

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

## Report on the audit of the financial statements

### Opinion

1. I have audited the financial statements of the Phumelela Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2024, statement of financial performance statement of changes in net assets, cash flow statement and 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, the financial statements present fairly, in all material respects, the financial position of the Phumelela Local Municipality as at 30 June 2024 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 5 of 2023 (DoRA).
3. Basis for opinion conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the responsibilities of the auditor-general 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 matters below. My opinion is not modified in respect of these matters.
7. Note 43 of the financial statements indicates that the municipality incurred a net loss of R11 427 735 during the year ended 30 June 2024 and, as of the date, the municipality's deducting pension, medical aid, and pay as you as earn from employees salaries, but has been unable to pay over R5 491 786 of these amounts deducted to the relevant third parties as disclosed in note 52. In addition, the municipality owed Eskom R205 581 201 (2023: R182 438 800) and the Department of Water and Sanitation R151 060 532,09 (2023: R159 798 238) as at 30 June 2024, which was long overdue. These events or conditions, along with other matters as set forth in note 43, indicate a material uncertainty exists that may cast significant doubt on the municipality's ability to going 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.

### **Underspending of conditional grants**

9. As disclosed in note 18 to the financial statements, the municipality materially underspent the conditional grants by R7 000 876 (2023: R13 144 330).

### **Material impairments**

10. As disclosed in note 7 to the financial statements, material losses R498 635 491 were incurred as a result of a write-off of irrecoverable trade debtors.

### **Restatement of corresponding figures**

11. As disclosed in note 40 to the financial statements, the corresponding figures for 30 June 2023 was restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2024.

### **Material losses**

12. As disclosed in note 49 to the financial statements, material electricity losses of R10 308 626 (2023: R5 869 563) were incurred, due to technical losses on the breakdown of transformers, cables, overhead lines, faulty meters, theft and vandalism.

13. As disclosed in note 49 to the financial statements, material water losses of R10 592 165 (2023: R6 670 895) were incurred due to defective meters, losses on the water network (breakage in pipelines and pumps, leaking valves), evaporation, theft, vandalism and damages as a result of blind excavations.

### **Unauthorised expenditure**

14. As disclosed in note 46 to the financial statements, unauthorised expenditure of R127 030 901 (2023: R72 133 854) was incurred, due to overspending of the budget and some conditional grants were not spent for its intended purposes.

### **Fruitless and wasteful expenditure**

15. As disclosed in note 47 to the financial statements, fruitless and wasteful expenditure of R21 556 473 (2023: R15 582 902) was incurred, due to interest charged on late payments to suppliers.

### **Irregular expenditure**

16. As disclosed in note 48 to the financial statements, irregular expenditure of R2 000 468 (2023: R10 646 508) was incurred, as adequate competitive bidding processes were not followed.

## Other matters

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

### Unaudited disclosure notes

18. In terms of section 125(2)(e) of the MFMA, the particulars of non-compliance with the MFMA should be disclosed in the financial statements. The disclosure requirements 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

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.

## Responsibilities of the auditor-general 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 annual performance report

23. In accordance with the Public Audit Act 25 of 2004 (PAA) and the general notice issued in terms thereof, I must audit and report on the usefulness and reliability of the reported performance information against predetermined objectives for the selected material performance indicators presented in the annual performance report. The accounting officer is responsible for the preparation of the annual performance report.
24. I selected the following material performance indicators related to basic services and infrastructure development presented in the annual performance report for the year ended 30 June 2024. I selected those indicators that measure the municipality's performance on its primary mandated functions and that are of significant national, community or public interest.

- Number of Constructed sewer reticulation and house connection for 118 houses, toilet's structure and outfall sewer in Zamani by 30 June 2024.
- Number of KM roads and storm Water constructed in Memel/Zamani by 30 June 2024
- Number of KM roads and storm Water constructed in Vrede/ Thembalihle by 30 June 2024
- Number of KM roads and storm Water constructed in Warden/Ezenzeleni by 30 June 2024.
- Number of Outfall Sewer refurbished by 30 June 2024
- Number of Outfall Sewer refurbished by 30 June 2024
- Number of water Reticulation network for 250 erven Phase2 (Ext1)
- Number of sewer Reticulation network for 250 erven Phase2 (Ext1)
- Installation of Warden 11Kv Bulk line Warden/Ezenzeleni by June 2024
- Number of outfall sewer line and revamping of pump station 3 and Upgrading of WWTW in Warden/ Ezenzeleni
- Number of Warden/Ezenzeleni Upgrading of sports facility Phase 5 by 30 June 2024.
- Number of Electrification of 176 houses in Memel
- Number of households with access to Water by June 2024
- Number of households with access to sanitation by June 2024
- Number of households with access to refuse removal by June 2024
- Number of households with access to Electricity by June 2024
- Percentage of Electricity distribution losses minimized by June 2024
- Percentage of minimization of water losses by June 2024

25. I evaluated the reported performance information for the selected material performance indicators against the criteria developed from the performance management and reporting framework, as defined in the general notice. When an annual performance report is prepared using these criteria, it provides useful and reliable information and insights to users on the municipality's planning and delivery on its mandate and objectives.

26. I performed procedures to test whether:

- the indicators used for planning and reporting on performance can be linked directly to the municipality's mandate and the achievement of its planned objectives

- all the indicators relevant for measuring the municipality's performance against its primary mandated and prioritised functions and planned objectives are included
- the indicators are well defined to ensure that they are easy to understand and can be applied consistently, as well as verifiable so that I can confirm the methods and processes to be used for measuring achievements
- the targets can be linked directly to the achievement of the indicators and are specific, time bound and measurable to ensure that it is easy to understand what should be delivered and by when, the required level of performance as well as how performance will be evaluated
- the indicators and targets reported on in the annual performance report are the same as those committed to in the approved initial or revised planning documents
- the reported performance information presented in the annual performance report in the prescribed manner
- there is adequate supporting evidence for the achievements reported and for the measures taken to improve performance.

27. I performed the procedures to report material findings only; and not to express an assurance opinion or conclusion.

28. I did not identify any material findings on the reported performance information for the selected indicators.

### **Other matters**

29. I draw attention to the matters below.

#### **Achievement of planned targets**

30. The annual performance report includes information on reported achievements against planned targets and provides measures taken to improve performance.

#### **Material misstatements**

31. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information for basic services and infrastructure development. Management subsequently corrected all the misstatements, and I did not include any material findings in this report.

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| <b>Report on compliance with legislation</b> |
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32. In accordance with the PAA and the general notice issued in terms thereof, I must audit and report on compliance with applicable legislation relating to financial matters, financial management and other related matters. The accounting officer is responsible for the municipality's compliance with legislation.

33. I performed procedures to test compliance with selected requirements in key legislation in accordance with the findings engagement methodology of the Auditor-General of South Africa (AGSA). This engagement is not an assurance engagement. Accordingly, I do not express an assurance opinion or conclusion.
34. Through an established AGSA process, I selected requirements in key legislation for compliance testing that are relevant to the financial and performance management of the municipality, clear to allow consistent measurement and evaluation, while also sufficiently detailed and readily available to report in an understandable manner. The selected legislative requirements are included in the annexure to this auditor's report.
35. The material findings on compliance with the selected legislative requirements, presented per compliance theme, are as follows:

#### **Annual financial statements**

36. The financial statements submitted for auditing were not fully prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of non-current assets, liabilities and disclosure items identified by the auditors in the submitted financial statement were subsequently corrected and the supporting records were provided subsequently, resulting in the financial statements receiving an unqualified audit opinion.

#### **Procurement and contract management**

37. 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.
38. Sufficient appropriate audit evidence could not be obtained that the preference point system was applied in all procurement of goods and services as required by section 2(1)(a) of the Preferential Procurement Policy Framework Act.

#### **Consequence management**

39. 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.
40. Irregular expenditure incurred by the municipality were not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.
41. 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.

#### **Expenditure management**

42. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
43. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R120 030 901 as disclosed in note 48 to the annual 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 and some conditional grants were not used for its intended purposes.

44. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R21 556 473, as disclosed in note 49 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by interest and penalties charged due to late payments to the suppliers.
45. Reasonable steps were not taken to prevent irregular expenditure amounting to R2 639 486, as disclosed in note 50 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 legislation during the bidding processes followed.

### **Conditional grants**

46. Performance in respect of programmes funded by the municipal infrastructure grant, extended public works programme grant, financial management grant and 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.

### **Strategic planning and performance**

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

### **Other information in the annual report**

48. The accounting officer is responsible for the other information included in the annual report. The other information referred to does not include the financial statements, the auditor's report and those selected material indicators presented in the annual performance report that have been specifically reported on in this auditor's report.
49. My opinion on the financial statements, the report on the audit of the annual performance report and the report on compliance with legislation do not cover the other information included in the annual report and I do not express an audit opinion or any form of assurance conclusion on it.
50. My responsibility is to read this other information and, in doing so, consider whether it is materially inconsistent with the financial statements and the selected material indicators 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, annual performance report and compliance with applicable legislation; however, my objective was not to express any form of assurance on it.
53. The matters reported below are limited to the significant internal control deficiencies that resulted in opinion, and the material findings on compliance with legislation included in this report.
54. The accounting officer and municipal council did not effectively oversee financial and performance reporting and compliance as well as related internal controls which resulted in the numerous misstatements.
55. The accounting officer and municipal council did not adequately monitor the action plan to address prior year findings resulting in recurring material misstatements and material non-compliance.
56. Management and the accounting officer did not adequately review and monitor compliance with applicable legislations which resulted in material non-compliance findings.
57. Management did not implement adequate controls over the daily and monthly processing and reconciling of transactions and as a result there were material misstatements in the annual financial statements and annual performance report.
58. Leadership did not implement effective human resource management to ensure that adequate and sufficiently skilled resources are in place and that performance is monitored, as a result repetitive material findings were identified without sufficient consequences.

Bloemfontein

30 November 2024



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*

## Annexure to the auditor's report

The annexure includes the following:

- The auditor-general's responsibility for the audit
- The selected legislative requirements for compliance testing

### Auditor-general's responsibility for the audit

#### Professional judgement and professional scepticism

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 material performance indicators and on the municipality's compliance with selected requirements in key legislation.

#### Financial statements

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
- conclude on the appropriateness of the 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 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

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.

I also provide the accounting officer with a statement that I have complied with relevant ethical requirements regarding independence and communicate with them all relationships and other matters that may reasonably be thought to bear on my independence and, where applicable, actions taken to eliminate threats or safeguards applied.

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## Compliance with legislation – selected legislative requirements

The selected legislative requirements are as follows:

| Legislation   | Sections or regulations   |
|---|---|
| [Act title and reference]   | [References to all selected requirements from this act or regulation]   |
| Municipal Finance Management Act 56 of 2003   | <p>Sections: 1, 11(1), 13(2), 14(1), 14(2)(a), 14(2)(b), 15, 24(2)(c)(iv), 28(1), 29(1), 29(2)(b), 32(2), 32(2)(a), 32(2)(a)(i), 32(2)(a)(ii),</p> <p>Sections: 32(2)(b), 32(6)(a), 32(7), 53(1)(c)(ii), 54(1)(c), 62(1)(d), 63(2)(a), 63(2)(c), 64(2)(b), 64(2)(c), 64(2)(e), 64(2)(f),</p> <p>Sections: 64(2)(g), 65(2)(a), 65(2)(b), 65(2)(e), 72(1)(a)(ii), 112(1)(j), 116(2)(b), 116(2)(c)(ii), 117, 122(1), 122(2), 126(1)(a),</p> <p>Sections: 126(1)(b), 127(2), 127(5)(a)(i), 127(5)(a)(ii), 129(1), 129(3), 133(1)(a), 133(1)(c)(i), 133(1)(c)(ii), 170, 171(4)(a), 171(4)(b)</p> |
| MFMA: Municipal budget and reporting regulations, 2009  | Regulations: 71(1)(a), 71(1)(a)(b), 71(2)(a), 71(2)(b), 71(2)(d), 72(a), 72(b), 72(c)   |
| MFMA: Municipal Investment Regulations, 2005  | Regulations: 3(1)(a), 3(3), 6, 7, 12(2), 12(3)  |
| MFMA: Municipal Regulations on financial Misconduct Procedures and Criminal Proceedings, 2014 | Regulations: 5(4), 6(8)(a), 6(8)(b), 10(1)  |
| MFMA: Municipal Supply Chain Management Regulations, 2017                                     | <p>Regulations: 5, 12(1)(c), 12(3), 13(b), 13(c), 16(a), 17(1)(a), 17(1)(b), 17(1)(c), 19(a), 21(b), 22(1)(b)(i), 22(2), 27(2)(a), 27(2)(e),</p> <p>Regulations: 28(1)(a)(i), 29(1)(a), 29(1)(b), 29(5)(a)(ii), 29(5)(b)(ii), 32, 36(1), 36(1)(a), 38(1)(c), 38(1)(d)(ii), 38(1)(e), 38(1)(g)(i),</p> <p>Regulations: 38(1)(g)(ii), 38(1)(g)(iii), 43, 44, 46(2)(e), 46(2)(f)</p>   |
| Construction Industry Development Board Act 38 of 2000  | Section: 18(1)  |
| Construction Industry Development Board Regulations, 2004                                     | Regulations: 17, 25(7A)   |
| Division of Revenue Act   | Sections: 11(6)(b), 12(5), 16(1); 16(3)   |
| Municipal Property Rates Act 6 of 2004  | Section: 3(1)   |
| Municipal Systems Act 32 of 2000  | <p>Sections: 25(1), 26(a), 26(c), 26(h), 26(i), 29(1)(b)(ii), 34(a), 34(b), 38(a), 41(1)(a), 41(1)(b), 41(1)(c)(ii), 42, 43(2),</p> <p>Sections: 54A(1)(a), 56(1)(a), 57(2)(a), 57(6)(a), 66(1)(a), 66(1)(b), 67(1)(d), 74(1), 96(b)</p> <p>Parent municipality with ME:<br/>Sections: 93B(a), 93B(b)</p>   |

| Legislation   | Sections or regulations   |
|---|---|
|   | Parent municipality with shared control of ME:<br>Section: 93C(a)(iv), 93C(a)(v)  |
| MSA: Disciplinary Regulations for Senior Managers, 2011   | Regulations: 5(2), 5(3), 5(6), 8(4)   |
| MSA: Municipal Planning and Performance Management Regulations, 2001  | Regulations: 2(1)(e), 2(3)(a), 3(3), 3(4)(b), 7(1), 8, 9(1)(a), 10(a), 12(1), 15(1)(a)(i), 15(1)(a)(ii)   |
| MSA: Municipal Performance Regulations for Municipal Managers and Managers Directly Accountable to Municipal Managers, 2006 | Regulations: 2(3)(a), 4(4)(b), 8(1), 8(2), 8(3)   |
| MSA: Regulations on Appointment and Conditions of Employment of Senior Managers, 2014                                       | Regulations: 17(2), 36(1)(a)  |
| MSA: Municipal Staff Regulations  | Regulations: 7(1),31  |
| Prevention and Combating of Corrupt Activities Act 12 of 2004   | Section: 34(1)  |
| Preferential Procurement Policy Framework Act 5 of 2000   | Sections: 2(1)(a), 2(1)(f)  |
| Preferential Procurement Regulations, 2017  | Regulations: 4(1), 4(2), 5(1), 5(3), 5(6), 5(7), 6(1), 6(2), 6(3), 6(6), 6(8), 7(1), 7(2), 7(3), 7(6), 7(8), 8(2), 8(5), 9(1), 10(1), 10(2),<br>Regulations: 11(1), 11(2) |
| Preferential Procurement Regulations, 2022  | Regulations: 4(1), 4(2), 4(3), 4(4), 5(1), 5(2), 5(3), 5(4)   |