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

Qualified opinion

1. I have audited the financial statements of the Lekwa Local Municipality set out on pages .. to.., which comprise the statement of financial position as at 30 June 2023, statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actuals 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 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 Lekwa Local Municipality as at 30 June 2023, and financial performance and cash flows for the year then ended in accordance with the Standards of Generally Recognised Accounting Practise (GRAP) , the requirements of the Municipal Finance Management Act 56 of 2003 (MFMA) the Division of Revenue Act 5 of 2022 (Dora).

Basis for qualified opinion

Irregular expenditure

3. The municipality did not have adequate systems to identify and disclose all irregular expenditure incurred during the year, as required by section 125(2)(d) of the MFMA. I was unable to quantify the understatement, as it was impracticable to do so. Consequently, I was unable to determine whether any adjustments were necessary to irregular expenditure stated at R178,46 milion (2021-22: R618,81 million), disclosed in note 47 to the financial statements as well as the adjustments made to irregular expenditure in the prior period errors disclosure in note 41 to the financial statements.

Property, plant and equipment

4. The municipality did not appropriately account for changes in useful lives for some of the property, plant and equipment in accordance with GRAP 17, *Property, plant and equipment*. Changes in remaining useful lives of the assets that were incorrectly accounted as an error instead of change in accounting estimates. Consequently, the opening balance of the property, plant and equipment was understated by R26,86 million and the opening balance of accumulated depreciation was overstated by the same amount.

Cash flow statement

Interest received bank and other financial assets

5. The municipality's cash received from interest received on bank account and other financial assets in the cash flow statement was incorrectly calculated as it did not include the other financial assets which constitute a departure from GRAP 2, *Cash flow statement*. Consequently, the interest received on bank accounts and other financial assets is understated by R105,52 million in the cash flow statements.

Suppliers

6. The municipality's cash paid to suppliers was incorrectly calculated as it included unallocated deposits, income received in advance and retention which constitute a departure from GRAP 2, Cash flow statement. Consequently, the suppliers is overstated by R38,36 million in the cash flow statement.

Context for opinion

7. I 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.

8. 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.

9. 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

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

11. Note 43 in the financial statements, which indicates that the municipality incurred an deficit of R664,54 million (2021-22: R622,13 million) during the year ended 30 June 2023, as of that date, the municipality's liabilities exceeded its assets by R 664,54 million (622,13 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

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

Material impairments – trade receivables

13. As disclosed in note 6 to the financial statements, material impairment of trade receivable from non-exchange transactions of R419,32 million (2021-22: R360,74 million) was incurred as a result of an impairment provision for doubtful debts.

14. As disclosed in note 7 to the financial statements, material impairment of trade receivables from exchange transactions of R1,29 billion (2021-22: R1,09 billion) was incurred as a result of an impairment provision for doubtful debts.

Material losses – electricity

15. As disclosed in note 35 to the financial statements, material electricity losses of R125,02 million (2021-22: R158,26 million) was incurred.

Material losses – water

16. As disclosed in note 35 to the financial statements, material water losses of R230,58 million (2021-22: R212,41 million) was incurred.

Other matter

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

Unaudited disclosure notes (MFMA 125)

18. 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.

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 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 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 area presented in the annual performance report. The accounting officer is responsible for the preparation of the annual performance report.

24. I selected the following key performance area presented in the annual performance report for the year ended 30 June 2023 for auditing. I selected key performance area that measures the municipality’s performance on its primary mandated functions and that is of significant national, community or public interest.

Key performance area	Page numbers	Purpose
Basic service delivery and infrastructure development 1	XX	Provision of basic services (water 100%, sanitation 100%, electricity 100%, solid waste and roads 100%)

25. I evaluated the reported performance information for the selected key performance area 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
- 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 is presented in the annual performance report in the prescribed manner. provided for any measures taken to improve performance.

27. I performed the procedures for the purpose of reporting material findings only; and not to express an assurance opinion or conclusion.

28. The material findings on the reported performance information for the selected key performance area are as follows:

Basic service delivery and infrastructure

Various indicators

29. The reported achievements below did not relate to the planned key performance indicator and targets. Additionally, I could not determine if the below reported achievements were correct, as there were no processes to consistently measure and report on achievements against planned indicators. Adequate supporting evidence was also not provided for auditing. Consequently, the reported achievement might be more or less than reported and was not reliable for determining if the target had been achieved.

Key performance indicators	Planned targets	Reported actual achievement
% Refurbishment of the Standerton Waste Water Treatment Works	100% Refurbishment of the 9ML Standerton Waste Water Treatment Works	Practical completion
% completion of civil works (phase 1) for the upgrade of A Sub station	50% completion of civil works (phase 1)	Transformer ordered
Electrical: 35 electrical panels connected. Water: Raw water, Kielser and Concor pump units as well as reseviors/pressure towers connected to SCADA.	Electrical: Expansion of SCADA system to include 35 remaining electrical panels to SCADA system. Water: Inclusion of raw water, Kieser and Concor networks to SCADA system.	Request was forwarded to Messrs Goldi, COFCO, Meadowsand Standerton Mills in November 2022, to assist with expansion of SCADA system and other challenges.

Number of streets cleaned on daily basis

30. There was no link between the key performance indicator and target of one (1) report and the achievement of planned objectives and strategic goals, as it did not measure actual service delivery. The key performance indicator and target measured the number of reports prepared instead of the number of streets cleaned on daily basis.

Various indicators

31. I could not determine if the below reported achievements were correct, as there were no processes to consistently measure and report on achievements against planned indicators. Adequate supporting evidence was also not provided for auditing. Consequently, the reported achievement might be more or less than reported and was not reliable for determining if the target had been achieved.

Key performance indicator	Strategic goal	Reported achievement
Number of water meters replaced	Improved access to water, sanitation, electricity and waste removal	221 water meters replaced
Number of boreholes repaired		14 boreholes repaired by 30 June 2023
% Construction of Kieser reservoir and pressure tower		Construction at 25%
Service provider procured for development of water services development (WSD) plan		Service provider not procured for WSD Plan
Number of VIP toilets installed		50 VIP toilets installed
% Construction of Coligny sewer line		100% practical completion
Number of street lights repaired		317 street lights repaired
Number of high mast lights repaired		37 highmast lights repaired
Number of electricity meters inspected and audited		4946 electricity meters inspected and audited
Square meters of road repaired		6252 m² patched
Meters of stormwater cleaned		1792m stormwater drainage maintained
Distance (km) of road rehabilitated		1,9km rehabilitated
0,530km of gravel road upgraded in Sivukile, Morgenzon		0,6km upgraded
% of households with access to refuse removal service		75%
% of businesses with access to refuse removal service		75%

Other matters

32. I draw attention to the matters below.

Achievement of planned targets

33. The annual performance report includes information on reported achievements against planned targets and provides measures taken to improve performance. This information should be considered in the context of the material findings on the reported performance information.

Material misstatements

34. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information of basic service delivery and infrastructure development. As management subsequently corrected 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 compliance with legislation

35. 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.

36. 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.

37. Through an established AGSA process, I selected requirements in key legislation for compliance testing that are relevant to the financial and performance management of themunicipality, 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.

38. The material findings on compliance with the selected legislative requirements, presented per compliance theme, are as follows:

Annual financial statements

39. 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, revenue and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.

Revenue management

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

Expenditure management

41. 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 paragraph. The majority of the disclosed irregular expenditure was caused by non-compliance with supply chain management (SCM) prescripts.

42. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R157,23 million, as disclosed in note 46 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 incurred on late payments to Eskom and DWS accounts and interest and penalties due to late submissions and payments of VAT and PAYE returns.

43. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R242,99 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 on certain votes on the approved budget.

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

Procurement and contract management

45. 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)

Consequence management

46. 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.

47. 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.

48. 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

49. 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).

Other information

50. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information referred to does not include the financial statements, the auditor’s report and those selected key performance areas presented in the annual performance report that have been specifically reported in this auditor’s report.

51. 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.

52. My responsibility is to read this other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected key performance areas presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

53. If, based on the work I have performed, I conclude that there is a material misstatement in this other information, I am required to report that fact. I have nothing to report

Internal control deficiencies

54. 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.

55. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified opinion, and the material findings on the annual performance report and the material findings on compliance with legislation included in this report.

56. Senior management did not implement adequate recording, reviewing, and reporting processes and controls to ensure credible, complete and accurate financial reporting as per the approved audit action plan.

57. The municipality did not adequately prepare regular, accurate and complete financial reports that are supported and evidenced by reliable information. The financial statements contained numerous misstatements, of which some were adequately corrected. This was mainly due to staff not fully understanding the requirements of the financial reporting framework.

58. The performance management system and related controls were inadequate as they did not describe how the performance planning, monitoring, measurement, review, reporting and improvement processes should be organised and managed to ensure valid, accurate and complete performance reporting.

59. Inadequate measures taken to improve compliance with key laws and regulations (they do not yield the desired results.

Material irregularities

60. In accordance with the PAA and the material irregularity (MI) regulations, I have a responsibility to report on material irregularities identified during the audit and on the status of material irregularities as previously reported in the auditor's report.

Material irregularities identified during the audit

Interest and penalties paid due to late payment of pay as you earn and other taxes

61. The municipality's failure to comply with section 2(1)(a) of the fourth schedule, resulted in interest and penalties being incurred by the municipality in line with section 14 of the fourth schedule, which states that- "the Commissioner may impose on that employer a penalty, which is deemed to be a percentage based penalty imposed under Chapter 15 of the Tax Administration Act, for each month that the employer fails to submit a complete return which in total may not exceed 10 per cent of the total amount of employees' tax deducted or withheld or which should have been deducted or withheld by the employer from the remuneration of employees for the period described in that subparagraph."

62. The municipality did not adhere to the legislation for paying over PAYE and other taxes timeously, as a result the municipality incurred interest and penalties. The non-compliance is likely to result in a material financial loss for the municipality due to the interest incurred by the municipality as a result of not paying over PAYE and other taxes timeously.

63. The accounting officer was notified of this material irregularity on 1 April 2022 and was invited to make a written submission on the actions taken and that will be taken to address the matter. The accounting officer responded with the actions taken to resolve the material irregularity. The following actions have been taken to resolve the material irregularity:

- Since July 2023, the municipality had submitted the monthly PAYE returns to the South Afrucan Revenue Service (Sars) by legislated due date on monthly basis. However, the municipality is still not paying Sars within the stipulated period. Consequently, as disclosed in the 46 of the annual financial statements interest and penalties amounting to R5,31 million was incurred in 2022-23 financial statements.

- The accounting officer reported the fruitless and wasteful expenditure for 2011 to 2021 to the municipal public accounts committee (MPAC) for investigation. The investigation was concluded, and the report was tabled to council. On 31 March 2023 council resolved that the fruitless and wasteful expenditure be written off.

- The accounting officer is implementing the financial recovery plan under the support of the National Government Intervention. There are various revenue enhancement program that the municipality is implementing to ensure improvement in the revenue collection this includes but not limited to the following:

    - National Treasury is funding the project for replacement and installation of electricity meter. At the date of this report, the project is in progress.
    - Munsoft was appointed for assistance with the system that aligns the billing as part of revenue management projects. At the date of this report, the service provider has put the system in place to monitor the billing process.

- The Development Bank of Southern Africa (DBSA) has appointed service provider to assist with revenue enhancement project. At the date of this report, the service provider was on site implementing the revenue enhancement project.

64. I will follow-up on the implementation of actions during my next audit.

Unfairly disqualified bidder – appointment of a service provider for security services

65. The municipality did not comply with preferential procurement regulation (PPR) of 2017 5(7) which states that, each tender that obtained the minimum qualifying score for functionality must be evaluated further in terms of price and the preference point system and any objective criteria envisaged in regulation 11.

66. On tender number SC01/2021-2024, the bid evaluation committee unfairly disqualified a bidder on functionality and consequently eliminated the bidder from further evaluation. Instead of allocating 15 points, the bidder was awarded no points for the functionality criteria "Service provider must submit proof of firearm registration", despite submitting certified copies of proof of registration of 45 firearms. The disqualified bidder submitted a bid of R74 887 978,68 which was lower than the winning bidder's price of R80 605 849,68.

67. The non-compliance is likely to result in a material financial loss for Lekwa Local Municipality due to the appointment of a bidder whose bid amount exceeded the amount of the unfairly disqualified bidder.

68. The accounting officer was notified of this material irregularity on 28 April 2023 and was invited to make a written submission on the actions taken and that will be taken to address the matter. The accounting officer responded on 21 June 2023 with the actions taken to resolve the material irregularity. The following action have been taken to resolve the material irregularity:

    - The accounting officer initiated negotiations with the appointed service provider to reduce the contract value/amount to be equal or less than that of the unfairly disqualified bidder to prevent financial loss. Thus far, these negotiations have not resulted in the reduction of the price by the winning bidder.

    - On 15 June 2023, the accounting officer appointed presiding officers to institute the disciplinary proceeding against the members of the bid evaluation committee. At the date of this audit report, the disciplinary proceedings were underway and are expected to be concluded by 31 December 2023.

    - On 16 May 2023, with the assistance of the Provincial Treasury, the municipality provided managers and supervisors with training on supply chain management processes in order to capacitate officials with capacity to sit in bids evaluations committee. Furthermore, the accounting officer committed to compile a SCM training plan by 31 December 2023, which will be implemented and monitored.

    - The accounting officer prepared a schedule of payment/invoice forecast for the remaining period to monitor and keep track of monthly invoice for the remainder of the contract to keep the payments within the contracted value to avoid further financial losses on this contract.

69. I will follow up on the implementation of actions during my next audit.

Interest and penalties paid due to non-timeous submission of value added tax (VAT) returns

70. The municipality's failure to comply with section 28(1)(a) and (b) of the VAT Act, resulted in interest and penalties being incurred by the municipality in line with section 39 of the VAT Act, which states that – "If any person who is liable for the payment of tax and is required to make such payment in the manner prescribed in section 28 (1), fails to pay any amount of such tax within the period for the payment of such tax specified in the said provision, he shall, in addition to such amount of tax, pay, impose a penalty equal to 10 per cent of the said amount of tax in line section 39(1)(a)(i) and where payment of the said amount of tax is made on or after the first day of the month following the month during which the period allowed for payment of the tax ended, interest on the said amount of tax , calculated at the prescribed rated (but subject to the provisions of section 45A) for each month or part of a month in the period reckoned from the said first day in line section 39(1)(a)(ii).

71. The non-compliance is likely to result in a material financial loss for Lekwa Local Municipality due to the interest and penalties incurred by the municipality as a result of not submitting of VAT returns within prescribed timeframes.

72. The accounting officer was notified of this material irregularity on 13 April 2022 and was invited to make a written submission on the actions taken and that will be taken to address the matter. The accounting officer responded with the actions taken to resolve the material irregularity. The following actions have been taken to resolve the material irregularity:

- The accounting officer reported the fruitless and wasteful expenditure for 2011 to 2021 to the MPAC for investigation. The investigation was concluded, and the report was tabled to council. On 31 March 2023 council resolved that the fruitless and wasteful expenditure be written off.

- The accounting officer is implementing the financial recovery plan under the support of the national government intervention to resolve the material irregularity and has taken various revenue enhancement strategies and controls that the municipality has been implementing, which includes amongst others the following:
    - Appointed a service provider to assist with the full implementation of the debt control and credit policy, prepaid meter audits and replacement of faulty meters. Some actions were implemented, and others are still in progress at the date of this audit report.

    - A schedule is prepared by expenditure manager and reviewed by the chief financial officer (CFO) ensuring that VAT returns and payments are tracked and monitored on monthly basis. As a result of the implementation of this control, the municipality has not incurred interest and penalties since July 2023 up until the date of this audit report.

73. Based on the above actions that have been taken to resolve the material irregularity. I considered all the substantiating evidence provided and I have concluded that appropriate actions have been taken to address the material irregularity and it is considered resolved.

Material irregularities in progress

74. 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, the responses of the accounting officer were not yet due. These material irregularities will be included in next year's auditor's report.

Status of previously reported material irregularities

Full and proper records not kept

75. 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.

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

77. 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.

78. 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.

79. 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.

80. The financial recovery plan included various planned actions to resolve the material irregularity. I considered the implementation of the actions included in the financial recovery plan and observed that the accounting officer improved preventative controls on keeping of proper records, some of the preventative controls implemented include daily and monthly processing of transactions for key line items and mantaining a proper filing system to ensure that accounting records are easily retrievable when required. The accounting officer has committed to further strengthening the control environment by continuous monitoring of the revenue enhancement plan and audit action plan.

81. I will follow up on the full implementation of the action in my next audit.

Auditor - General

Mbombela

30 November 2023

AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence