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

Report on the audit of the financial statements

Qualified of opinion

1. I have audited the financial statements of the Setsoto Local Municipality set out on pages ... to ... and ... to ..., which comprise the statement of financial position as at 30 June 2021, statement of financial performance, statement of changes in net assets, cash flow statement, statement of comparison of budget information with actual information 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 and the possible 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 Setsoto Local Municipality as at 30 June 2021, and its financial performance and cash flows for the year then ended in accordance with the South African 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 10 of 2020 (Dora).

Basis for qualified opinion

Service charges

3. I was unable to obtain sufficient appropriate audit evidence for service charges of electricity and water, as the municipality did not have adequate systems in place to adequately account for the billing of services based on the consumer's monthly consumption. I was unable to confirm the service charges by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to service charges stated at R199 680 856 (2020: R189 913 073) in note 22 to the financial statements.

Provisions

4. I was unable to obtain sufficient appropriate audit evidence for the provision for environmental rehabilitation, as the municipality did not have adequate systems in place to provide adequate supporting evidence for the estimated costs and assumptions used in determining the provision for environmental rehabilitation. I was unable to confirm the provision for environment rehabilitation by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to the provision for environmental rehabilitation stated at R15 796 102 in note 18 to the financial statements.

Context for the 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 auditor-general's responsibilities 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. Note 43 to the financial statements indicates that the municipality incurred a net loss of R218 145 943 during the year ended 30 June 2021. In addition, the municipality had an average creditors payment period of 139 days and the municipality owed Eskom R28 064 402 (2020: R32 779 491) as at 30 June 2021. These events or conditions, along with other matters set out 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

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

Irregular expenditure

10. As disclosed in note 47 to the financial statements, the municipality incurred irregular expenditure of R77 876 589 (2020: R92 455 092), due to non-compliance with supply chain management (SCM) requirements.

Unauthorised expenditure

11. As disclosed in note 45 to the financial statements, the municipality incurred unauthorised expenditure of R319 561 516 (2020: R127 354 819), due to the overspending of the budget as a result of non-cash items.

Restatement of corresponding figures

12. As disclosed in note 41 to the financial statements, the corresponding figures for 30 June 2020 were restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2021.

Material uncertainty relating to claims against the municipality

13. With reference to note 52 to the financial statements, the municipality is the defendant in various claims against the municipality. The municipality is opposing these claims. The ultimate

outcome of these matters could not be determined and no provision for any liabilities that may result was made in the financial statements.

Material losses

14. As disclosed in note 49 to the financial statements, material water distribution losses of R12 098 388 (2020: R15 425 713) and electricity distribution losses of R10 706 280 (2020: R11 112 061) were incurred by the municipality mainly due to leakages, burst water pipes, line losses, tampering and theft.

Material impairment

15. As disclosed in note 10 to the financial statements, consumer debtors were impaired by R252 831 528 (2020: R185 239 119).

Other matters

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

Unaudited disclosure notes

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 thereon.

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 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.

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 material findings on the usefulness and reliability of the reported performance information against predetermined objectives for the selected key performance area (KPA) 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 KPA presented in the municipality's annual performance report for the year ended 30 June 2021:

KPA	Pages in the annual performance report
KPA 1 – basic service delivery and infrastructure	x – x

26. 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.

27. The material findings on the usefulness and reliability of the performance information of the selected KPA are as follows:

KPA 1 – basic services and infrastructure

Various indicators

28. The indicators listed below were approved in the service delivery and budget implementation plan for the 2020-2021 financial year, but they were not reported on in the annual performance report. As a result, I was unable to audit the reliability of the indicators. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the indicators listed below:

Indicator description	Planned target
Percentage of total water losses	30%
Percentage of households with access to basic sanitation	97%
Percentage of households with access to basic water supply	100%

29. I was unable to obtain sufficient appropriate audit evidence to support the measures taken to improve performance against the targets listed below as reported in the annual performance report. This was due to limitations placed on the scope of my work and/or adequate supporting evidence was not provided for the measures reported. I was unable to confirm the reported measures taken by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported measures taken to improve performance:

Indicator description	Planned target	Reported achievement
Percentage of progress made on the development of the water network on 1110 site with water Marquard/ Moemaneng	1%	0%
Percentage of progress made on the development of the sewer network on 1110 site with sewer Marquard/Matwabeng	1%	0%
Percentage of progress made on upgrading of van soelen in Meqheleng/Ficksburg	29%	0%
Percentage of progress made on conversion of 969 VIP into waterborne sanitation system	0%	0%
Percentage of progress on the upgrading of the wastewater treatment works in Clocolan/Hlohlolwane	10%	0%
Percentage of replacement of an old 5km asbestos water rising main pipeline in Clocolan/Hlohlolwane completed	50%	0%
Percentage of Ficksburg/Meqheleng: Rehabilitation of 1,5 km surfaced and storm water drainage completed	30%	0%
MIG covid-19: development of boreholes in Marquard/ Moemaneng	25%	0%
Percentage of construction of Cyferfontein raw water abstraction pump station: earth works, casted concrete reinforcement walls and roof mechanical concrete doors completed	29%	0%
Percentage of the resuscitation of the WWTW in Senekal/Matwabeng	100%	0%
RBIG covid-19: development of boreholes in Clocolan/ Hlohlolwane	100%	0%

30. The achievements reported in the annual performance report differed materially from the supporting evidence provided for the indicators listed below:

Indicator description	Reported achievement
Percentage of unblocked sewer spillages	100%
Percentage of repaired/replaced sewer manholes	100%
Percentage of VIP and septic tanks serviced	100%

Other matters

31. I draw attention to the matters below.

Achievement of planned targets

32. 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 and reliability of the reported performance information in paragraphs 28 to 30 of this report.

Adjustment of material misstatements

33. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information of KPA 1 – basic services and infrastructure. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

Report on the audit of compliance with legislation

Introduction and scope

34. 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.

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

Annual financial statements

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 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.

37. The financial statements were not submitted to the auditor-general, for auditing, within two months after the end of the financial year, as required by section 126(1)(a) of the MFMA.

Expenditure management

38. Reasonable steps were not taken to prevent irregular expenditure amounting to R77 876 589 as disclosed in note 47 to the financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by non-compliance with SCM requirements.

39. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R2 504 899, as disclosed in note 46 to the 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 charged by the South African Revenue Service (Sars).

40. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R319 561 516, as disclosed in note 45 to the financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by overspending of the expenditure vote.

Revenue management

41. An effective system of internal control for debtors/revenue was not in place, as required by section 64(2)(f) of the MFMA.

Strategic planning and performance management

42. The internal controls processes relating to the performance monitoring, measurement, review and reporting were not performed, as required by municipal planning and performance management reg 7(1).

Procurement and contract management

43. 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(1)(a) and (c). A similar non-compliance was also reported in the prior year.

44. Sufficient appropriate audit evidence could not be obtained that invitations for competitive bidding were advertised for a required minimum period of days, as required by SCM regulation 22(1) and 22(2).

45. 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. A similar limitation was also reported in the prior year. This limitation was identified in the procurement processes for the upgrading of wastewater treatment works (WTW) in Clocolan and upgrading of the De Put 500 mm raw water pipeline from De Put dam to WTW in Senekal/Matwabeng.

46. The performance of some of the contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA. Similar non-compliance was also reported in the prior year. This non-compliance was identified in the procurement processes for the upgrading of WTW in Clocolan and upgrading of the De Put 500 mm raw water pipeline from the De Put dam to WTW in Senekal/Matwabeng.

47. The 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. A similar non-compliance was also reported in the prior year.

Utilisation of conditional grants

48. I was unable to obtain sufficient appropriate audit evidence that the regional bulk infrastructure grant was spent for its intended purposes in accordance with the applicable grant framework, as required by section 17(1) of the Dora.

Consequence management

49. 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.

50. 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.

Strategic planning and performance management

51. The internal controls processes relating to the performance monitoring, measurement, review and reporting were not performed, as required by municipal planning and performance management reg 7(1).

Other information

52. 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 the selected KPA presented in the annual performance report that have been specifically reported in this auditor's report.

53. 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.

54. 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 KPA presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

55. 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

56. 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, findings on the annual performance report and the findings on compliance with legislation included in this report.

57. The leadership did not in all instances exercise oversight responsibilities to ensure that accurate and reliable supporting evidence was submitted timeously, as limitation of scope qualifications was reported above. In addition, material misstatements in the financial statements and annual performance report were identified during the audit.

58. The leadership did not implement adequate consequence management to ensure that instances of unauthorised and irregular expenditure were investigated during the financial year and the responsible officials are held accountable for incurring such expenditure.

59. Although the municipality had an action plan to address the prior year findings, this was not adequately implemented and monitored as there was repeat qualifications reported and instances of unauthorised, irregular and fruitless and wasteful expenditure were identified again in the current year due to the slow responses by management.

60. There were vacancies in key management position as well as support staff during the financial year. There was also instability in the accounting officer position. This contributed to the lack of adequate oversight over compliance, financial and performance reporting.

61. Management did not implement adequate processes to effectively monitor compliance with key legislation, which resulted in repeat non-compliance with applicable laws and regulations being reported.

Material irregularities

62. 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 the material irregularities reported in the previous year's auditor's report.

63. The material irregularities identified are as follows:

Eskom not paid within 30 days

64. The accounting officer did not take all reasonable steps to ensure that amounts due to Eskom for the bulk purchases of electricity were paid within 30 days of receiving the relevant invoice or statement, as required by section 65(2)(e) of the MFMA. The late payment resulted in interest of R2 837 021 being incurred for the period 1 April 2019 to 31 March 2020. The interest incurred is likely to result in a material financial loss for the municipality due to the liability to pay the interest to Eskom.

65. The accounting officer was notified of the material irregularity on 30 March 2021 and was invited to make written submission on the actions taken and those that will be taken to address this matter. The following actions have been taken or is in progress to resolve the material irregularity:

- The municipality is continuously engaging with Eskom to reach a mutual agreement on a payment agreement.
- The municipality planned to reduce the electricity distribution losses through various interventions as part of their revenue enhancement strategy implemented within the various departments at the municipality.
- The investigation of the fruitless and wasteful expenditure incurred will be performed by the municipal public accounts committee (MPAC) to determine if any official should be held liable for the loss, once the council elected new committee members towards January 2022.

66. I will follow up on the investigation and the implementation of the planned actions during my next audit.

Late payment of employee taxes

67. The municipality did not pay over money deducted from employees within seven days after the end of the month during which the amounts were deducted or withheld from employees in respect of their liability for normal tax, as required by section 2(1) of the fourth schedule of the Income Tax Act 58 of 1962. The late payment resulted in a material financial loss for the municipality due to interest of R118 071 and penalties of R1 887 396 incurred for the period 1 April 2019 to 30 June 2020.

68. The accounting officer was notified of this material irregularity on 30 March 2021 and was invited to make a written submission on the actions taken and that will be taken to address the matter. The following actions have been taken or is in progress to resolve the material irregularity:

- The municipality paid the full outstanding amount due to the (Sars).
- The municipality is currently in the process of appointing a service provider to assist with the recovery of Value Added Tax and the remission of interest and penalties payable to Sars as part of the revenue enhancement strategy.
- The investigation of the fruitless and wasteful expenditure incurred will be performed by the MPAC to determine if any official should be held liable for the loss, once the council elected new committee members towards January 2022.

69. I will follow up on the investigation and implementation of the planned actions during my next audit.

Auditor-General

Bloemfontein

17 December 2021

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 KPA 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 related to events or conditions that may cast significant doubt on the Setsoto 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 this auditor's report. However, future events or conditions may cause a municipality to cease continuing 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.

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.