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

Report on the audit of the financial statements

Opinion

1. I have audited the financial statements of the Setsoto 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, 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, the financial statements present fairly, in all material respects, the financial position of the Setsoto 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 (GRAP) and the requirements of the Municipal Finance Management Act 56 of 2003 (MFMA) and the Division of Revenue Act 9 of 2021 (Dora).

Basis for opinion

3. 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.

4. 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.

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

Material uncertainty relating to going concern

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

7. The municipality reported a deficit of R124 553 657 for the period ended 30 June 2022. Note 54 to the financial statements indicates that the municipality was unable to pay its creditor's accounts when they fall due. The municipality owed Eskom R22 028 676 (2021: R26 641 637) as at 30 June 2022, which was long overdue. These events or conditions, along with other matters set out in note 54, 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

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

Unauthorised expenditure

9. As disclosed in note 48.1 to the financial statements, the municipality incurred unauthorised expenditure of R176 617 291 (2021: R319 561 516), due to the overspending of the budget.

Irregular expenditure

10. As disclosed in note 48.2 to the financial statements, the municipality incurred irregular expenditure of R53 609 988 (2021: R77 876 589), due to non-compliance with supply chain management (SCM) requirements.

Restatement of corresponding figures

11. As disclosed in note 55 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 2022.

Contingent liabilities

12. With reference to note 43 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

13. As disclosed in note 3 and note 4 to the financial statements, receivables from exchange transactions and receivables from non-exchange transactions were impaired by R250 326 574 (2021: R251 050 115).

14. As disclosed in note 52 to the financial statements, material water distribution losses of R12 717 711 (2021: R12 098 388) and electricity distribution losses of R7 161 780 (2021: R10 706 280) were incurred by the municipality mainly due to leakages, burst water pipes, line losses, tampering and theft.

Other matters

Unaudited disclosure notes

15. 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

16. 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

17. 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 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.

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.

Auditor-general's responsibilities 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

Introduction and scope

21. 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 area (KPA) presented in the annual performance report. I was engaged to perform procedures to identify findings but not to gather evidence to express assurance.

22. I was engaged to evaluate 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 2022:

23. 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 annual performance report of the municipality for the year ended 30 June 2022:

KPA	Pages in the annual performance report
KPA 1 – basic services	x – x

24. 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.

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

KPA 1 – basic services

Percentage of unplanned water interruptions and sewer blockages complaints/callouts responded to within the required timeframe

26. The planned target of 100% for this indicator was not specific in clearly identifying the nature and required level of performance and/or measurable and did not specify the period or deadline for delivery.

Various indicators

27. The reported targets for these indicators did not agree with the planned targets as approved in the service delivery and budget implementation plan (SDBIP) for the indicators listed below:

Indicator descriptions	Planned targets per the SDBIP	Planned targets as per APR
Percentage of households with access to basic sanitation	Blank	97%
Percentage of households with access to basic water supply	Blank	100%
Percentage of unplanned water interruptions and sewer blockages complaints/callouts responded to within require timeframe	Blank	100%
Percentage of households with access to electricity	Blank	100%
Percentage electricity losses	Blank	12%

Various indicators

28. I was unable to obtain sufficient appropriate audit evidence that systems and processes were established to enable consistent measurement and reliable reporting of performance against the predetermined indicator definitions for the indicators listed below. This was due to

insufficient measurement definitions and processes. As a result, I was also unable to obtain sufficient appropriate audit evidence for the achievements reported in the annual performance report as well as the reasons for the variances between the planned targets and these reported achievements of the listed indicators. I was unable to validate the existence of the systems or to confirm the reasons for the variances and the reported achievements by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements and reasons for the variances.

Indicator descriptions	Planned targets	Reported achievements
Percentage electricity losses	12%	34%
Percentage of total water losses	20%	31%
Percentage of callouts on unplanned water services interruption responded to within 24 hours	100%	99%
Percentage of callouts responded to within 24 hours for sanitation	100%	71%
Percentage of household with access to basic water supply	100%	92%
Percentage of households with access to basic sanitation (Municipal managers)	100%	82%
Percentage of households with access to basic sanitation (Directors)	97%	82%
Percentage of households with access to electricity	100%	94%

Various indicators

29. I was unable to obtain sufficient appropriate audit evidence for the achievements reported against targets in the annual performance report, due to the lack of accurate and complete records. I was unable to confirm the reported achievements by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements.

Indicator descriptions	Planned targets	Reported achievements
Percentage of households with access to refuse removal (Municipal managers)	91%	104%
Percentage of households with access to refuse removal (Directors)	90%	95%

Other matters

30. I draw attention to the matters below.

Achievement of planned targets

31. 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 26 to 29 of this report.

Adjustment of material misstatements

32. 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. 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

33. 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.

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

Annual financial statements

35. 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, expenditure, and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected resulting in the financial statements receiving an unqualified audit opinion.

Expenditure management

36. Reasonable steps were not taken to prevent irregular expenditure amounting to R53 609 988 as disclosed in note 48.2 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by non-compliance with SCM requirements.

37. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R176 617 291, as disclosed in note 48.1 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 budget vote.

38. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R2 147 448, as disclosed in note 48.3 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 charged on late payments to the supplier.

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

Strategic planning and performance management

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

Consequence management

41. Unauthorised expenditure incurred by the municipality was not investigated to determine if any person was liable for the expenditure, as required by section 32(2)(a) of the MFMA.

42. Irregular expenditure incurred by the municipality were not investigated to determine if any person was liable for the expenditure, as required by 32(2)(b) of the MFMA and reporting regulations 75(1).

43. Fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person was liable for the expenditure, as required by section 32(2)(b) of the MFMA and reporting regulations 75(1).

Procurement and contract management

44. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).

45. Sufficient appropriate audit evidence could not be obtained that contracts were awarded only to bidders who submitted a declaration on whether they were employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).

46. Sufficient appropriate audit evidence could not be obtained that the performance of contractors or providers was monitored on a monthly basis, as required by section 116(2) of the MFMA. This non-compliance was identified in the procurement processes for the upgrading of Van Soelen outfall sewer pipeline.

47. Sufficient appropriate audit evidence could not be obtained that contract performance and monitoring measures were in place to ensure effective contract management as required by section 116(2)(c)(ii) of the MFMA. A similar limitation was also reported in the prior year. This limitation was identified in the procurement processes for the upgrading of Van Soelen outfall sewer pipeline.

Other information

48. 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 has been specifically reported in this auditor's report.

49. My opinion on the financial statements and findings on the reported performance information and compliance with legislation does not cover the other information and I do not express an audit opinion or any form of assurance conclusion on it.

50. 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.

51. 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

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

53. Leadership did not in all instances exercise oversight, to ensure that accurate and reliable information is submitted timeously, as there were material misstatements in the financial statements and annual performance report that required adjustments during the audit.

54. Council did not ensure that all instances of unauthorised and irregular expenditure are investigated and the responsible officials are held accountable.

55. Although the municipality had an action plan to address the prior year's findings, this was not adequately implemented and monitored as instances of unauthorised, irregular and fruitless and wasteful expenditure and material misstatements in the annual financial statements and annual performance report was identified again in the current year.

56. Management did not implement effective human resource management to ensure that adequate resources are in place and that performance is monitored. There were significant vacancies in key management positions as well as support staff during the financial year.

57. Management did not implement adequate processes to effectively monitor compliance with key legislation, which resulted in non-compliance with applicable laws and regulations in some cases.

Material irregularities

58. 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.

Status of previously reported material irregularities

Eskom not paid within 30 days

59. 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.

60. 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 had several engagements with Eskom to reach a mutual agreement on a payment agreement. Following a meeting held on 19 September 2022, the municipality submitted a proposed payment plan for the period October 22 to 30 June 2023, which was subsequently accepted by Eskom.
- The municipality further reached agreement with Eskom to extend the payment terms from 15 days to 30 days, and to reduce the interest rate on amounts due by 2.5%.
- 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.

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

Interest and penalties on late payment of employee taxes

62. 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.

63. The accounting officer was notified of this material irregularity on 30 March 2021. The following actions have been taken to resolve the material irregularity:

- The municipality paid the full outstanding amount due to the Sars.
- The municipality undertook a process to review its staff establishment, which was approved by council during June 2022.
- As part of its revenue enhancement strategy, the municipality appointed a service provider on 10 January 2022 to assist with the submission of request for remission of penalties and interest against applicable taxes for the past five years.

64. Therefore, the material irregularity has been resolved.

Other reports

65. 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 did not form part of my opinion on the financial statements or my findings on the reported performance information or compliance with legislation.

66. The municipality was under investigation by the Directorate for Priority Crime Investigation (Hawks) due to the alleged fraud and corruption for the conversion of 969 VIP toilets into waterborne sanitation system project. By the date of this report, the report on the outcome of this investigation was not yet available.

Auditor General

Bloemfontein

30 November 2022

AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence

Annexure – Auditor-general's responsibility for the audit

67. 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

68. 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/ accounting authority'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 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 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

69. 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.

70. 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.