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

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Victor Khanye Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2021, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as 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 Victor Khanye Local Municipality as at 30 June 2021, and 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 4 of 2020 (Dora).

Basis for qualified opinion

Work in progress – water infrastructure

3. The municipality did not assess, at reporting date, whether there was an indication that work in progress for water infrastructure as presented in note 4 may be impaired in accordance with GRAP 21, *Impairment of non-cash generating assets.* As a result, accumulated depreciation and impairment was understated and the carrying value of the water infrastructure was overstated. This also affected the impairment loss on property, plant and equipment as stated in the statement of financial performance. I was unable to quantify the full extent of the overstatement of water infrastructure and the understatement of impairment loss on property, plant and equipment as it was impracticable to do so.

VAT receivable

4. I was unable to obtain sufficient appropriate audit evidence for the adjustments made to the value-added tax (VAT) receivable comparative figure due to the status of the accounting records. I was unable to confirm the vat receivable by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to VAT receivable, stated at R41,65 million (2020: R31,03 million), in note 40.6 to the financial statements.

Sale of electricity – prepaid electricity

5. I was unable to obtain sufficient appropriate audit evidence that sale of electricity – prepaid electricity had been properly accounted for due to the status of the accounting records. I was

unable to confirm sale of electricity – prepaid electricity by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to sale of electricity – prepaid electricity, stated at R38,10 million (2020: R 34,59 million) in note 20 to the financial statements, and the related other debtors, stated at R10,49 million (2020: R16,70 million) in note 8 to the financial statements. In addition, there is an impact on the same amounts for prepaid electricity revenue, stated at R38,10 million (2020: R34,59 million), and receivable from agent, stated at R14,51 million (2020: R8,14 million), in the disclosure of principal-agent arrangement in note 51 to the financial statements.

Commission expense

6. I was unable to obtain sufficient appropriate audit evidence that commission expense had been properly accounted for due to the status of the accounting records. Furthermore, I was unable to obtain sufficient appropriate audit evidence to confirm the prior year correction to commission expense as stated in note 39.8 to the financial statements. I was unable to confirm the commission expense and the related prior period correction thereto by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to commission expense, stated at R34,97 million (2020: R30,38 million) in notes 34 and 51 (stated at the same amount) and stated at R1,26 million in note 39.8, to the financial statements.

Debt written off

7. The municipality did not account for the debt written off retrospectively, in accordance with the requirements of GRAP 3, *Accounting policies, estimates and errors*. The debt was written off to rectify billing errors from prior years, but the errors were not corrected by restating the opening balances of customer service debtors and provision for impairment, as well as property rates debtors and provision for impairment property rates for the earliest prior period. This resulted in the following misstatements:

- understatement of debt written off, as stated in note 27 to the financial statements;
- overstatement of gross customer service debtors and misstatement of provision for impairment, as stated in note 8 to the financial statements;
- as well as the overstatement of gross property rates debtors and misstatement of provision for impairment property rates debtors, as stated in note 9 to the financial statements.
- The debt written off restatement as stated in note 39.4 to the financial statements was also understated.

I was unable to quantify the full extent of the above misstatements as it was impracticable to do so.

Irregular expenditure

8. 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. This resulted in the understatement of irregular expenditure. I was unable to quantify the full extent of the understatement to irregular expenditure of R188,32 million (2019-20: R122,91 million) as disclosed in note 38.1 to the financial statements as it was impracticable to do so.

Prior period errors and reclassifications

9. The municipality did not correctly make adjustments for prior period errors relating to irregular expenditure, trade and other receivables from exchange transactions, trade and other receivables from non-exchange transactions, accumulated surplus and VAT receivables in accordance with GRAP 3, *Accounting policies, estimates and errors*. I was unable to quantify the full extent of the following misstatements as it was impracticable to do so:

- Understatement of total restatements to irregular expenditure, stated at R56,52 million in note 39.10 to the financial statements
- Understatement of restatements to trade and other receivables from exchange transactions, stated at R9,21 million in note 39.7 to the financial statements
- Understatement of restatements to trade and other receivables from non-exchange transactions, stated at negative R15,65 million in note 39.6 to the financial statements
- Understatement of restatements to VAT receivable, stated at R189 569 in note 39.9 to the financial statements
- Misstatement of total restatement to accumulated surplus, stated in notes 39.3 and 39.5 to the financial statements

Context for the opinion

10. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of this auditor's report.

11. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *International code of ethics for professional accountants* (*including International Independence Standards*) (IESBA code) as well as other ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.

12. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Emphasis of matters

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

Material losses – water

14. As disclosed in note 40.1 to the financial statements, the municipality incurred material water losses of 3 841 794 units (2019-2020: 5 105 255 units), which represents 59% (69%:2019-2020) of total water purchased.

Other matter

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

Unaudited disclosure notes

16. 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

17. 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.

18. 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

19. 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.

20. 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

21. 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 development priorities presented in the annual performance report. I performed procedures to identify material findings but not to gather evidence to express assurance.

22. 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.

23. 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 development priority presented in the municipality's annual performance report for the year ended 30 June 2021:

Development priority	Pages in the annual performance report
KPA 1 – basic service delivery and infrastructure	x – x

24. 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.

25. The material findings in respect of the usefulness and reliability of the selected development priorities are as follows:

KPA 1 – basic service delivery and infrastructure

Number of households in formal human settlements provided with (alternative sanitation) by Jun 2021

26. I was unable to obtain sufficient appropriate audit evidence that clearly defined the predetermined evidence of collection or that related systems and processes were established to enable consistent measurement and reliable reporting of the actual achievement for the indicator. This was due to insufficient measurement definitions and processes. I was unable to test whether the indicator was well-defined and verifiable by alternative means. As a result, I was unable to audit the reliability of the achievement of 50 households in formal human settlements provided with (alternative sanitation) by June 2021 reported against the target of 50 households in formal human settlements provided with (alternative sanitation) by June 2021 in the annual performance report.

Other matter

27. I draw attention to the matters below.

Achievement of planned targets

28. Refer to the annual performance report on pages xx to xx for information on the achievement of planned targets for the year. This information should be considered in the context of the material findings on the usefulness of the reported performance information in paragraph 26 of this report.

Adjustment of material misstatements

29. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of KPA 1 – basic service delivery and infrastructure. 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 included in the basis for qualified opinion paragraphs.

Report on the audit of compliance with legislation

Introduction and scope

30. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

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

Annual financial statements

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

Expenditure management

33. 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.

34. Reasonable steps were not taken to prevent unauthorised expenditure of R65 621 751, as disclosed in note 38 to the annual financial statements, in contravention of section 62(1) (d) of the MFMA.

Strategic planning and performance management

35. The municipality did not maintain its performance management system and related controls, which did not describe how the performance measurement and reporting processes should be conducted and managed, as required by municipal planning and performance management regulation 7(1).

Procurement and contract management

36. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by supply chain management (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).

37. 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).

38. 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 the 2017 preferential procurement regulation 8(2).

Consequence management

39. 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.

40. 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.

41. 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.

Revenue management

42. The municipality did not have in place an effective system of internal control for revenue and debtors , as required by section 64(2) (f) of the MFMA.

43. The municipality did not have in place an adequate management, accounting and information system which accounts for revenue, debtors and receipt of revenue, as required by section 64(2) (e) of the MFMA.

Assets management

44. The municipality did not have in place an effective system of internal control for assets including an asset register, as required by section 63(2) (c) of the MFMA.

45. The municipality did not have in place an adequate management, accounting and information system which accounts for assets, as required by section 63(2) (a) of the MFMA.

Conditional grants

46. The disaster management grant was not spent for its intended purposes in accordance with the applicable grant framework, as required by section 17(1) of Dora.

Other information

47. 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 development priority presented in the annual performance report that has been specifically reported in the auditor's report.

48. 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.

49. 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 development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

50. 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

51. 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.

52. Leadership did not adequately develop and monitor the implementation of action plans to address internal control deficiencies.

53. The accounting officer did not adequately manage controls over compliance with laws and regulations, daily and monthly processing and reconciling of transactions.

54. The municipality did not prepare regular, accurate and complete financial and performance reports that are supported and evidenced by reliable information.

Mbombela

Auditor General

01 March 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 selected development priorities 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 Victor Khanye 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 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.