence could not be provided for the reported achievements against planned targets of important indicators.

Key performance area: Human settlements

Usefulness of reported performance information

27. The FMPPPI requires performance indicators to be well defined by having clear definitions so that data can be collected consistently and is easy to understand and use. A total of 33% of the indicators were not well defined.

Reliability of reported performance information

28. The FMPPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure reliable reporting of actual achievements against planned objectives, indicators and targets. The reported performance information was not reliable when compared to the evidence provided.

Key performance area: Public transport

29. I did not raise any material findings on the usefulness and reliability of the reported performance information for this key performance area.

Additional matters

30. I draw attention to the following matters:

Achievement of planned targets

31. Refer to the annual performance report on pages xx to xx for information on the achievement of the planned targets for the year. This information should be considered in

the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 26, 27 and 28 of this report.

Adjustment of material misstatements

32. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of eradication of bucket system, VIP toilets in Botshabelo, Mangaung and Thaba Nchu, a focus on the basics, building solar farming, power plant feasibility study, safety and security; human settlements and public transport. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information.

Compliance with legislation

33. 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:

Budget

34. The total unforeseen and unavoidable expenditure incurred exceeded R15 million, in contravention of municipal budget and reporting regulation 72.

Financial statements

35. 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 identified by the auditors in the submitted financial statements were not adequately corrected, resulting in the financial statements receiving a qualified audit opinion.

Procurement and contract management

36. I could not obtain sufficient appropriate audit evidence that the performance of certain contractors and providers had been monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
37. The contract performance and monitoring measures and methods on certain contracts were not sufficient to ensure effective contract management, in contravention of section 116(2)(c) of the MFMA.
38. Persons in the service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e) and the code of conduct for staff members issued in terms of the Municipal Systems Act, 2000 (Act No. 32 of 2000).

169

Human resource management and compensation

39. The senior managers directly accountable to the municipal manager did not sign performance agreements, as required by section 57(2)(a) of the Municipal Systems Act.

Expenditure management

40. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
41. Reasonable steps were not taken to prevent unauthorised expenditure, as required by section 62(1)(d) of the MFMA.
42. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA.

Asset management

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

Consequence management

44. Unauthorised expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) of the MFMA.
45. Allegations of financial misconduct laid against officials of the municipality were not investigated as required by section 171(4)(a) of the MFMA.

Internal control

46. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with legislation. 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

47. The leadership did not effectively monitor and enforce the corrective action plans to address weaknesses in the processes of financial and performance reporting identified in previous financial years. The leadership also did not ensure that effective performance management and monitoring processes were implemented, that employees were aligned to the objectives of the municipality, and that there was effective consequence management.
48. The position of city manager was vacant for more than six months during the year under review.

Handwritten signature

Financial and performance management

49. The municipality lacked formalised processes to manage performance reporting, including the safeguarding of information and, importantly, the effective monitoring and evaluation of reported performance information.
50. Weaknesses in the processes and controls pertaining to asset management were not addressed and the lack of regular monitoring and reconciliation of asset information resulted in the unreliability of the control records. Management did not implement the auditors' recommendations, included in their action plan, to address the weaknesses. These weaknesses gave rise to material misstatements in the annual financial statements.
51. Management did not implement consequence management based on the non-achievement of deadlines that were set in the action plan to address the matters reported in the previous financial year.

Governance

52. The municipality did not have an effective risk management function during the year as its risk committee did not function and did not give direction to the risk management department. Management did not respond sufficiently in this regard to the concerns raised by the audit committee which resulted in the breakdown of this critical function.

Ruditor - General

Bloemfontein

10 February 2017



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence