INTSIKA YETHU LOCAL MUNICIPALITY

Audit Report

For the year ended 30 June 2022

AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence

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

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Intsika Yethu Local Municipality set out on pages … to …, which comprise the statement of financial position as at 30 June 2022, 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 the effects of the matters described in the basis for qualified opinion section of this report, the financial statements present fairly, in all material respects, the financial position of the Intsika Yethu Local Municipality as at 30 June 2022, and its financial performance and cash flows for the year then ended in accordance with South African Standards of Generally Recognised Accounting Practice (GRAP) and the requirements of the Municipal Finance Management Act No. 56 of 2003 (MFMA) and the Division of Revenue Act No. 9 of 2021 (Dora).

Basis for qualified opinion

Property, plant and equipment

3. The municipality did not assess all assets for impairment in accordance with GRAP 21, *Impairment of non-cash-generating assets*. Damaged and significantly deteriorated assets were included in the infrastructure assets without being impaired. Furthermore the municipality did not account for its property, plant and equipment in accordance with GRAP 17, *Property plant and equipment*. Certain fixed assets recorded in the municipality's fixed asset register could not be located during the physical verification of assets. Consequently, I was unable to determine the full extent of the overstatement of property, plant and equipment stated at R525,7 million (2021: R535,2 million) in note 7 to the financial statements and the understatement of impairment loss stated at R18,7 million in note 30 to the financial statements, as it was impractical to do so.

Context for the opinion

4. 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.

5. 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.

6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Emphasis of matters

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

Restatement of corresponding figures

8. As disclosed in note 38 to the financial statements, the corresponding figures for 30 June 2021 were restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2021.

Other matter

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

Unaudited disclosure note

10. 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

11. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with Standards of 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 financial statements that are free from material misstatement, whether due to fraud or error.

12. 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

13. 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.

14. 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

15. 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 key performance areas presented in the annual performance report. I performed procedures to identify material findings but not to gather evidence to express assurance.

16. 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.

17. 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 key performance area presented in the municipality's annual performance report for the year ended 30 June 2022:

Key performance areas	Pages in the annual performance report
KPA 1 – basic services and infrastructure development	x – x

18. I performed procedures to determine whether the reported performance information was properly presented and whether performance 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.

19. The material findings on the usefulness of the performance information of the selected key performance areas are as follows:

KPA 1 – basic services and infrastructure development

Various indicators

20. The planned targets for the following indicators were not specific in clearly identifying the nature and required level of performance:

Indicator name in annual performance report	Indicator target in annual performance report
Number of Km's of access roads constructed as per defined project list	42,4 km
Number of Km's of gravel roads maintained as per defined project list	11 km
Number of areas receiving waste management service	12

Number of dwellings provided with connections to the mains electricity supply

21. The reason provided for the variance between the planned target of 200 and the reported achievement of 0, did not agree to the supporting evidence provided.

Other matter

22. I draw attention to the matter below.

Achievement of planned targets

23. Refer to the annual performance report on pages ... to ... for information on the achievement of planned targets for the year. This information should be considered in the context of the material findings on the usefulness of the reported performance information in paragraphs 20 and 21 of this report.

Report on the audit of compliance with legislation

Introduction and scope

24. 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.

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

Annual financial statements, performance report and annual report

26. 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. 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 and disclosure items 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.

Strategic planning and performance management

27. The performance management system and related controls were inadequate as it did not describe how the performance planning processes should be organised, as required by municipal planning and performance management regulation 7(1).

Asset management

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

Expenditure management

29. Reasonable steps were not taken to prevent irregular expenditure amounting to R46 604 751 as disclosed in note 40 to the annual financial statements, as required by section 62(1)(d) of the MFMA. Most of the irregular expenditure was caused by contravention of legislation relating to supply chain management.

30. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R19 263 620, as disclosed in note 40 to the financial statements, in contravention of section 62(1)(d) of the MFMA. Most of the disclosed fruitless and wasteful expenditure was caused by payments to suppliers for interest or for work not done.

31. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R36 174 223, as disclosed in note 40 to the financial statements, in contravention of section 62(1)(d) of the MFMA. Most of the unauthorised expenditure was caused by the overspending of the budget.

Procurement and contract management

32. Some tender submissions that failed to achieve the minimum qualifying score for functionality criteria were not disqualified in accordance with preferential procurement regulation 5(6) of 2017.

33. The performance of some contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.

34. Contract performance and monitoring measures were not in place to ensure effective contract management, as required by section 116(2)(c)(ii) of the MFMA.

Consequence management

35. Some of the 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.

36. Some of the irregular 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.

Human resource management

37. Appropriate systems and procedures to monitor, measure and evaluate the performance of staff were not developed and adopted, as required by section 67(1)(d) of the Municipal Systems Act 32 of 2000.

Other information

38. 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 key performance areas presented in the annual performance report that have been specifically reported in this auditor's report.

39. 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.

40. 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 key performance areas presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

41. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, and 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

42. 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.

43. There was insufficient oversight to ensure consistent implementation and monitoring of controls over financial information, performance information and compliance with legislation. This was due to a lack of capacity and accountability as well as inadequate communication between departments within the municipality.

44. The municipality did not have a proper system of record management for the financial environment as material misstatements were identified, resulting in a qualified audit opinion.

45. The municipality did not have adequate systems to monitor compliance with all applicable legislation and, as a result, non-compliance with legislation was not prevented. There were inadequate supervision, monitoring and consequence management in respect of the management of municipal operations.

46. Although the municipality developed an audit action plan to address audit findings, the plan was not implemented throughout the year; therefore resulting in recurring material misstatements.

Material irregularities

47. In accordance with the PAA and the Material Irregularity Regulations, I have a responsibility to report on material irregularities identified during the audit and on the status of material irregularities reported in the previous year's auditor's report.

Material irregularities identified during the audit

Payment for goods not received

48. The municipality made payments to multiple suppliers for upgrading gravel roads in Cofimvaba extension 1, but did not receive the related goods or services amounting to a likely material financial loss. The municipality's controls were not effective as they did not prevent the municipality from paying the contractor for preliminary and general costs and contract price adjustments without receiving full value.

49. The municipality therefore did not comply with section 65(2)(a) of the MFMA, which requires reasonable steps to be taken to ensure that the municipality has and maintains an effective system of expenditure control including procedures for the approval, authorisation, withdrawal and payment of funds. The non-compliance resulted in a likely material financial loss for the municipality by 1 April 2019.

50. The accounting officer was notified of the material irregularity on 16 November 2021. Council referred the material irregularity to MPAC for investigation and recovery process. An independent service provider was appointed by the Accounting Officer to investigate the matter and whose findings at the conclusion would be tabled before the Council for its

consideration and decision making. The Accounting Officer then reported the matter to South African Police Services in accordance with the MFMA.

51. The disciplinary board was appointed to conduct an investigation with view of a disciplinary process regarding the project. The new MPAC which assumed duties after the elections is still investigating and its report will be presented to Council for its consideration. The municipal public accounts committee and the disciplinary board recommended that a forensic investigation be conducted. The investigation was still in progress at the date of this report.

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

Material irregularities in progress

53. I identified a material irregularity during the audit and notified the accounting officer, as required by material irregularity regulation 3(2). By the date of this auditor's report, I had not yet completed the process of evaluating the response from the accounting officer. This material irregularity will be included in the next year's auditor's report.

Other reports

54. In addition to the investigations relating to material irregularities, I draw attention to the following engagements conducted by various parties which 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 do not form part of my opinion on the financial statements or my findings on the reported performance information or compliance with legislation.

55. The Directorate for Priority Crime Investigation (Hawks) is investigating allegations of fraudulent expenditure emanating from the awarding of the contract for upgrading gravel roads to surfaced roads in extension 1. The investigation was still in progress at the date of this report.

Auditor - General

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 key performance areas 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 Intsika Yethu 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 to 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.