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

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Dihlabeng Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2021, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as notes to the financial statements, including a summary of significant accounting policies.

2. In my opinion, except for the effects and 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 Dihlabeng 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

Property, Plant and equipment

3. The municipality did not classify all fixed assets in accordance with GRAP 1, *Presentation of financial statements* as, in some instances, assets were not consistently aggregated by nature or function, but rather by the ultimate use of the asset. In addition, land was not separately disclosed from buildings. Misstatements were identified with regards to the following classes of assets:

Class of assets	2021 overstatement/ (understatement)	2020 overstatement/ (understatement)
Land	R163 811 380	-
Infrastructure water	(R14 025 451)	(R62 916 100)
Infrastructure electrical	(R2 255 819)	R57 703 027
Infrastructure sewer	(R35 298 857)	R18 427 607
Infrastructure roads	R9 782 653	(R2 994 805)
Infrastructure community buildings	(R116 550 483)	(R2 975 334)
Infrastructure storm water	1 468 924	R468 527

Infrastructure solid waste	(6 932 347)	(R7 712 922)

4. Furthermore, I was unable to obtain sufficient appropriate audit evidence for disposals/write-offs of R16 811 420 as there was no adequate system of internal control to substantiate these disposals. I was unable to confirm property, plant and equipment by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to property, plant and equipment stated at R1 750 102 862 (2020: R1 786 845 067) in note 12 to the financial statements.

5. During 2020, I was unable to obtain sufficient appropriate audit evidence for amounts disclosed as transfers in the reconciliation of property, plant and equipment in note 12 as there was no adequate system of internal control to substantiate these transfers. In addition I was unable to confirm the restatement of the corresponding figures for the reversal of prior year impairment as adequate supporting evidence was not provided. I was unable to determine whether any adjustment was necessary to property, plant and equipment stated R1 786 845 067. My audit opinion on the financial statements for the period ended 30 June 2020 was modified accordingly. My opinion on the current year financial statements was also modified because of the possible effect of this matter on the comparability of the property, plant and equipment for the current period.

Commitments

6. I was unable to obtain sufficient appropriate audit evidence for commitments, as the municipality did not maintain accurate and complete records of the contractual information used to determine commitments. I could not confirm the amounts by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to commitments stated at R32 391 150 (2020: R11 410 095) in note 44 to the financial statements.

Contracted services

7. I was unable to obtain sufficient appropriate evidence to confirm that contracted services were only recognised where goods and services were actually received, due to the status of the accounting records. I was unable to confirm contracted services by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to contracted services stated at R87 139 593 (2020: R75 360 256) in note 36 to the financial statements.

General expenditure

8. During 2020, I was unable to obtain sufficient appropriate evidence to confirm that general expenses were only recognised where goods and services were actually received, due to the status of the accounting records. I was unable to confirm general expenses by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to general expenses stated at R65 807 007 in note 37 to the financial statements. My audit opinion on the financial statements for the period ended 30 June 2020 was modified accordingly. My opinion on the current year financial statements was also modified because of

the possible effect of this matter on the comparability of the general expenditure for the current period.

Repairs and maintenance

9. During 2020, I was unable to obtain sufficient appropriate evidence to confirm that repairs and maintenance were only recognised where goods and services were actually received, due to the status of the accounting records. I was unable to confirm repairs and maintenance by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to repairs and maintenance stated at R14 336 826 in the financial statements. My audit opinion on the financial statements for the period ended 30 June 2020 was modified accordingly. My opinion on the current year financial statements was also modified because of the possible effect of this matter on the comparability of the repairs and maintenance for the current period.

Context for the opinion

10. 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.

11. 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.

12. 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

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

14. Note 50 to the financial statements indicates that the municipality incurred a net loss of R164 096 001 for the year ended 30 June 2021 and, as of that date, the municipality's current liabilities exceeded its current assets by R519 051 397. In addition, the municipality owed Eskom R542 013 593 (2020: R404 919 251) and the Department of Water Affairs R54 427 508 (2020: R28 956 389) as at 30 June 2021, which was long overdue. These events or conditions, along with other matters as set forth in note 50, 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

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

Irregular expenditure

16. As disclosed in note 54 to the financial statements, the municipality incurred irregular expenditure of R151 323 677 (2020: R129 954 049), due to non-compliance with supply chain management (SCM) requirements.

Unauthorised expenditure

17. As disclosed in note 52 to the financial statements, the municipality incurred unauthorised expenditure of R255 555 816 (2020: R154 809 376), due to overspending of the budget.

Restatement of corresponding figures

18. As disclosed in note 48 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

19. With reference to note 45 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 were made in the financial statements.

Material losses

20. As disclosed in note 35 to the financial statements, material water distribution losses of R60 294 487 (2020: R32 020 651) and electricity distribution losses of R34 167 819 (2020: R26 236 577) were incurred by the municipality mainly due to leakages, burst water pipes, line losses, tampering and theft.

Material impairment

21. As disclosed in note 6, and 8 to the financial statements, receivables from non-exchange transactions; and consumer debtors from exchange and non-exchange transactions and other receivables were impaired by R1 058 616 883 (2020: R869 729 458).

Other matter

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

Unaudited disclosure notes

23. 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.

Responsibilities of the accounting officer for the financial statements

24. 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.

25. 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

26. 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.

27. 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

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

29. 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 2021:

KPA	Pages in the annual performance report
KPA 1 – accelerated service delivery and infrastructure development (Public works technical services)	x – x

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

KPA 1 – Accelerated service delivery and infrastructure development (Public works technical services)

Various indicators

31. I was unable to obtain sufficient appropriate audit evidence that clearly defined the predetermined source information and method of collection or that related systems and processes were established to enable consistent measurement and reliable reporting of the actual achievement of the indicators listed below. This was due to a lack of measurement definitions and processes. I was unable to confirm that the indicators are well-defined, measurable and verifiable by alternative means.

32. In addition, the reported achievements were not consistent with the planned targets. As a result I was unable to audit the reliability of the achievements in the annual performance report of the listed indicators:

Indicator description	Planned target	Reported achievement
Caledon abstraction upgraded by 2020	Upgrading of Caledon raw water abstraction point in fouriesburg	Finalisation of EIA and WULA realised
44 km raw water pipe line constructed by 2023	Total project budget - R20 000 000	0% progress realised
Clarens water purification works upgraded by 2021	Clarens/Kgubetswana: upgrading of the water purification works (163894)	0% progress realised
Clarens/Phahameng pump station and Kgubetswana lower outfall sewer pipeline upgraded and refurbished by 2021	Upgrading and refurbishment of Clarens/Phahameng pump station and Kgubetswana lower outfall sewer pipeline.	100% construction progress realised
Refurbishment of Bethlehem waste water treatment works	Refurbishment of Bethlehem waste water treatment works	100% construction progress realised

Other matter

33. I draw attention to the matter below.

Achievement of planned targets

34. Refer to the annual performance report on pages xx… to xx… 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 31 to 32 of this report.

Report on the audit of compliance with legislation

Introduction and scope

35. 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.

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

Annual financial statements

37. 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, current assets, liabilities and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

Expenditure management

38. Payments were made from the municipality's bank accounts without the approval of the accounting officer as required by section 11(1) of the MFMA.

39. Reasonable steps were not taken to ensure that the municipality implements and maintains an effective system of expenditure control, including procedures for the approval, authorisation, withdrawal and payment of funds, as required by section 65(2)(a) of the MFMA.

40. 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.

41. Reasonable steps were not taken to prevent irregular expenditure amounting to R151 323 677 as disclosed in note 54 to the financial statements, as required by section 62(1)(d) of the MFMA.

42. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R255 555 816 as disclosed in note 52 to the financial statements, as required by section 62(1)(d) of the MFMA.

Asset management

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

44. 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.

45. Capital assets were transferred without the municipal council having, in a meeting open to the public, decided on whether the assets were still needed to provide the minimum level of basic municipal services and considered the fair market value of the assets and the economic and community value to be received in exchange for the assets, as required by section 14(2)(a) and 14(2)(b) of the MFMA.

Procurement and contract management

46. 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 by SCM Regulation 17(1)(a) and (c). Similar non-compliance was also reported in the prior year.

47. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM Regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM Regulation 36(1).

48. Measures to combat the abuse of the SCM system were not implemented as per the requirements of SCM Regulation 38(1), because some of the contracts were awarded to providers who committed a corrupt or fraudulent act in competing for the contract and abused the SCM system of the municipality.

49. Some of the contracts were awarded to bidders based on preference points that were not calculated in accordance with the requirements of section 2(1)(a) of the Preferential Procurement Policy Framework Act 5 of 2000 and its regulations. This non-compliance was identified in the procurement processes for the appointment of panels for the construction and maintenance of roads and stormwater infrastructure and for the panel for the supply and delivery of electricity materials.

50. The invitation to tender for procurement of commodities designated for local content and production, did not stipulate the minimum threshold for local production and content as required by the 2017 preferential procurement regulation 8(2). Similar non-compliance was also reported in the prior year.

51. 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. Similar non-compliance was also reported in the prior year.

52. 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. Similar non-compliance was also reported in the prior year.

Utilisation of conditional grants

53. Performance in respect of programmes funded by the water services infrastructure grant was not evaluated within two months after the end of the financial year, as required by section 12(5) of the Dora .

54. I was unable to obtain sufficient appropriate audit evidence that the expanded public works 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

55. 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.

56. 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.

57. Fruitless and wasteful 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.

58. Allegations of financial misconduct laid against officials of the municipality were not investigated, as required by section 171(4)(a) of the MFMA.

59. Allegations of financial misconduct laid against officials of the municipality were investigated by the disciplinary board, relevant treasury or an independent investigator or team of investigators appointed by council, as required by municipal regulations on financial misconduct procedures and criminal proceedings 5(4).

60. Cases of financial misconduct which constitute a crime committed by officials were always reported to the South African Police Service, as required by the municipal regulations on financial misconduct procedures and criminal proceedings 10(1).

61. Allegations of theft or fraud which exceeded R100 000 were reported to the South African Police Service, as required by section 34(1) of the Prevention and Combating of Corrupt Activities Act 12 of 2004.

Other information

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

63. 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.

64. 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.

65. 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

66. 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 audit opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

67. Leadership did not implement adequate oversight on the implementation of measures designed to promote a culture of ethical conduct.

68. Leadership and management of the municipality did not exercise adequate oversight over financial and performance reporting and compliance with legislation. The leadership did not take effective steps to ensure that there were consequences for poor performance and transgressions with applicable laws and regulations, as unauthorised, irregular and fruitless and wasteful expenditure was not investigated during the current financial year. The action plans designed to address findings previously reported and to prevent repeat findings were not implemented or were inadequate. This was due to instability in the positions of the municipal manager as well as the chief financial officer during the year and lack of consequence management.

69. Senior management did not implement adequate reviews over the regular disciplines of recording and reconciling of transactions and compliance with regulatory framework. This was due to slow response by management as material misstatements in financial statements and performance reports were not timely detected and corrected.

70. The audit committee was not appropriately constituted, did not implement adequate oversight over risk management and internal controls, nor reported regularly to the municipal council on financial and performance management and reporting. This was due to slow response by management in appointing additional members of the audit committee.

Other reports

71. I draw attention to the following engagements conducted by various parties which had, or could have had, 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.

72. The municipality was under investigation by the Directorate for Priority Crime Investigation (Hawks) on allegations of irregularities in SCM and disposal of assets. The investigation commenced during 2017/18 financial year and was still ongoing at the reporting date.

73. The special investigations unit (SIU) were investigating allegations of irregularities in the implementation of capital projects approved by the National Treasury to address emergency service delivery needs as a result of the national state of disaster due to the Covid-19 pandemic. The investigations were ongoing at the reporting date.

Auditor-General

Bloemfontein

30 November 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 relating to events or conditions that may cast significant doubt on the ability of the Dihlabeng 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.