

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

## Report on the audit of the financial statements

### Qualified opinion

1. I have audited the financial statements of the Metsimaholo Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2022, 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 the 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 this auditor's report, the financial statements present fairly, in all material respects, the financial position of the Metsimaholo Local Municipality as at 30 June 2022, and its financial performance and cash flows for the year then ended in accordance with the 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 qualified opinion

#### Property, plant and equipment

3. The municipality did not correctly classify infrastructure assets in accordance with GRAP 17, *Property, plant and equipment*, as infrastructure assets were incorrectly classified as information technology (IT) equipment. Consequently, infrastructure assets was understated by R18 939 200 and IT equipment was overstated by the same amount. In addition, I was unable to obtain sufficient appropriate audit evidence that property, plant and equipment had been properly accounted for, due to the status of the accounting records. I was unable to confirm the property, plant and equipment by alternative means. Consequently, I was unable to determine whether any further adjustment was necessary to property, plant and equipment, stated at R1 319 635 770 (2021: R1 231 528 168) in note 7 to the financial statements...

#### Investment property

4. The municipality did not account for investment property in accordance with GRAP 16, *Investment property*. The municipality accounted for land and buildings over which it has, in substance, lost control, resulting in investment property being overstated by R14 793 167. In addition, I was unable to obtain sufficient appropriate audit evidence that investment property had been properly accounted for, due to the status of the accounting records. I was unable to confirm the investment property by alternative means.

Consequently, I was unable to determine whether any further adjustment was necessary to investment property, stated at R242 260 298 (2021: R240 181 961) in note 9 to the financial statements. This also has an impact on the surplus for the period and on the accumulated surplus.

### Service charges

5. The municipality did not recognise service charges from exchange transactions, as required by GRAP 9, *Revenue from exchange transactions*. Consumers were identified that were incorrectly classified as indigent and service charges were levied against accounts registered in the name of the municipality. Consequently, service charges and receivables from exchange transactions were each understated by R23 954 904 (2021: R19 187 908).

### Impairment losses

6. The municipality did not calculate the provision for impairment of its debtors in accordance with GRAP 104, *Financial Instruments*. The municipality did not apply the correct assumptions and rates for debtors due to the incorrect assessment of the credit risk for a group of debtors. Consequently, impairment losses disclosed in note 32 to the financial statements is understated by R41 557 752 and receivables from non - exchange transactions is overstated by the same amount. Additionally, there was an impact on the surplus for the period and on the accumulated surplus.

### Irregular expenditure

7. The municipality did not disclose all instances of irregular expenditure incurred in the notes to the financial statements as required by section 125(2)(d)(i) of the MFMA. The municipality made payments in contravention of supply chain management (SCM) requirements which were not disclosed. I was unable to determine the full extent of the understatement of irregular expenditure, stated at R649 234 975 (2021: R480 723 536) in note 45.3 to the financial statements, as it was impracticable to do so.

### Context for the opinion

8. 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 financial statements section of my report.
9. 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.
10. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

## **Emphasis of matters**

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

### **Restatement of corresponding figures**

12. As disclosed in note 42 to the financial statements, the corresponding figures for 30 June 2021 were restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2022.

### **Material uncertainty relating to claims against the municipality**

13. With reference to note 50 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 provided for in the financial statements.

### **Unauthorised expenditure**

14. As disclosed in note 45.1 to the financial statements, the municipality incurred unauthorised expenditure of R25 418 564 (2021: R19 051 380) , due to overspending of the budget

### **Material losses**

15. As disclosed in note 46.1.8 to the financial statements, the municipality incurred material water distribution losses of R15 750 944 (2021: R65 888 545) and material electricity distribution losses of R55 498 644 (2021: R48 296 420), mainly due to illegal connections, leakages, burst water pipes, line losses, tampering and theft.

## **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 on it.

### **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 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 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 2022:

KPA	Pages in the annual performance report
KPA 1 – service delivery and infrastructure development	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 – service delivery and infrastructure development**

##### **Refuse removal service extended to all new formal settlements as per township register within Metsimaholo LM (2 614 hhs in Themba Kubeka)**

28. The planned indicator and target was 2 614 households (refuse removal service extended to Themba Kubeka), but the reported achievement referred to was 50% (target not achieved). In addition, I was unable to obtain sufficient appropriate audit evidence for the achievement of 50% reported against target 2 614 households in the annual performance report due to the lack of accurate and complete records. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement.

##### **Number of illegal dumping sites removed**

29. The achievement of 12 (dumping sites removed) was reported against target 12 (dumping sites removed) in the annual performance report. However, some supporting evidence provided materially differed from the reported achievement, while in other instances I was unable to obtain sufficient appropriate audit evidence. This was due to the lack of accurate and complete records. I was unable to further confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any further adjustments were required to the reported achievement.

## **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 28 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 – service delivery and infrastructure development. 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 current and non-current assets, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements and the supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

### **Procurement and contract management**

36. 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.
37. I could not obtain sufficient appropriate audit evidence that contracts were awarded to bidders in an economical manner and prices for the goods or services were reasonable, as required by section 62(1)(a) of the MFMA.

38. Some of the contracts and quotations were awarded to bidders based on preference points that were not allocated and calculated in accordance with the requirements of section 2(1)(a) of the Preferential Procurement Policy Framework Act 5 of 2000 and its regulations.
39. Some of the invitations 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 2017 preferential procurement regulation 8(2).
40. 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.
41. 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.
42. Awards were made to providers who were in the service of other state institutions or whose directors were in the service of other state institutions, in contravention of section 112(1)(j) of the MFMA and SCM regulation 44. Similar awards were identified in the previous year and no effective steps were taken to prevent or combat the abuse of the SCM process, as required by SCM regulation 38(1).

#### **Expenditure management**

43. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R25 418 564, as disclosed in note 45.1 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 by technical department.
44. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The expenditure disclosed does not reflect the full extent of the irregular expenditure incurred, as indicated in the basis for qualification opinion paragraph.
45. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R1 050 514, as disclosed in note 45.2 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 charges due to the late payment of outstanding balances.

#### **Utilisation of conditional grants**

46. The municipal infrastructure grant was not spent for its intended purposes in accordance with the applicable grant framework, as required by section 16(1) of Dora.
47. The water services infrastructure grant was not spent for its intended purposes in accordance with the applicable grant framework, as required by section 16(1) of Dora.
48. 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 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.
51. 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.

### **Strategic planning and performance management**

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

### **Revenue management**

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

### **Asset management**

54. 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.
55. Capital assets were disposed of 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.

### **Human resource management**

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

## Other information

57. 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.
58. 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.
59. 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.
60. 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

61. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.
62. The positions of managers reporting directly to the municipal manager have been vacant for a very long period. This has resulted in various officials acting in these positions, contributing to the instability in the leadership of the municipality.
63. The implementation of the corrective measures included in the audit action plan were inadequate and not effectively monitored to ensure that the weaknesses relating to the financial, performance and supply chain management were addressed.
64. Management did not implement proper record keeping to ensure that complete and accurate information was available to support financial and performance reporting.
65. Management's lack of detailed review of the financial statements and the underlying records resulted in material misstatements that were not detected by the municipality's internal processes.

## Material irregularities

66. In accordance with the PAA and the Material Irregularity Regulations, I have a responsibility to report on material irregularities identified during the audit.

### Material irregularities in progress

67. I identified material irregularities during the audit and notified the accounting officer, as required by material irregularity regulation 3(2). By the date of this auditor's report, the response of the accounting officer was not yet due. These material irregularities will be included in the next year's auditor's report.

AUDITOR - GENERAL

Bloemfontein

30 November 2022



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*

## **Annexure – Auditor-general’s responsibility for the audit**

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements and the procedures performed on reported performance information for the 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 Metsimaholo 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 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.