

**REPORT OF THE AUDITOR-GENERAL TO THE FREE STATE LEGISLATURE AND COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF THE KOPANONG LOCAL MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2008**

**REPORT ON THE FINANCIAL STATEMENTS**

**Introduction**

1. I was engaged to audit the accompanying financial statements of the Kopanong Local Municipality which comprise the balance sheet as at 30 June 2008, income statement and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes as set out on pages [xx] to [xx].

**Responsibility of the accounting officer for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the entity-specific basis of accounting, as set out in accounting policy note 1 and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2007 (Act No. 1 of 2007) (DoRA). This responsibility includes:
  - Designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
  - Selecting and applying appropriate accounting policies
  - Making accounting estimates that are reasonable in the circumstances.

**Responsibility of the Auditor-General**

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA) and section 126 of the MFMA, my responsibility is to express an opinion on these financial statements based on my audit in accordance with the International Standards on Auditing and *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008*. Because of the matters discussed in the Basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

**Basis of accounting**

4. The municipality's policy is to prepare financial statements on the entity-specific basis of accounting, as set out in accounting policy note 1.

**Basis for disclaimer of opinion**

**Fixed assets**

5. For reasons as detailed below I was unable to obtain sufficient appropriate audit evidence as to the existence, rights, completeness and valuation of fixed assets to the value of R3 486 634 as disclosed in the balance sheet and the related detailed disclosure in note 5 to the financial statements.
  - Neither the municipality nor its electricity service provider maintained a reliable record of assets that contained all relevant information and that allowed for the proper identification and verification of fixed assets.
  - No year-end fixed asset verification procedures were performed by the municipality in respect of electricity assets with a total disclosed cost price of R3 366 867 that were managed by the appointed electricity service provider.

- Due to significant weaknesses identified in the year-end fixed asset verification procedures performed by the municipality, I am unable to place any reliance on the results thereof.
- Sufficient and appropriate supporting documentation could not be obtained in respect of fixed asset acquisitions of R1 135 697.
- Motor vehicles with a cost price of R264 554 were not registered in the name of Kopanong Local Municipality.
- According to the municipality's accounting policy, fixed assets are stated either at historical cost or at valuation where assets had been acquired with a grant or donation, while they are in existence and fit for use, except in the case of bulk assets, which are written off at the end of their estimated life as determined by the treasurer. Contrary to the prescripts of the municipality's accounting policy, a significant number of fixed assets have not been disclosed at either cost price or valuation but are included in the asset records at a value of either R1 or zero value, as the actual costs or fair value of the assets had not been determined. The value of fixed assets is therefore misstated by an unquantifiable amount that would equate to the cost or fair value of these assets had it been determined.

Due to the extent of the weaknesses in the municipality's fixed asset records, the lack of sufficient appropriate supporting documentation and no reliance that could be placed on the internal verification of assets, I could also not perform reasonable alternative procedures to obtain all the documentation and explanations deemed necessary.

### **Receivables**

6. Due to the lack of sufficient appropriate audit evidence I was unable to perform all the procedures or obtain all the documentation and explanations deemed necessary to obtain adequate audit assurance as to the existence of receivables with a value of R238 189 included in receivables as disclosed on the balance sheet and in note 9 to the financial statements. Alternative procedures also did not provide me with adequate audit assurance as to the existence of the receivables.
7. I was unable to obtain sufficient appropriate audit evidence in respect of the existence and valuation of and the municipality's rights to a value-added tax (VAT) receivable originating from the electricity service provider amounting to R1 244 103 included in the disclosed receivables per the balance sheet and note 9 to the financial statements. Alternative procedures performed also did not provide me with the required audit assurance.
8. Due to insufficient appropriate audit evidence audit assurance as to the valuation and existence of the VAT debtor amounting to R4 870 979, as disclosed in note 10 to the financial statements, could not be obtained. Due to a lack of supporting documentation, no alternative procedures could be performed.

### **Inventory**

9. Due to significant weaknesses observed in the year-end inventory count processes, I am unable to confirm that the processes would have resulted in reliable inventory records that could be utilised to gain adequate audit assurance as to the existence, completeness and valuation of consumable stores amounting to R396 360 as disclosed on the balance sheet and in note 8 to the financial statements. In the absence of reliable year-end inventory records, there was also no reasonable alternative procedure which I could perform to gain adequate audit assurance in this regard.

## Long-term liabilities

10. I was unable to obtain loan agreements in respect of long-term liabilities with a value of R3 156 001 as disclosed on the balance sheet and in note 2 to the financial statements. Alternative procedures performed to obtain the agreements from external sources were also not successful. I was thus unable to obtain sufficient appropriate audit evidence as to the existence and valuation of and the municipality's obligation in respect of long-term liabilities and the occurrence, completeness and accuracy of capital charges of R710 040 as disclosed in note 23 to the financial statements.

## Provisions

11. The leave records of the municipality and its records of work attendance were not reliable for purposes of establishing the accuracy and completeness of leave to the credit of officials at year-end. The leave records were therefore not a reliable basis for calculating the provision for leave as included on the balance sheet and disclosed in note 11 to the financial statements. Therefore it was not possible to gain adequate audit assurance as to the valuation of the provision for leave amounting to R2 055 736. In the absence of reliable leave records it was also not possible to perform alternative procedures to accurately determine the value of the provision.

## Payables

12. I was unable to obtain sufficient appropriate audit evidence in respect of payments to the value of R1 573 549 allocated against conditional grants received. Consequently, I was unable to obtain adequate audit assurance as to the occurrence and accuracy of the related expenditure and revenue recognised in the income statement for the said amount and the valuation of the unspent portion of these grants to the value of R328 153 as disclosed on the balance sheet and in note 12 to the financial statements. Due to the lack of sufficient appropriate audit evidence there were also no reasonable alternative procedures that I could perform to gain adequate audit assurance in this regard.
13. Included in payables as disclosed on the balance sheet and in note 12 to the financial statements, was a control account to the value of R276 303 (2007: R140 108) that had been created to manage the contributions made by the public to the capital infrastructure expenses planned to facilitate the installation of new electricity connections. Due to a lack of sufficient appropriate audit evidence, I was unable to gain adequate audit assurance as to whether the services in respect of which these contributions were made had been rendered and thus whether the control account, or portion thereof, represents an obligation to or, alternatively, revenue for the municipality. Due to the lack of information I was also unable to perform reasonable alternative procedures to gain adequate audit assurance as to the classification of this payable.
14. I was unable to obtain sufficient appropriate audit evidence in respect of salary creditors to the value of R8 618 574, trade creditors to the value of R122 611 and other creditors to the value of R110 477. Consequently, I was not able to gain adequate audit assurance as to the existence and valuation of these payables and whether the payables represent obligations of the municipality. Due to the lack of information, I was also unable to perform reasonable alternative audit procedures to provide me with the required audit assurance.

## Expenditure

15. I was unable to obtain the lease agreements supporting rental expenditure to the value of R290 506 and, consequently, I could not obtain adequate audit assurance as to the accuracy and completeness of these expenses. In the absence of sufficient appropriate supporting documents, I was also unable to perform reasonable alternative audit procedures to obtain the required audit assurance.

16. I was unable to obtain sufficient appropriate audit evidence in respect of expenditure transactions to the value of R195 744 and, consequently, I could not obtain adequate audit assurance as to the occurrence, accuracy and classification of these expenses. In the absence of sufficient appropriate audit evidence, I was also unable to perform reasonable alternative audit procedures to provide me with the required audit assurance.

### Revenue

17. Adequate audit assurance as to the completeness and accuracy of assessment rates revenue amounting to R7 387 507 disclosed in note 14 to the financial statements could not be obtained due to the following:

- Interim valuations have not been performed and the valuation roll, on which assessment rates were to be based, had not been updated since 1 July 2004
- No reconciliation of or explanations for a difference of R508 427 between the actual income levied for assessment rates and a calculation of the assessment rates income based on the valuation roll could be provided.

Accordingly, I was not able to determine whether any adjustments might be necessary to the amounts disclosed in the financial statements for debtors, revenue, deficit for the year and accumulated deficit. In the absence of sufficient appropriate evidence, I was also not able to perform reasonable alternative procedures to gain the required audit assurance in this regard.

18. A complete list/register for rotating electricity meters registered in the Kopanong district could not be provided by the electricity service provider or by the municipality. I was thus unable to determine whether a debtor account existed and whether meter readings were taken in respect of all installed electricity meters. Consequently, I was unable to obtain sufficient appropriate audit evidence as to the completeness of revenue from this source that amounted to R6 059 288 for the year under review.

19. Valid contracts/agreements in support of the leasing of municipal properties could not be submitted. Rental registers with respect to properties were not complete, were not reviewed by senior officials and were not reconciled to rental income. I was thus unable to obtain sufficient appropriate audit evidence as to the occurrence, completeness and accuracy of rental income amounting to R965 596 included in actual income in the income statement. Due to the extent of the weaknesses and lack of information, no alternative procedures could be performed.

20. According to the municipality's financial records, an amount of R10 561 138 was received in respect of the sale of prepaid electricity. However, the total value for revenue from this source as per the service provider's records indicated that prepaid electricity sold amounted to R10 314 244. The difference of R246 894 could not be adequately explained or reconciled and I was thus unable to obtain sufficient appropriate audit evidence to provide me with adequate audit assurance as to the accuracy and completeness of revenue from prepaid electricity sales. Due to the lack of reconciliations and explanations for the difference, I was also unable to perform reasonable alternative procedures.

### Capital commitments

21. I was unable to obtain sufficient appropriate audit evidence to provide me with audit assurance as to the completeness and valuation of the capital commitments amounting to R22 831 519 (2007: R550 664) as disclosed in note 30 to the financial statements. Due to the lack of audit evidence I was also unable to perform reasonable alternative procedures to obtain adequate audit assurance on the disclosed value of commitments.

## Disclaimer of opinion

22. Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements of Kopanong Local Municipality. Accordingly, I do not express an opinion on the financial statements.

## Emphasis of matters

I draw attention to the following matters:

### Fruitless expenditure

23. As disclosed in note 31 to the financial statements, fruitless expenditure to the amount of R1 271 801 was incurred during the financial year.

### Irregular expenditure

24. As disclosed in note 32 to the financial statements, irregular expenditure to the amount of R2 784 974 was incurred during the financial year.

### Unauthorised expenditure

25. As disclosed in note 33 to the financial statements, unauthorised expenditure to the amount of R13 807 693 was incurred during the financial year.

## OTHER MATTERS

I draw attention to the following matters that relate to my responsibilities in the audit of the financial statements:

### Internal controls

26. Section 62(1)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes that gave rise to the inefficiencies in the system of internal control, which led to the disclaimer of opinion. The root causes are categorised according to the five components of an effective system of internal control. In some instances deficiencies exist in more than one internal control component.

Reporting item	Control environment	Risk assessment	Control activities	Information and communication	Monitoring
Fixed assets	X		X		
Receivables			X		
Inventory			X		
Long-term liabilities			X		
Provisions			X		
Payables			X		
Expenditure			X		
Revenue			X		
Capital commitments			X		

Control environment: establishes the foundation for the internal control system by providing fundamental discipline and structure for financial reporting.

Risk assessment: involves the identification and analysis by management of relevant financial reporting risks to achieve predetermined financial reporting objectives.

Control activities: policies, procedures and practices that ensure that management's financial reporting objectives are achieved and financial reporting risk mitigation strategies are carried out.

Information and communication: supports all other control components by communicating control responsibilities for financial reporting to employees and by providing financial reporting information in a form and time frame that allow people to carry out their financial reporting duties.

Monitoring: covers external oversight of internal controls over financial reporting by management or other parties outside the process; or the application of independent methodologies, like customised procedures or standard checklists, by employees within a process.

## **Non-compliance with applicable legislation**

### **Municipal Finance Management Act, 2003 (Act No. 56 of 2003)**

27. Section 69(3)(a) of the MFMA prescribes that the accounting officer must no later than 14 days after approval of an annual budget submit to the mayor a draft service delivery and budget implementation plan for the budget year. Section 53(1)(c)(ii) of the MFMA prescribes that the mayor of a municipality must take all reasonable steps to ensure that the municipality's service delivery and budget implementation plan is approved by the mayor within 28 days after the approval of the budget. No evidence could be obtained that a draft service delivery and budget implementation plan for the 2008-09 budget year had been prepared and submitted as required.
28. In terms of section 65(2)(e) of the MFMA the accounting officer of a municipality must ensure that all money owing by the municipality is paid within 30 days of receiving the relevant invoice or statement, unless prescribed otherwise for certain categories of expenditure. In respect of payments with a total value of R2 097 252, I was unable to obtain sufficient appropriate audit evidence that the payment was made within the prescribed period.

### **Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA)**

29. Section 66 of the MSA prescribes that a municipal manager, within a policy framework determined by the municipal council and subject to any applicable legislation, must among others attach to all the posts on its approved staff establishment the remuneration and other conditions of service as may be determined in accordance with any applicable labour legislation and should establish a process or mechanism to regularly evaluate the staff establishment and, if necessary, review the staff establishment and the remuneration and conditions of service. I could not obtain sufficient appropriate audit evidence that municipal manager complied with these prescripts of the MSA.

## **Matters of governance**

30. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of certain key governance responsibilities, which I have assessed as follows:

<b>Matter of governance</b>	<b>Yes</b>	<b>No</b>
<b>Audit committee</b>		
<ul style="list-style-type: none"> <li>The municipality had an audit committee in operation throughout the financial year.</li> </ul>	X	
<ul style="list-style-type: none"> <li>The audit committee operates in accordance with approved, written terms of reference.</li> </ul>		X
<ul style="list-style-type: none"> <li>The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA.</li> </ul>		X
<b>Internal audit</b>		
<ul style="list-style-type: none"> <li>The municipality had an internal audit function in operation throughout the financial year.</li> </ul>	X	
<ul style="list-style-type: none"> <li>The internal audit function operates in terms of an approved internal audit plan.</li> </ul>		X
<ul style="list-style-type: none"> <li>The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA.</li> </ul>		X
<b>Other matters of governance</b>		
<ul style="list-style-type: none"> <li>The annual financial statements were submitted for audit as per the legislated deadlines section 126 of the MFMA for municipalities.</li> </ul>	X	
<ul style="list-style-type: none"> <li>The annual report was submitted to the auditor for consideration prior to the date of the auditor's report.</li> </ul>	X	
<ul style="list-style-type: none"> <li>The financial statements submitted for audit were not subject to any material amendments resulting from the audit.</li> </ul>		X
<ul style="list-style-type: none"> <li>No significant difficulties were experienced during the audit concerning delays or the unavailability of expected information and/or the unavailability of senior management.</li> </ul>		X
<ul style="list-style-type: none"> <li>The prior year's external audit recommendations have been substantially implemented.</li> </ul>		X
<ul style="list-style-type: none"> <li>Provincial SCOPA resolutions have been substantially implemented.</li> </ul>		X
<b>Implementation of Standards of Generally Recognised Accounting Practice (GRAP)</b>		
<ul style="list-style-type: none"> <li>The municipality submitted an implementation plan, detailing progress towards full compliance with GRAP, to the National Treasury and the relevant provincial treasury before 30 October 2007.</li> </ul>	X	
<ul style="list-style-type: none"> <li>The municipality substantially complied with the implementation plan it submitted to the National Treasury and the relevant provincial treasury before 30 October 2007, detailing its progress towards full compliance with GRAP.</li> </ul>	X	
<ul style="list-style-type: none"> <li>The municipality submitted an implementation plan, detailing further progress towards full compliance with GRAP, to the National Treasury and the relevant provincial treasury before 31 March 2008.</li> </ul>	X	

#### Unaudited supplementary schedules

31. The supplementary information set out on pages 24 to 31 of the financial statements do 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.

## **OTHER REPORTING RESPONSIBILITIES**

### **REPORT ON PERFORMANCE INFORMATION**

32. I have reviewed the performance information as set out on pages xx to xx.

#### **Responsibility of the accounting officer for the performance information**

33. In terms of section 121(3)© of the MFMA, the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the MSA.

#### **Responsibility of the Auditor-General**

34. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008* and section 45 of the MSA.

35. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.

36. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

#### **Non-compliance with regulatory requirements**

##### **No quarterly reporting on performance information**

37. No quarterly reports on progress made in achieving measurable objectives and targets were prepared as a whole for Kopanong Local Municipality to facilitate effective performance monitoring, evaluation and corrective action as required by section 166 of the MFMA.

##### **Existence and functioning of a performance audit committee**

38. The municipality did not appoint and budget for a performance audit committee, nor was any other audit committee utilised as the performance audit committee, as required by regulation 14(2)(a) of the *Local Government Municipal Planning and Performance Management Regulations, 2001*.

##### **Internal auditing of performance measurements**

39. The municipality did not develop and implement mechanisms, systems and processes for auditing the results of performance measurement as part of its internal auditing processes, as required in terms of section 45 of the MSA and section 165(2)(b)(v) of the MFMA.

##### **Mid-year performance assessment not performed**

40. A report by the accounting officer on mid-year budget and performance assessments, as required by section 72 of the MFMA, could not be submitted.

##### **General key performance indicators not included in the Integrated Development Plan (IDP)**

41. The key performance indicators set by the Kopanong municipality did not include all general key performance indicators applicable to the municipality, as prescribed in terms of section 43(1) of the MSA.



### Lack of sufficient appropriate audit evidence

42. I was unable to obtain sufficient appropriate audit evidence in relation to the performance information of the Kopanong Local Municipality, as I was unable to obtain access to the following records pertaining to key performance indicators listed below:
- (a) The percentage of households with access to basic level of water
  - (b) The percentage of households with access to basic level of sanitation.

### Input, output, outcome indicators and targets

43. Input, output, outcome indicators and targets were not set for development priorities and objectives in the IDP, as prescribed in terms of section 41 of the MSA.

### No financial plan was developed for the 2007-08 financial year

44. A financial plan was not compiled for the municipality, as required in terms of section 26(h) of the MSA.

### Lack of reporting on all predetermined objectives in annual report

45. I draw attention to the fact that the Kopanong Local Municipality has not reported on all the predetermined objectives, as required by section 25 of the MSA.
- The following development priorities and objectives included in the IDP were not included in the annual performance report:

Development priority	Objective
Environment	To ensure that landfill sites are managed and operated according to the relevant permit conditions and in accordance with the district integrated waste management plan. To register landfill sites with the Department of Environmental Affairs and Tourism and Department of Water Affairs and Forestry. To identify and develop appropriate land for the provision of landfill sites.
Disasters	To improve the municipality's preparedness to respond appropriately to disasters.

- Furthermore, it was found that the following objectives that were included in the IDP were not included in the annual performance report:

Development priority	Objective
Water and sanitation (sewerage)	To eradicate all bucket toilet facilities by December 2007.
	To improve the supply of bulk water.
Poverty and unemployment	To promote local tourism.
	To facilitate, encourage and support public and private initiatives to promote agricultural extension programmes, including processing of agricultural produce.
Health	To ensure that towns are maintained to an acceptable level of cleanliness.
Housing	To produce 8 000 serviced sites by 2012 to meet housing needs.
Streets and storm water management	To improve and extend all access roads.

Cemeteries	To increase available cemetery space in all towns.
Sports and recreation facilities	To promote the provision of public libraries in Springfontein, Philippolis, Gariep Dam and Trompsburg.
Communication	To improve the municipality's external and internal communication.
Safety and security	To improve area and street lighting in all towns.

**APPRECIATION**

46. The assistance rendered by the staff of the Kopanong Local Municipality during the audit is sincerely appreciated.

*Auditor-General*

Bloemfontein  
28 November 2008



A U D I T O R - G E N E R A L