

Report of the auditor-general to the Free State Legislature and the council on the Tokologo Local Municipality

Report on the audit of the financial statements

Disclaimer of opinion

1. I was engaged to audit the financial statements of Tokologo Local municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2017, statement of financial performance, statement of changes in net assets and cash flow statement and statement of comparison of budget with actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. I do not express an opinion on the financial statements of the municipality. Because of the significance of the matters described in the basis for disclaimer of opinion section of my report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

Basis for disclaimer of opinion

Property, plant and equipment

3. I was unable to obtain sufficient appropriate audit evidence for infrastructure assets and work in progress included in property, plant and equipment due to non-submission of the municipality's invoices and completion certificates that support the values of the assets. I was unable to confirm property, plant and equipment by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the property, plant and equipment stated at R642 214 729 (2016: R580 286 047) as disclosed in note 11 to the financial statements. In addition, the municipality could not reconcile the work in progress register with the financial statements furthermore completed projects could not be reconciled with the infrastructure asset register as required by SA Standards of GRAP, GRAP 17, *property, plant and equipment*, resulting in property, plant and equipment being understated by R46 006 200 (2016: R51 010 937).

Service charges

4. I was unable to obtain sufficient appropriate audit evidence that revenue service charges had been properly accounted for, due to the status of the accounting records. The municipality did not have adequate systems of internal control for the recording of all transactions and to support tariffs used to bill some of its consumers. I was unable to confirm revenue service charges by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to revenue service charges stated at R38 339 641 (2016: R20 268 481) in note 20 to the financial statements.

Consumer receivables from exchange transactions

5. I was unable to obtain sufficient appropriate audit evidence that other receivables included in consumer receivables from exchange transactions had been properly accounted for, due to lack of supporting documentation for the suspense accounts that were not cleared as at year-end. I was unable to confirm consumer receivables from exchange transactions by alternative means. Consequently, I was unable to determine whether any further adjustment was necessary to consumer receivables from exchange transactions stated at R12 177 819 in note 4 to the financial statements.

Payables from exchange transactions

6. The municipality did not have adequate systems in place to ensure that payables from exchange transactions as stated in note 17 to the financial statements have been correctly accounted for in terms of SA Standards of GRAP 104, *Financial Instruments*. This resulted in payables from exchange being overstated by R10 548 0480. Additionally, there was a resultant impact on the surplus for the year and on the accumulated surplus

Cash flow statement

7. The municipality did not present the cash flow statement in accordance with SA Standards of GRAP, GRAP 2, *Cash flow statements*. The cash flows from operating activities relating to the prior year figures were misstated as the impact of restatements made to the statement of financial position were not correctly included in the cash flow calculations, resulting in the corresponding figures of the cash flow statement being misstated by R15 886 098.

Statement of changes in net assets

8. The entity did not disclose the statement of changes in net assets in accordance with SA Standards of GRAP, GRAP 1, *Preparation of Financial Statements*. The municipality did not reconcile the prior year closing accumulated surplus to the current year opening balance after adjusting for prior period errors, there is an unreconciled difference of R7 979 644 on the statement of changes in net assets which has resulted in the opening accumulated surplus balance being understated.

Total expenditure

9. Total expenditure was materially misstated by R9 247 757 due to the cumulative effect of individually immaterial uncorrected misstatements in the following items:
 - Bulk purchases stated at R18 921 177 was overstated by R3 808 363
 - Repairs and maintenance stated at R3 355 547 was overstated by R2 305 594
 - Employee related costs stated at R36 907 066 was overstated by R2 839 524
 - General Expenditure stated at R13 888 362 was understated by R194 039
 - Remuneration of Councillors stated at R12 459 907 was understated by R170 508

- Depreciation stated at R3 429 975 was understated by R192 110
- Contracted Services stated at R36 907 066 was overstated by R150 405

In addition, I was unable to obtain sufficient appropriate audit evidence and to confirm the total expenditure by alternative means:

- Finance cost for which evidence could not be obtained of R700 528 as included in the disclosed balance of R3 429 975

Material uncertainty related to going concern

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

11. Note 47 to the financial statements, indicates that as of 30 June 2017, the municipality's current liabilities exceeded its current assets by R60 704 415. These conditions, along with other matters as set forth in note 47, indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern and to meet its service delivery objectives.

Emphasis of matters

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

Restatement of corresponding figures

13. As disclosed note 45 to the financial statements, the corresponding figures for 30 June 2016 have been restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2017.

Material impairments

14. As disclosed in note 4 to the financial statements, Consumer receivables from exchange transactions were impaired by R112 674 791 (2016: R81 361 418).

Material losses

15. As disclosed in note 52 to the financial statements, material electricity losses which represents 72% (2016:44%) of total electricity purchased were incurred, mainly due to administrative and technical errors, negligence, theft of electricity, tampering with meters and connections which form part of illegal consumption and faulty meter

Irregular expenditure

16. As disclosed in note 51 to the financial statements, the municipality incurred irregular expenditure of R57 441 308 (2016: R44 521 442) mainly due to non-compliance with supply chain management (SCM) requirements.

Other matters

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

Unaudited disclosure note

18. 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.

Unaudited supplementary information

19. 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.

Responsibilities of the party responsible for the financial statements

20. The accounting officer is responsible for the preparation and fair presentation of the state financial statements in accordance with the statement of generally accepted accounting practice and the requirements of the municipal finance management act 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.
21. In preparing the financial statements, the accounting officer is responsible for assessing the Tokologo 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 intention is to liquidate the municipality or to cease operations, or there is no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

22. 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.
23. A further description of my responsibilities for the audit of the financial statements is included in the annexure to the auditor's report.

Introduction and scope

24. 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 key performance areas (KPAs) presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
25. 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.
26. 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 KPAs presented in the annual performance report of the municipality for the year ended 30 June 2017:

Development priorities	Pages in the annual performance report
KPA 1: Basic municipal service and infrastructure development	x – x

27. I performed procedures to determine whether the reported performance information 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.
28. The material findings in respect of the usefulness and reliability of the selected development priorities are as follows:

KPA 1 – Basic municipal service and infrastructure development

Performance of service providers monitored (Number of performance evaluation reports on service providers' performance)

29. The source information and evidence for the achievement of the planned indicator were not clearly defined, as required by the Framework for Managing Programme Performance Information (FMPPI).

Various indicators

30. The source information, evidence and method of calculation for the achievement of the planned indicators listed below, were not clearly defined, as required by the FMPPI. In

addition, the targets as determined during planning for these indicators were not specific in clearly identifying the nature and required level of performance and measurable, as required by the FMPPI.

Indicator description	Reported performance
Households with access to a minimum standard of water provision (Percentage of households with access to water services)	Achieved
Households with minimum standard of sanitation services (Develop business plan to address sanitation backlog)	Achieved
Households with access to a minimum standard of refuse removal services (Number of households with access to refuse removal services)	Achieved

31. The source information, evidence and method of calculation for the achievement of the planned indicators listed below were not clearly defined, as required by the FMPPI. In addition the targets as determined during planning for these indicators were not specific in clearly identifying the nature and required level of performance, as required by the FMPPI.

Indicator description	Reported performance
Drain and sewer blockages (Number of drain and sewer blockages attended to)	Achieved
Continuous monitoring of projects (Number of monthly projects)	Achieved

32. The source information and evidence for the achievement of the planned indicators listed below were not clearly defined, as required by the FMPPI:

Indicator description	Reported performance
Improvement in blue drop status of the municipality (Number of samples sent to the laboratory)	Achieved
Improvement in green drop status of the Municipality (Number of samples sent to the laboratory)	Achieved
Improvement in quality of drinking water (Number of water samples tested)	Achieved
Repairs and maintenance to network (Number of monthly burst pipes or leakages reports produced and submitted)	Achieved

33. I was unable to obtain sufficient appropriate evidence for the reported achievement of the indicators listed below. This was 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:

Indicator description	Reported achievement
Households with access to a minimum standard of water provision	Achieved
Refurbishment of reservoir and reduction of water losses	Achieved
Improvement in blue drop status of the municipality	Achieved
Improvement in green drop status of the municipality	Achieved
Improvement in quality of drinking water	Achieved
Campaigns held on conservation of water	Not achieved
Repairs and maintenance to network	Achieved
Water service authority workshops held	Not achieved
To improve quality of service rendered on electricity	Achieved
Compliance to grant funds and implementation of bylaws	Achieved
Repairs on street lightning and dysfunctional meter boxes	Achieved
Households with minimum standard of sanitation services	Achieved
Drain and sewer blockages	Achieved
Monitor spillage on underground water	Not achieved
Households with access to a minimum standard of refuse removal services	Achieved
Maintenance of landfill sites Dealesville	Achieved
Maintenance of landfill sites Boshof	Achieved
Repaired potholes in Boshof and Hertzogville	Achieved
Improved road safety	Achieved
Effective management of graveyards in Tokologo	Achieved
Graveyards maintained	Achieved
Develop programmes for sports	Not achieved
Upgrading of parks and recreational facilities	Achieved
Capital budget and grant funding on programmes and projects	Achieved
Performance of service providers monitored	Achieved
Continuous monitoring of projects	Achieved
MIG report compiled quarterly and submitted	Achieved
EPWP report compiled and submitted monthly	Achieved
Review WSDP document	Achieved
Disasters victim supported	Achieved
Disaster management and response workshops held	Achieved

34. The strategic objectives listed below were not reported while the planned strategic objectives were approved in the service delivery budget implementation plan. This is not in line with the requirements of section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000).

Planned strategic objectives per annual planning document
Ensure that all residents have access to electricity
Effective management of graveyards
Compliance with legislative framework and MFMA
To ensure disaster preparedness for extreme climate event

Other matter

35. I draw attention to the matter below.

Achievement of planned targets

36. 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 underachievement 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 x, x and x of this report

Report on audit of compliance with legislation

Introduction and scope

37. 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.

38. The material findings in respect of the compliance criteria for the applicable subject matters are as follows;

Strategic planning and performance management

39. Amendments to the IDP were made without consultation with the district municipality as required by municipal planning and performance management regulations 34(b) and 3(6)(a).

40. The IDP did not include the key performance indicators and targets as required by sections 26(i) of the MSA and municipal planning and performance management regulations 2(1)(e).

Budgets

41. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R84 117 137, as disclosed in note 49 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA.

Annual financial statements, performance and annual reports

42. 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, which resulted in the financial statements receiving a disclaimer of audit opinion.

Procurement and contract management

43. Sufficient appropriate audit evidence could not be obtained that some contracts were awarded in accordance with the legislative requirements, as there were no proper record keeping of tender.
44. 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 SCM regulation 17(a) and (c).
45. Some of the quotations were accepted from prospective providers who were not on the list of accredited prospective providers and did not meet the listing requirements prescribed by the SCM policy, in contravention of SCM regulations 16(b) and 17(b).
46. Some of the 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.
47. Sufficient appropriate audit evidence could not be obtained that goods and services of a transaction value above R500 000 were procured by inviting competitive bids and that deviations were approved by the accounting officer only if it was impractical to invite competitive bids, as required by SCM regulations 19(a) and 36(1).
48. Some of the competitive bids were not always evaluated by bid evaluation committees which were composed of officials from the departments requiring the goods or services and at least one SCM practitioner of the municipality, as required by SCM regulation 28(2).
49. Some of the contracts were awarded to bidders based on preference points that were not allocated in accordance with the requirements of the Preferential Procurement Policy Framework Act and its regulations.
50. Some of the construction contracts were awarded to a contractor that was suspended with the CIDB and did not qualify for the contract in accordance with section 18(1) of the CIDB Act and CIDB regulations 17 and 25(7A)
51. 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 as required by preferential procurement regulation 9(1).

Human resource management

52. Appointments were made in posts which were not provided for in the approved staff establishment, as required by section 66(3) of the MSA.

Expenditure management

53. Effective steps were not taken to prevent irregular expenditure amounting to R57 441 308 as disclosed in note 51 to the annual financial statements, as required by section

62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by non-compliance in the competitive bidding process. Irregular expenditure amounting to R18 245 909 was incurred on construction of a 10 kilometre ductile iron pipeline project.

- 54. Effective steps were not taken to prevent fruitless and wasteful expenditure amounting to R2 669 833, as disclosed in note 50 to the annual financial statements,
- 55. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred, accounted for creditors and accounted for payments made, as required by section 65(2)(b) of the MFMA.
- 56. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.

Revenue management

- 57. An adequate management, accounting and information system which accounts for revenue and debtors were not in place, as required by section 64(2)(e) of the MFMA.
- 58. An effective system of internal control for revenue was not in place, as required by section 64(2)(f) of the MFMA.
- 59. The council failed to adopt an oversight report containing the council's comments on the annual report within the prescribed timelines, as required by section 129(1) of the MFMA.

Asset management

- 60. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA
- 61. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Liability management

- 62. An adequate management, accounting and information system which accounts for liabilities was not in place, as required by section 63(2)(a) of the MFMA.
- 63. An effective system of internal control for liabilities (including a creditors listing) was not in place, as required by section 63(2)(c) of the MFMA.

Consequence management

- 64. 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.
- 65. Irregular expenditure incurred by the municipality were not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA
- 66. Fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.

Other information

67. 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 thereon and those selected development priorities presented in the annual performance report that have been specifically reported on in the auditor's report.
68. 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.
69. 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 KPAs presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
70. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, 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

71. 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. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for disclaimer of opinion, the findings on the annual performance report performance report and the findings on compliance with legislation included in this report.
72. Leadership did not always take prompt and adequate action to address weaknesses in internal control which resulted in non-compliance with applicable legislation and gave rise to unauthorised, irregular expenditure and fruitless and wasteful expenditure. Management did not always properly analyse the control weaknesses and implement appropriate follow-up actions that adequately addressed the root cause timeously.
73. Leadership did not fill in critical vacancies within the prescribed period to ensure that management establishes a system of internal control and communicate adequate policies and procedures that support the understanding and execution of internal control objectives.
74. Effective performance systems processes and procedures, and the management thereof, had not been adequately developed and implemented as a result information not being available for audit and delayed responses to requests for information.
75. The audit committee did not ensure that there was the required impact in addressing the control weaknesses by promptly monitoring the action plan to ensure that internal control deficiencies are addressed to prevent repeat findings on compliance and reported

performance information. Furthermore, the risk assessment process did not prevent the potential risks around asset management and revenue management, which resulted in the modified audit opinion.

Other reports

76. 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.
77. Due to the hacking of the IT environment and the municipality struggling to draw reports from the system for the audit. An ICT audit to evaluate the IT security network of the municipality to identify areas where there are weaknesses and provide measures in which these can be resolved to avoid such issues from re-occurring. The IT audit was performed on the 14th of November 2017 to assess the environment as at that time, the report on the matter was then provided to management.

Auditor General

Bloemfontein

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 development priorities 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 concerns 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 Tokologo Local 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.

- 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.
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 here applicable, related safeguards.