Report of the auditor-general to the Eastern Cape Provincial Legislature and council on the Raymond Mhlaba Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Raymond Mhlaba Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2022, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget information with 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 thepossible effects of the matters described in the basis for qualified opinion section of this auditor's report, the financial statements present fairly, in all material respects, the financial position of the Raymond Mhlaba Local Municipality as at 30 June 2022 and its financial performance and cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act 56 of 2003 (MFMA) and Division of Revenue Act 9 of 2021 (Dora).

Basis for qualified opinion

Receivables from non-exchange transaction

3. The municipality did not account for all receivables from non-exchange transactions as required by GRAP 104, *Financial instruments*. The municipality did not include all debtors from the billing system in the debtor's age analysis. I was unable to determine the full extent of the understatement of receivables from non-exchange to the financial statements as it was impracticable to do so.

Payables from exchange transactions – trade payables

4. The Municipality did not recognise all outstanding amounts meeting the definition of a liability in accordance with GRAP 1, *Presentation of financial statements*. As the municipality did not maintain adequate records of outstanding payments for goods and services received but not yet paid at year-end, I was unable to determine the full extent of the understatement of trade payables in note 12 to the financial statements as it was impracticable to do so.

Payables from exchange transactions – debtors with credit balances

5. The municipality did not have an adequate system in place to verify all debtors with credit balances. As a result, I was unable to obtain sufficient appropriate audit evidence to confirm the existence of debtors with credit balances and I was unable to confirm this by alternative means.

Consequently, I was unable to determine whether any adjustments were necessary to debtors with credit balances stated at R31,2 million in note 12 to the financial statements.

Irregular expenditure

6. The municipality did not have proper systems in place to identify and disclose all irregular expenditure as required by section 125(2)(d) of the MFMA. This expenditure resulted from payments made in contravention of the supply chain management (SCM) regulations. I was unable to confirm the amount of irregular expenditure by alternative means. It was impracticable to determine the full extent of the understatement. Consequently, I was unable to determine whether any adjustments were necessary to the irregular expenditure, disclosed at R51,7 million in note 46.3 to the financial statements.

Corresponding figures – Bulk purchases

7. I was unable to obtain sufficient appropriate audit evidence to confirm that bulk purchases were actually received by the municipality due to the lack of adequate systems and processes in place to verify the units purchased. I could not confirm the expenditure on bulk purchases by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to bulk purchases, stated at R69,4 million in the financial statements.

Context for the opinion

8. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of my report.

9. 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.

10. 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 financial sustainability

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

12. I draw attention to note 57 in the financial statements, which indicates that the municipality's current liabilities at 30 June 2022 exceeded the current assets. This situation, along with other matters as set forth in note 57, indicate the existence of a material uncertainty that may cast significant doubt about the entity's ability to continue as a going concern.

Emphasis of matters

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

Restatement of corresponding figures

14. As disclosed in note 42 to the financial statements, the corresponding figures for 30 June 2021 were restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2022.

Impairments

15. As disclosed in note 4 to the financial statements, the municipality incurred material losses of R280,5 million (2021: R236,5 million) as a result of the allowance for impairment on service receivables.

Other matters

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

Unaudited disclosure note

17. 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.

Unaudited supplementary schedules

18. The supplementary information 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 these schedules and, accordingly, I do not express an opinion on them.

Responsibilities of the accounting officer for the financial statements

19. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA, 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.

20. 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.

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

21. 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.

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

Report on the audit of the annual performance report

Introduction and scope

23. In accordance with the Public Audit Act 25 of 2004 (PAA) and the general notice issued in terms thereof, I have a responsibility to report on the usefulness and reliability of the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report. I performed procedures to identify material findings but not to gather evidence to express assurance.

24. My procedures address the usefulness and reliability of the reported performance information, which must be based on the municipality's approved performance planning documents. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures do not examine whether the actions taken by the municipality enabled service delivery. My procedures do not extend to any disclosures or assertions relating to the extent of achievements in the current year or 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.

25. 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 development priorities presented in the municipality's annual performance report for the year ended 30 June 2022:

Development priority	Pages in the annual performance report
KPA 2 – Basic service delivery and infrastructure development	x – x

26. 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.

27. The material findings on the usefulness of the performance information of the selected development priority are as follows:

KPA 2 – Basic service delivery and infrastructure development

Number of refuse removal collected from formal households

28. The planned indicator was not specific in clearly identifying the nature and required level of performance as the indicator is worded to refer to the amount of refuse removed from formal households whereas the actual measure is the number of formal households from which refuse is collected.

Other matters

29. I draw attention to the matters below.

Achievement of planned targets

30. Refer to the annual performance report on pages ... to ... for information on the achievement of planned targets for the year and management's explanations provided for the under/over achievement of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance.

Adjustment of material misstatements

31. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information of KPA 2 – Basic service delivery and infrastructure development. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness of the reported performance information. Those that were not corrected are reported above.

Report on the audit of compliance with legislation

Introduction and scope

32. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the municipality's compliance with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

33. The material findings on compliance with specific matters in key legislation are as follows:

Financial statements, performance report and annual report

34. 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 non-current assets, revenue and expenditure identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.

Expenditure management

35. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred and accounted for creditors, as required by section 65(2)(b) of the MFMA.

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

37. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The expenditure disclosed does not reflect the full extent of the irregular expenditure incurred, as indicated in the basis for qualification paragraph. The majority of the disclosed irregular expenditure was caused by non-compliance with SCM regulations.

38. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R16,6 million, as disclosed in note 46.2 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by interest and penalties on late payments.

Asset management

39. An adequate management, accounting and information system that accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.

Strategic planning and performance management

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

Procurement and contract management

41. Sufficient appropriate audit evidence could not be obtained that contracts were extended or modified with the approval of a properly delegated official as required by SCM Regulation 5.

42. Some of the invitations for competitive bidding were not advertised for a required minimum period of days, in contravention of SCM regulation 22(1) and 22(2).

43. Awards were made to providers who were in the service of the municipality, in contravention of section 112(j) of the MFMA and SCM regulation 44. Furthermore, the provider failed to declare that he was in the service of the municipality, as required by SCM regulation 13(c). Similar non-compliance was reported in the previous year and the municipality did not take disciplinary action against the suppliers and officials involved.

Other information

44. 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 and those selected development priorities presented in the annual performance report that have been specifically reported in this auditor's report.

45. 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 on it.

46. 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 development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

47. If, based on the work I have performed, I conclude that there is a material misstatement in this other information; I am required to report that fact. I have nothing to report in this regard.

Internal control deficiencies

48. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

49. Leadership did not adequately discharge its oversight of the implementation and monitoring of internal controls to ensure sound financial and performance management and compliance with legislation. Although leadership had developed an audit action plan to address the prior year external audit findings, not all actions were implemented adequately resulting in repeat findings in the current year

50. Management introduced a new accounting system, during the year under review which has the capability of storing the municipality's supporting documents online. This system however did not operate as anticipated as the required documentation could not be retrieved from the system, it also did not pull through the information from other system resulting in errors on debtors and payables.

51. Although the internal audit and audit committee were in place at the municipality, management did not adequately implement the recommendations made by these structures. This limited the effectiveness of these structures in contributing to an improved control environment at the municipality.

Material irregularities

52. In accordance with the PAA and the Material Irregularity Regulations, I have a responsibility to report on material irregularities identified during the audit.

Material irregularities identified during the audit

Interest incurred on Eskom account not paid within 30 days (note 46.2)

53. The municipality incurred interest to Eskom on invoices from 1 July 2019 to 30 March 2020 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 be paid within 30 days of receiving the relevant invoice or statement, unless prescribed otherwise for certain categories of expenditure.

54. This non-compliance resulted in material financial loss of R6,3 million as disclosed in the corresponding amounts of note 46.2 to the financial statements.

55. I notified the accounting officer of the material irregularity on 14 January 2022 and invited her to make a written submission on the actions that had been or would be taken to address the matter. The accounting officer made written submissions and I considered the representations made and the documents submitted and concluded that appropriate actions are not being taken to address the material irregularity.

56. I recommend that the accounting officer should take the following actions to address the material irregularity, which should be implemented by 30 June 2023 with progress reports every 2 months:

    1) Negotiate a reasonable payment arrangement with Eskom and properly budget for the amounts to be paid.
    2) Appropriate action should be taken to implement the existing financial plan to address the financial problems of the municipality that are preventing it from paying Eskom within 30 days, as required by MFMA section 65(2)(e). The financial plan should include realistic timeframes and milestones to be achieved and include as a minimum strategies to:
        (a) Implement the revenue enhancement interventions with the intention to increase the collection of revenue;
        (b) Efficiently manage the available resources of the municipality to optimise and reduce costs by eliminating wastage whilst obtaining value in respect of all costs incurred.

57. I will follow-up on the implementation of the recommendations, within the time frame stipulated, as required by section 5A (1) of the PAA.

Penalties paid due to late payment of third-party payments

58. The municipality did not pay employees' tax, deducted from employees salaries and wages, to the South African Revenue Service (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 58 of 1962 (Income Tax Act) and section 210 of the Tax Administration

Act 28 of 2011. The municipality was required to pay penalties to SARS due to the non-compliance with the Income Tax Act. This non-compliance resulted in a material financial loss to the municipality amounting to R1,7 million, as disclosed in the annual financial statements.

59. I notified the accounting officer of the material irregularity on 14 January 2022 and invited them to make a written submission on the actions that had been or would be taken to address the matter. The accounting officer accounting performed and investigation and instituted consequence management against the officials identified. The accounting officer further concluded that it was impractical to recover the loss recovered and referred the matter to municipal public accounts committee.

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

East London

30 November 2022

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 this auditor's report, I also:

   - identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error; design and perform audit procedures responsive to those risks; and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control
   - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control
   - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer
   - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists relating to events or conditions that may cast significant doubt on the ability of the Raymond Mhlaba Local 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

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 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.