

Report of the auditor-general to the Eastern Cape Provincial Legislature and the council of Amahlathi Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Amahlathi Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2023, 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 notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the effects of the matters described in the basis for qualified opinion section of my report, the financial statements present fairly, in all material respects, the financial position of the Amahlathi Local Municipality as at 30 June 2023 and its financial performance and cash flows for the year then ended in accordance with the Standards of Generally Recognised Accounting Practice (GRAP) and the requirements of the Municipal Finance Management Act 56 of 2003 (MFMA) and the Division of Revenue Act 05 of 2022 (DORA).

Basis for qualified opinion

Property, plant and equipment

3. The municipality did not depreciate property, plant and equipment in accordance with GRAP 17, *Property, plant and equipment*. Useful lives that were inconsistent with the municipality's accounting policy were applied and in some instances, prior year revisions of useful lives were not considered in the current year depreciation calculation. Consequently, property, plant and equipment disclosed in note 10 to the financial statements and statement of financial position was overstated by R4.3 million and depreciation understated by R4.3 million, respectively. Additionally, there was an impact on the surplus for the period and on the accumulated surplus.

General expenses

4. The municipality did not record invoices in the accounting system when the transactions occurred in accordance with GRAP 1, *Presentation of financial statements*. As a result, general expenses were also recorded in the incorrect financial period. Consequently, general expenses disclosed in note 33 to the financial statements and statement of financial performance were overstated by R6.5 million, and trade payables understated by R6.5 million, respectively. Additionally, there was an impact on the surplus for the period and on the accumulated surplus.

Context for opinion

5. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the responsibilities of the auditor-general for the audit of the financial statements section of my report.
6. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *International code of ethics for professional accountants (including International Independence Standards)* (IESBA code) as well as other ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
7. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Material uncertainty relating to going concern

8. I draw attention to the matter below. My opinion is not modified in respect of this matter.
9. I draw attention to note 43 to the financial statements, which indicates that the municipality's inability to pay creditors within due dates, negative key financial ratios and net current liability was realised. As stated in note 43, these events or conditions, along with other matters as set forth in note 43, 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

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

Restatement of corresponding figures

11. As disclosed in note 41 to the financial statements, the corresponding figures for 30 June 2022 were restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2023.

Material impairments of consumer debtors and receivables from non-exchange transactions

12. As disclosed in notes 4 and 5 to the financial statements, cumulative debt impairments of R73.7 million (2021-22: R57.1 million) and R25.8 million (2021-22: R31.1 million) were made to consumer debtors and receivables from non-exchange transactions respectively.

Material electrical distribution losses

13. As disclosed in note 48 to the financial statements, material electrical distribution losses of R18.2 million (2021-2022: R15.3 million) was incurred, which represents 42.1% (2021-2022: 34.5%) of total electricity purchased. The losses are attributed to normal losses and illegal connections.

Contingent liabilities

14. As disclosed in note 38 to the financial statements, the municipality is the defendant in several lawsuits. The municipality is opposing the claims, and the ultimate outcome of the matters could not be determined.

Other matter

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

Unaudited disclosure notes

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

Responsibilities of the accounting officer for the financial statements

17. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the 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 the financial statements that are free from material misstatement, whether due to fraud or error.
18. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the municipality or to cease operations or has no realistic alternative but to do so.

Responsibilities of the auditor-general for the audit of the financial statements

19. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
20. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.

Report on the audit of the annual performance report

21. In accordance with the Public Audit Act 25 of 2004 (PAA) and the general notice issued in terms thereof, I must audit and report on the usefulness and reliability of the reported performance against predetermined objectives for the selected development priority presented in the annual performance report. The accounting officer is responsible for the preparation of the annual performance report.
22. I selected the following development priority presented in the annual performance report for the year ended 30 June 2023 for auditing. I selected a development priority that measures the municipality's performance on its primary mandated functions and that is of significant national, community or public interest.

Development priority	Page numbers	Purpose
Service delivery and infrastructure development	XX	Provide basic services to all citizens wherever they reside

23. I evaluated the reported performance information for the selected development priority against the criteria developed from the performance management and reporting framework, as defined in the general notice. When an annual performance report is prepared using these criteria, it provides useful and reliable information and insights to users on the municipality's planning and delivery on its mandate and objectives.
24. I performed procedures to test whether:
- the indicators used for planning and reporting on performance can be linked directly to the municipality's mandate and the achievement of its planned objectives
 - the indicators are well defined to ensure that they are easy to understand and can be applied consistently, as well as verifiable so that I can confirm the methods and processes to be used for measuring achievements
 - the targets can be linked directly to the achievement of the indicators and are specific, time bound and measurable to ensure that it is easy to understand what should be delivered and by when, the required level of performance as well as how performance will be evaluated
 - the indicators and targets reported on in the annual performance report are the same as those committed to in the approved initial or revised planning documents
 - the reported performance information is presented in the annual performance report in the prescribed manner
 - there is adequate supporting evidence for the achievements reported and for measures taken to improve performance.
25. I performed the procedures for the purpose of reporting material findings only and not to express an assurance opinion or conclusion.

26. The material findings on the reported performance information for the development priority are as follows.

Service delivery and infrastructure development

KPI 26: % of inspected damaged road markings and signs maintained

27. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of the percentage of inspected damaged road markings and signs maintained, as the indicator was not based on the planned performance and reporting management processes and systems. This was due to lack of established processes in properly defining the units of measure and means of verification of reported information. Consequently, the reported achievement (100% of road markings and signs maintained per inspection report) reported against the target of (100% of road markings and signs maintained per inspection report) might be less than reported.

Various indicators

28. I was unable to obtain sufficient appropriate audit evidence that systems and processes were established to enable measurement and reliable reporting of performance against indicator definitions. This has resulted in the municipality not properly defining the units of measure and means of verification of reported information. Consequently, the reported achievement might be more or less than reported and was not reliable for determining if the target had been achieved.

Indicator number	Indicator description	Target	Reported achievement
KPI 9	% progress towards roads constructed at Border Post (gravelled)	100%	94%
KPI 10	% progress towards paving of Cathcart Road by June 2023 (KPI NO. 10)	100%	85%
KPI 14	% progress towards construction of Stutterheim Recreation Centre	15%	15%
KPI 15	% progress towards construction of Keiskammahoek Recreation Centre	15%	15%

Other matters

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

Achievement of planned targets

30. The annual performance report includes information on reported achievements against planned targets and provides measures taken to improve performance. This information should be considered in the context of the material findings on the reported performance information.

Material misstatements

31. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information for service

delivery and infrastructure development. Management did not correct all the misstatements and I reported material findings in this regard.

Report on compliance with legislation

32. In accordance with the PAA and the general notice issued in terms thereof, I must audit and report on compliance with applicable legislation relating to financial matters, financial management and other related matters. The accounting officer is responsible for the municipality's compliance with legislation.
33. I performed procedures to test compliance with selected requirements in key legislation in accordance with the findings engagement methodology of the Auditor-General of South Africa (AGSA). This engagement is not an assurance engagement. Accordingly, I do not express an assurance opinion or conclusion.
34. Through an established AGSA process, I selected requirements in key legislation for compliance testing that are relevant to the financial and performance management of the municipality, clear to allow consistent measurement and evaluation, while also sufficiently detailed and readily available to report in an understandable manner. The selected legislative requirements are included in the annexure to this auditor's report.
35. The material findings on compliance with the selected legislative requirements, presented per compliance theme, are as follows:

Annual financial statements, annual performance report and annual report

36. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of current assets, current liabilities and disclosures identified by the auditors in the submitted financial statements were subsequently corrected and supporting records were provided subsequently, but the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.

Strategic planning and performance

37. The performance management system and related controls were inadequate as it did not describe how the performance planning, monitoring, measurement, review and reporting should be conducted, organised and/or managed as required by municipal planning and performance management regulation 7(1).

Asset management

38. 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.

Expenditure management

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

40. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred, as required by section 65(2)(b) of the MFMA.
41. Reasonable steps were not taken to prevent irregular expenditure amounting to R16.7 million as disclosed in note 47 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by standardisation of salaries.
42. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R10.3 million, as disclosed in note 46 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA.
43. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R36.2 million, as disclosed in note 45 to the annual financial statements, in contravention of section 62(1)(d) 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.

Other information in the annual report

45. The accounting officer is responsible for the other information included in the annual report, which includes the audit committee's report. The other information referred to does not include the financial statements, the auditor's report and those selected development priority presented in the annual performance report that have been specifically reported on in this auditor's report.
46. My opinion on the financial statements, the report on the audit of the annual performance report and the report on compliance with legislation do not cover the other information included in the annual report and I do not express an audit opinion or any form of assurance conclusion on it.
47. My responsibility is to read this other information and, in doing so, consider whether it is materially inconsistent with the financial statements and the selected development priority presented in the annual performance report or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
48. If, based on the work I have performed on the other information that I obtained prior to the date of this auditor's report, I conclude that there is a material misstatement of this other information, I am required to report that fact. I have nothing to report in this regard.

Internal control deficiencies

49. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with applicable legislation however, my objective was not to express any form of assurance on it.

50. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified opinion and the material findings on the annual performance report and the material findings on compliance with legislation included in this report.
51. The accounting officer did not consistently implement and monitor the required daily and monthly financial disciplines to ensure that transactions were appropriately recorded and reported, as required by the financial accounting framework. Management did not adequately establish an adequate performance management system to ensure that reported performance was appropriately defined and verifiable. Furthermore, inadequate monitoring resulted in reoccurring of non-compliance with legislation.

Material irregularities

52. In accordance with the PAA and the material irregularity (MI) regulations, I have a responsibility to report on material irregularities identified during the audit and on the status of material irregularities as previously reported in the auditor's report.

Status of previously reported material irregularities

Interest paid to Eskom due to late payment of invoices

53. The municipality paid interest to Eskom on invoices that were not paid within 30 days. The payments not made within 30 days constitute non-compliance with section 65(2)(e) of the MFMA, which requires the accounting officer to take all reasonable steps to ensure that all money owing by the municipality are paid within 30 days of receiving the relevant invoice or statement, unless prescribed otherwise for certain categories of expenditure.
54. The non-compliance resulted in a material financial loss of R5 million in the form of interest, which is included as fruitless and wasteful expenditure in note 46 to the financial statements.
55. The accounting officer was notified of the material irregularity on 18 November 2021 and was invited to make a written submission on the actions taken and those that will be taken to address the matter. The accounting officer responded by providing evidence of investigation concluded on 15 December 2021. The investigation concluded that there were insufficient funds to make the payment on time and no persons were identified to be responsible. The investigation further found that there was no breakdown in controls and that the unavailability of funds was the main root cause.
56. The following actions have been taken to respond to the material irregularity:
- The municipality proposed a payment arrangement with Eskom in July 2023 and further applied for debt relief as per circular 124 of the MFMA in August 2023.
 - The municipality has engaged the high court to set aside (as it considered to be invalid), the council decision for standardisation of salaries. The case was set down on 2 November 2023, whereby judgement was reserved. The outcome of this case is expected to significantly improve the municipality's cash flows.

- The municipality has implemented revenue enhancement strategies and cost containment policy to strengthen its financial management controls, where implementation is reviewed monthly by the CFO.
- The council initiated a legal process of recovering some of the capital outlaid in procuring the fleet. The case was dismissed by the court in November 2022 and subsequent to that the municipality lodged an appeal application which was granted in June 2023. The municipality subsequently lodged a notice of appeal in July 2023.

57. The following actions are planned to be taken to respond the material irregularity:

- Follow up with Treasury for approval of the Eskom debt relief incentive application.
- Monthly payments towards Eskom old debt and settling of current invoices whilst awaiting outcome of application.
- Continuous implementation of the financial recovery plan, revenue enhancement strategy and cost containment policy to mitigate its financial crisis.

58. I will follow up on the implementation of the planned actions during the next audit.

Interest and penalties charged by SARS due to late payments

59. The municipality did not pay employees' tax that was deducted from employees over to the South African Revenue Services (SARS) within seven days after the end of the month during which the amount was deducted. This was in contravention of section 2(1) of the Fourth Schedule of the Income Tax Act and section 210 of Tax Administration Act. The municipality was required to pay penalties to SARS due to non-compliance with the Income Tax Act.

60. The non-compliance resulted in a material financial loss of R3.8 million in the form of interest, which is included as fruitless and wasteful expenditure in note 46 to the financial statements.

61. The accounting officer was notified of the material irregularity on 26 November 2021 and was invited to make a written submission on the actions taken and those that will be taken to address the matter. The accounting officer responded by providing evidence of investigation concluded on 22 January 2022. The investigation concluded that there were insufficient funds to make the payment on time and no persons were identified to be responsible. The investigation also found that there was no breakdown in controls and that the unavailability of funds was the main root cause.

62. The following actions have been taken to respond to the material irregularity:

- The municipality has engaged the high court to set aside (as it considered to be invalid), the council decision for standardisation of salaries. The case was set down on 2 November 2023, whereby judgement was reserved. The outcome of this case is expected to significantly improve the municipality's cash flows.
- The municipality has implemented revenue enhancement strategies and cost containment policy to strengthen its financial management controls, where implementation is reviewed monthly by the CFO.

- The council initiated a legal process of recovering some of the capital outlaid in procuring the fleet. The case was dismissed by the court in November 2022 and subsequent to that the municipality lodged an appeal application which was granted in June 2023. The municipality subsequently lodged a notice of appeal in July 2023.

63. The following actions are planned to be taken to respond to the material irregularity:

- Continuous implementation of the financial recovery plan, revenue enhancement strategy and cost containment policy to mitigate its financial crisis.

64. I will follow up on the implementation of the planned actions during the next audit.

Auditor - General

East London

12 December 2023



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

Annexure to the auditor's report

The annexure includes the following:

- The auditor-general's responsibility for the audit
- The selected legislative requirements for compliance testing

Auditor-general's responsibility for the audit

Professional judgement and professional scepticism

As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements and the procedures performed on reported performance information for selected development priority and on municipality's compliance with selected requirements in key legislation.

Financial statements

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
- conclude on the appropriateness of the use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists relating to events or conditions that may cast significant doubt on the ability of the municipality to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify my opinion on the financial statements. My conclusions are based on the information available to me at the date of this auditor's report. However, future events or conditions may cause a municipality to cease operating as a going concern
- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and determine whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

Communication with those charged with governance

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 provide the accounting officer with a statement that I have complied with relevant ethical requirements regarding independence and communicate with them all relationships and other matters that may reasonably be thought to bear on my independence and, where applicable, actions taken to eliminate threats or safeguards applied.

Compliance with legislation – selected legislative requirements

The selected legislative requirements are as follows:

Legislation	Sections or regulations
Municipal Finance Management Act 56 of 2003	Section 1 - Paragraph (a), (b) & (d) of the definition: irregular expenditure, Section 1 - Definition: service delivery and budget implementation plan, Sections 11(1), 13(2), 14(1), 14(2)(a), 14(2)(b), 15, 24(2)(c)(iv), 29(1), Sections 29(2)(b), 32(2), 32(2)(a), 32(2)(a)(i), 32(2)(a)(ii), 32(2)(b), Sections 32(6)(a), 32(7), 53(1)(c)(ii), 54(1)(c), 62(1)(d), 62(1)(f)(i), Sections 62(1)(f)(ii), 62(1)(f)(iii), 63(1)(a), 63(2)(a), 63(2)(c), 64(2)(b), Sections 64(2)(c), 64(2)(e), 64(2)(f), 64(2)(g), 65(2)(a), 65(2)(b), 65(2)(e), Sections 72(1)(a)(ii), 112(1)(j), 116(2)(b), 116(2)(c)(ii), 117, 122(1), Sections 122(2), 126(1)(a), 126(1)(b), 127(2), 127(5)(a)(i), 127(5)(a)(ii), Sections 129(1), 129(3), 133(1)(a), 133(1)(c)(i), 133(1)(c)(ii), 170, Sections 171(4)(a), 171(4)(b)
MFMA: Municipal Budget and Reporting Regulations, 2009	Regulations 71(1), 71(2), 72
MFMA: Municipal Investment Regulations, 2005	Regulations 3(1)(a), 3(3), 6, 7, 12(2), 12(3)
MFMA: Municipal Regulations on Financial Misconduct Procedures and Criminal Proceedings, 2014	Regulations 5(4), 6(8)(a), 6(8)(b), 10(1)
MFMA: Municipal Supply Chain Management Regulations, 2017	Regulations 5, 12(1)(c), 12(3), 13(b), 13(c), 13(c)(i), 16(a), 17(1)(a), Regulations 17(1)(b), 17(1)(c), 19(a), 21(b), 22(1)(b)(i), 22(2), 27(2)(a), Regulations 27(2)(e), 28(1)(a)(i), 28(1)(a)(ii), 29(1)(a), 29(1)(b), Regulations 29(5)(a)(ii), 29(5)(b)(ii), 32, 36(1), 36(1)(a), 38(1)(c), Regulations 38(1)(d)(ii), 38(1)(e), 38(1)(g)(i), 38(1)(g)(ii), 38(1)(g)(iii), 43, Regulations 44, 46(2)(e), 46(2)(f)
Municipal Systems Act 32 of 2000	Sections 25(1), 26(a), 26(c), 26(h), 26(i), 29(1)(b)(ii), 29(3)(b), 34(a), 34(b), Sections 38(a), 41(1)(a), 41(1)(b), 41(1)(c)(ii), 42, 43(2), 56(a), 57(2)(a), Sections 57(4B), 57(6)(a), 66(1)(a), 66(1)(b), 67(1)(d), 74(1), 93J(1), 96(b) Parent municipality with ME: Sections 93B(a), 93B(b)

Legislation	Sections or regulations
	Parent municipality with shared control of ME: Sections 93C(a)(iv), 93C(a)(v)
MSA: Municipal Planning and performance Management Regulations, 2001	Regulations 2(1)(e), 2(3)(a), 3(3), 3(4)(b), 3(6)(a), 7(1), 8, 9(1)(a), 10(a), Regulations 12(1), 15(1)(a)(i), 15(1)(a)(ii)
MSA: Municipal Performance Regulations for Municipal Managers and Managers directly Accountable to Municipal Managers, 2006	Regulations 2(3)(a), 4(4)(b), 8(1), 8(2), 8(3)
MSA: Regulations on Appointment and Conditions of Employment of Senior Managers, 2014	Regulations 17(2), 36(1)(a)
MSA: Disciplinary Regulations for Senior Managers, 2011	Regulations 5(2), 5(3), 5(6), 8(4)
Annual Division of Revenue Act	Section 11(6)(b), 12(5), 16(1), 16(3)
Construction Industry Development Board Act 38 of 2000	Section 18(1)
Construction Industry Development Board Regulations	Regulations 17, 25(7A)
Municipal Property Rates Act 6 of 2004	Section 3(1)
Preferential Procurement Policy Framework Act 5 of 2000	Sections 2(1)(a), 2(1)(f)
Preferential Procurement Regulations, 2017	Regulations 4(1), 4(2), 5(1), 5(3), 5(6), 5(7), 6(1), 6(2), 6(3), 6(6), 6(8), Regulations 7(1), 7(2), 7(3), 7(6), 7(8), 8(2), 8(5) 9(1), 10(1), 10(2), Regulations 11(1), 11(2)
Preferential Procurement Regulations, 2022	Regulations 4(1), 4(2), 4(3), 4(4), 5(1), 5(2), 5(3), 5(4)
Prevention and Combating of Corrupt Activities Act 12 of 2004	Section 34(1)