Report of the auditor-general to the Mpumalanga Provincial Legislature and the council on the Lekwa Local Municipality

Report on the audit of the financial statements

Disclaimer of opinion

1. I was engaged to audit the financial statements of the Lekwa Local Municipality set out on pages x to x, 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. I do not express an opinion on the financial statements of the municipality. Because of the significance of the matters described in the basis for disclaimer of opinion section of this auditor's report, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

Basis for disclaimer of opinion

Cash and cash equivalents

3. I was unable to obtain sufficient appropriate audit evidence for bank balances, due to the inadequate status of the accounting records. The municipality did not have adequate systems of internal control for reconciling all bank transactions and could not provide reconciliations between the bank accounts and the accounting records. I could not confirm bank balances by alternative means. The cash and cash equivalents included in risk management in note 42 to the financial statements also included this amount.

4. Consequently, I was unable to determine whether any adjustment was necessary to the cash and cash equivalents of R15,49 million (2020-21: R26,99 million) and risk management as disclosed in note 3 and 42 respectively to the financial statements. Since the cash and cash equivalents balance is included in the determination of net cash flows from operating and investing activities reported in the statement of cash flows. I was unable to determine whether any adjustments were necessary in the cash flows from operating activities stated at R33,03 million (2020-21: R37,45) million and investing activities stated at R44,54 (2020-21: R53,56) in the financial statements.

Payables from exchange transactions - accrued expense

5. The municipality did not recognise all invoices relating to one of their accounts with the Department of Water and Sanitation (DWS) for bulk water purchases in accordance with GRAP 1, *Presentation of financial statements* in the current and prior years. Consequently, payables from exchange transactions – accrued expense was understated by R646,78 million (2020-21: R557,43 million), VAT receivables was understated by R84,36 million (2020-21: R72,71 million) and bulk purchases - water was understated by R77,70 million (2020-21:

R70,21 million). Consequently ,the water losses stated at R212,41 million (2020-21: R77, 97- million is misstated. Additionally, there was an impact on the deficit for the period under review and on the accumulated deficit.

6. The municipality did not accurately record accrued expenses in the financial statements, as required by *GRAP 1, Presentation of financial statements*. Consequently, trade and other payables – accrued expenses was overstated by R49,93 million (2020-21:R49,93 million overstated) additionally, there was an impact on the deficit for the period under review and on the accumulated deficit.

Provisions - Department of water and sanitation

7. The municipality reversed amounts relating to one of the DWS account in the prior year, in contravention of *Grap 19, Provisions,contingent liabilities and contingent asset.* This resulted in provisions being understated by R157,42m (2020-21: R157,42m). Additionally, there was an impact on the deficit for the period under review and on the accumulated deficit.

8. Furthermore, the municipality did not recognise all interest charged on outstanding invoices received from DWS for bulk water purchases in accordance with GRAP 1, *Presentation of financial statements* for current and prior year. I could not determine the full extent of the understatement of provisions - department of water and sanitation and finance costs respectively for current and prior years as it was impracticable to do so. Additionally, there was an impact on the deficit for the period under review and on the accumulated deficit.

Contracted services

9. The municipality did not recognise some expenditures in accordance with GRAP 1, *Presentation of financial statements* .Some of the invoices of contracted services relating to services that were received in the prior year were recorded as the current financial year's transactions, resulting in expenditure and payables from exchange transactions being overstated by R38 million (2020-21: R38 million understated) . This also had an impact on the surplus for the period under review and on the accumulated surplus.

Net cash flows from operating and investing activities

10. The municipality did not correctly prepare and disclose the net cash flows from operating and investing activities, as required by GRAP 2, *Cash flow statements*. This was due to multiple errors in determining cash flows from operating and investing activities. I was unable to determine the full extent of the errors in the net cash flows from operating and investing activities as it was impracticable to do so.

11. Consequently, I was unable to determine whether any adjustments were necessary to cash flows from operating and investing activities, stated at R33,04 million (2020-21: 37,45 million) and R44,54 million (2020-21: R53,56 million):, respectively, in the financial statements.

Segment Information

12. The municipality did not accurately disclose segment reporting in the financial statements, as required by *GRAP 18, Segment reporting* for current and prior year. The segment information disclosed for expenditure in the current year and assets in the prior year did not reconcile back to the GRAP amounts disclosed in the financial statements. Consequently, segment information was misstated by R67,90 million (2020-21: R216, 33million).

Unauthorised expenditure

13. The municipality did not spend the municipal infrastructure grant for its intended purposes in accordance with the applicable grant framework, as required by section 16(1) of the Division of Revenue Act of 2021 (Dora). However, the amount was not disclosed. Consequently, unauthorised expenditure was understated by R30,77 million.

Irregular expenditure

14. The municipality did not accurately record irregular expenditure in the financial statements, as required by section 125(2)(d) of the Municipal Financial Management Act 56 of 2003 (MFMA). The current year's opening balance was also misstated due to error on adjustment made to prior period balance which was overstated by R169, 31 million.

15. Furthermore, the municipality did not recognise all instance of irregular expenditure to the financial statements, as required by section 125(2)(d) of the Municipal Financial Management Act 56 of 2003 (MFMA). This was due to non-investigation of instances of prior year irregular expenditure. I was unable to determine the full extent of the understatement of irregular expenditure stated at R 703,56 million (2020-21: R 673,19 million) in note 47 to the financial statements, as it was impracticable to do so.

Fruitless and wasteful expenditure

16. The municipality did not recognise fruitless and wasteful expenditure, as required by section 125(2) (d) of the Municipal Financial Management Act 56 of 2003 (MFMA). The penalties and interest for late submission of returns to the South African Revenue Service (SARS) including interest on DWS invoices were not all recorded in the fruitless and wasteful expenditure register. I was unable to determine the full extent of the understatement of fruitless and wasteful expenditure stated at R566,35 million as disclosed in note 46 to the financial statements.

Contingencies

17. The municipality disclosed a possible contingent liability in contravention of *Grap 19, Provisions,contingent liabilities and contingent asset* for the prior and current year. The disclosure note 39 included the case between the municipality and DWS for possible contingent liability, however the municipality failed to lodge a formal dispute to support the possible contingent liability.Consequently, contingencies disclosure was misstated by R 646,78 million (2020-21: R 557,43 million).

Prior year adjustments

18. The municipality did not accurately disclose the restatements of corresponding amounts for payables from exchange transaction, provisions, bulk purchases, contracted services, fruitless and wasteful expenditure and irregular expenditure in contravention of *Grap 3,Accounting policies, changes in accounting estimates and errors*. I was unable to determine the full extent of the misstatement to these affected financial statement line items in the prior year adjustments as it was impracticable to do so.

19. Furthermore, I was unable to obtain sufficient appropriate audit evidence for the restatements of corresponding amounts for cash and cash equivalents in the financial statements. As disclosed in note 41 to the financial statements, the restatement was made to rectify a previous year misstatement but it could not be substantiated by supporting audit evidence. I was unable to confirm this restatement by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to the prior year adjustments note in the financial statements.

Material uncertainty relating to going concern

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

21. I draw attention to note 43 in the financial statements, which indicates that the municipality incurred an accumulated deficit of R921,09 m.illion during the year ended 30 June 2022, as of that date, the municipality's liabilities exceeded its assets by R921,09 million. The municipality plans to address the cash flow shortages through enhanced revenue collection and a resultant consistency in the payment of creditors, when they become due.

Emphasis of matters

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

Material impairments – trade receivables

23. As disclosed in note 6 to the financial statements, material impairment of trade receivable from non-exchange transactions of R360,73 million (2020:21: R287,85 million) was incurred as a result of an impairment provision for doubtful debts.

24. As disclosed in note 7 to the financial statements, material impairment of trade receivables from exchange transactions of R1,12 billion (2020:21: R961,47 million) was incurred as a result of an impairment provision for doubtful debts.

Material losses – electricity

25. As disclosed in note 35 to the financial statements, material electricity losses of R158,26 million (2020:21: R124,40 million) was incurred.

Other matters

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

Unaudited disclosure notes (MFMA 125)

27. 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, we do not express an opinion on it.

Withdrawal from the audit engagement

28. Due to the limitation imposed on the scope of the audit by management, we have disclaimed our opinion on the financial statements. However, for the legislated requirement to perform the audit of municipality, we would have withdrawn from the engagement in terms of the International Standards of Auditing (ISAs).

Responsibilities of the accounting officer for the financial statements

29. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the Standards of Generally Recognised Accounting Practise (GRAP) , the requirements of the Municipal Finance Management Act 56 of 2003 (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.

30. 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

31. My responsibility is to conduct an audit of the financial statements in accordance with the International Standards on Auditing (ISAs) and to issue an auditor's report. However, because of the matters described in the basis for disclaimer of opinion section of this auditor's report, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

32. 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 the other ethical requirements that relevant to my audit of the financial statements in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.

Report on the audit of the annual performance report

Introduction and scope

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

34. 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 key performance area presented in the municipality's annual performance report for the year ended 30 June 2022:

Key performance area (KPA)	Pages in the annual performance report
KPA 1 – Service delivery and infrastructure development	**x – x**

35. 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.

36. The material findings on the usefulness and reliability of the performance information of the selected key performance areas are as follows:

Indicators (KPI 20): Number of electricity meters inspected and audited

37. The reported target of 1 026 electricity meters inspected and audited by 2022-06-30 did not agree with the planned target of 600 electricity meters inspected and audited by 2022-06-30 as per the approved in the service delivery budget implementation plan (SDBIP). The changes were made without the necessary approval.

Indicators (KPI 27): % of households with weekly access to refuse removal service provided

38. The planned indicator and target were 100% of households with access to weekly refuse removal service provided (30 518), but the reported achievement referred to was 4.

Various indicators

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

KPI no.	Indicator description (KPIs)	Reported achievement per report/ register/list	Reported achievement per APR
KPI 1	% Completion of design for sewer treatment works upgrade	0%	100%
KPI 8	km of gravel road upgraded	0.42 km	0.7 km
KPI 19	km of sewer line installed	0 km	0.5 km

Various indicators

40. 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 indicator is well-defined and verifiable by alternative means. As a result, I was unable to audit the reliability of the achievements reported in the annual performance report of the listed indicators.

KPI no.	Indicator description	Planned targets per APR	Reported actual achievement per APR
KPI 01	% completion of design for sewer treatment works upgrade	100% completed design for sewer treatment plan upgrade	100% design for upgrade of sewer treatment works
KPI 16	% completion of fencing of Rooikoppen cemetery	100% completion of fencing of Rooikoppen cemetery	100% Rooikoppen cemetery fenced
KPI 19	Km of sewer line installed	0.5km sewer line installed	0.5km sewer line installed in Q3
KPI 22	Number of old water meters replaced	80 water meters replaced	88 water meters replaced
KPI 25	Square meters of potholes patched	2000m² of potholes patched	15200m² of potholes patched
KPI 27	% of households with weekly access to refuse removal service provided	100% of households with access to weekly refuse removal service provided (30518)	4

Various indicators

41. There was no clear and logical link on how the indicators listed below will contribute to achieving the planned outcome or will measure the actual service delivery and the planned output to which they relate:

- KPI 27: % of households with weekly access to refuse removal service provided – reported achievement was four (4).

- KPI 28: Number of reports on businesses with access to refuse removal at least once a week reported achievement was 4 reports.

Other matters

42. We draw attention to the matters below. Our conclusion is not modified in respect of these matters.

Achievement of planned targets

43. Refer to the annual performance report on pages x to x 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 paragraph 37 to 41 of this report.

Adjustment of material misstatements

44. We identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on 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

45. 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.

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

Annual financial statements, annual performance report and annual report

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

Expenditure management

48. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1) (d) of the MFMA. The full extent of the irregular expenditure could not be quantified as indicated in the basis for qualification paragraph. The majority of the disclosed irregular expenditure was caused by none-compliance with SCM Reg 19(a) – appointment of service providers without following competitive bidding processes.

49. Reasonable steps were not taken to prevent fruitless and wasteful expenditure, as required by section 62(1) (d) of the MFMA. The expenditure disclosed does not reflect the full extent of the fruitless and wasteful expenditure incurred as indicated in the basis for qualification paragraph. The majority of the disclosed fruitless and wasteful expenditure was caused by interest incurred on late payments to Eskom account and interest and penalties due to late submission and payment of VAT and PAYE returns.

50. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R 233,47 million, as disclosed in note 45 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 within various votes.

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

Strategic management, planning and performance management

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

Conditional Grants

53. 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.

Procurement and contract management

54. 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). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM Regulation 36(1).

55. Some of the contracts were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM Regulation 13(c).

56. Some of the quotations were accepted from bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM Regulation 13(c). Similar non-compliance was also reported in the prior year.

57. Some of the invitations for competitive bidding were not advertised for a required minimum period of days, in contravention of SCM Regulation 22(1) and 22(2).

58. The invitation to tender for procurement of commodities designated for local content and production, did not stipulated 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. Similar non-compliance was also reported in the prior year.

59. 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.

Consequence management

60. 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.

61. 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.

62. 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.

Internal control deficiencies

63. 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 disclaimer of opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

64. Leadership did not exercise oversight responsibility regarding financial and performance reporting and compliance and related internal controls.

65. Management did not ensure that controls were implemented over daily and monthly processing and reconciling of transactions.

66. Management did not prepare regular, accurate and complete financial and performance reports that were supported and evidenced by reliable information.

67. Management did not review and monitor compliance with applicable laws and regulations.

Material irregularities

68. 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.

69. The material irregularities identified are as follows:

Material irregularities in progress

70. I identified other material irregularities during the audit and notified the accounting officer of these, as required by material irregularity regulation 3(2). By the date of this auditor's report, I had not yet completed the process of evaluating the responses from the accounting officer .These material irregularities will be included in the next year's auditor's report.

Status of previously reported material irregularities

Full and proper records not kept

71. Reasonable steps were not taken in the 2019-20 financial year to ensure that full and proper records were kept of infrastructure assets, consumer debtors, service charges, payables, accruals and commitments, as required by section 62(1) (b) of the MFMA.

72. The non-compliance contributed to a disclaimed audit opinion as I could not obtain sufficient appropriate audit evidence to support the amounts and disclosures in the financial statements.

73. The lack of full and proper records is likely to result in substantial harm to the municipality as it contributed to the material uncertainty regarding its ability to continue operations, as disclosed in note 41 to the 2019-20 financial statements. This, in turn, is likely to have a negative impact on the municipality's ability to discharge its service delivery mandate.

74. The accounting officer was notified of the material irregularity on 11 June 2021 and invited to make a written submission on the actions taken and that will be taken to address the matter.

75. The accounting officer responded to the notification on 17 November 2021 and the accounting officer indicated that a financial recovery plan is currently being implemented, and is being monitored by accounting officer and stakeholders with the aim of improving the financial sustainability.

76. The financial recovery plan included the following action amount others to resolve the material irregularity by 30 September 2022.

- Development of audit action plan to resolve the internal control deficiencies
- Perform full asset verification and update the fixed assets register
- Implement revenue enhancement plan which includes the valuation roll reconciliation

- Implement proper record management.

77. I am in the process of evaluating the implementation of the actions included in the financial recovery plan.

Other reports

78. 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.

79. An independent consultant investigated allegations of possible maladministration at the municipality, at the request of the member of the executive council for cooperative governance and traditional affairs, in terms of section 106(1) (B) of the Municipal Systems Act 32 of 2000. The investigation was concluded and the recommendations of the investigation had been partially implemented at the time of this report.

AUDITOR- GENERAL

Mbombela

15 December 2022

AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence