Auditing to build public confidence

AUDITOR-GENERAL
SOUTH AFRICA

Report of the auditor-general to the North West Provincial Legislature and the council on the Mahikeng Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Mahikeng Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2021, and the statement of financial performance, statement of changes in net assets, cash flow statement and the 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 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 Mahikeng Local Municipality as at 30 June 2021, 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 4 of 2020 (DoRA).

Basis for qualified opinion

Receivables from exchange and non-exchange transactions

3. The municipality did not make an assessment of its financial assets that includes the financial difficulty, dilinquency, probable sequestration or loss of markets for receivables from exchange transactions and receivables from non-exchange transactions as required by GRAP 104, *Financial instruments* and GRAP 108, *Statutory receivables*. I was unable to quantify the full impact of this misstatement on receivables from exchange trancactions of R59 807 063 as disclosed in note 9 or receivables from non-exchange transactions of R16 503 176 as disclosed in note 8 to the financial statements as it was impracticable to do so.

Payables from exchange transactions

4. During 2020, I was unable to obtain sufficient appropriate audit evidence for unallocated receipts included in sundry creditors – advance payments as information included in the age analysis was insufficient to identify and audit the unallocated receipts. My audit opinion on the financial statements for the period ended 30 June 2020 was modified accordingly. I was still unable to confirm these creditors by alternative means. Consequently, my opinion on the current period's financial statements is also modified because of the possible effect of this matter on the comparability of the current period's figures.

Context for the opinion

5. 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.
6. 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.
7. 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

8. I draw attention to the matter below. My opinion is not modified in respect of this matter.
9. As disclosed in note 38 of the financial statements, the municipality reported a deficit of R141 608 990 for the year, current liabilities exceed current assets by R381 775 302 and the municipality is struggling to collect all revenue for services rendered to consumers. These conditions along with other matters included in the note indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern.

Emphasis of matters

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

Unauthorised, irregular and fruitless and wasteful expenditure

11. As disclosed in note 40 to the financial statements, unauthorised expenditure of R120 803 265 was incurred in the current year and unauthorised expenditure of R1 176 061 381 in respect of previous years have not yet been dealt with in accordance with section 32 of the MFMA.
12. As disclosed in note 42 to the financial statements, irregular expenditure of R209 770 249 was incurred in the current year and irregular expenditure of R1 189 694 499 from prior years have not yet been dealt with in accordance with section 32 of the MFMA.
13. As disclosed in note 41 to the financial statements, fruitless and wasteful expenditure of R559 695 was incurred in the current year and fruitless and wasteful expenditure of R37 652 049 from prior years have not yet been dealt with in accordance with section 32 of the MFMA.

Restatement of the corresponding figures

14. As disclosed in note 36 to the financial statements, the corresponding figures for 30 June 2020 were restated as a result of adjustments made to correct errors in the financial statements of the municipality.

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. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

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 the 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 there is 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 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 the 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 usefulness and reliability of the reported performance information against predetermined objectives for selected programme 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 also did not extend to any disclosures or assertions relating to 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 programme presented in the annual performance report of the municipality for the year ended 30 June 2021:

Programme	Pages in the annual performance report
KPA 5 – Basic service delivery and infrastructure investment	119 – 125

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 programme are as follows:

KPA 5 – Basic service delivery and infrastructure investment

Various indicators

26. I was unable to obtain sufficient appropriate audit evidence that systems and processes were established to enable consistent measurement and reliable reporting of performance against the predetermined indicator definitions for the indicators listed below. This was due to insufficient measurement definitions and processes. As a result, I was also unable to obtain sufficient appropriate audit evidence for the achievements reported in the annual performance report. I was unable to validate the existence of the systems and the reported achievements by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements for the following indicators:

Indicator	Planned target	Reported achievement
44. Number of kilometres of tarred road maintained	8 km	17.784 km
45. Number of kilometres of storm water drainage maintained	4 km	4.1626 km
46. Number of kilometres of rural gravel road maintained	5 km	7.8 km
65 Number of illegal dumping sites cleared	55	35

Other matters

27. I draw attention to the matters below.

Achievement of planned targets

28. Refer to the annual performance report on pages 119 to 125 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 25 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 5 – Basic service delivery and infrastructure investment. As management subsequently corrected only some of the misstatements, I reported material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

Report on 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 municipality's compliance 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:

Strategic and performance management

32. The integrated development plan (IDP) was not drafted considering the integrated development process and proposals submitted to it by the district municipality, as required by section 29(3)(b) of the Municipal Systems Act 32 of 2000 (MSA).

Financial statements and annual report

33. 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. Some material misstatements of current liabilities, revenue and expenditure identified by the auditors in the submitted financial statements were adequately corrected and the supporting records could be provided subsequently but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

Asset management

34. Funds were invested in a mutual bank in contravention of municipal investment regulation 6.

Expenditure management

35. Reasonable steps were not taken to prevent unauthorised expenditure of R120 803 265, as disclosed in note 40 to the financial statements, in contravention of section 62(1)(d) of the MFMA.
36. Reasonable steps were not taken to prevent fruitless and wasteful expenditure of R559 695, as disclosed in note 41 to the financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was interest caused by late and non-payments of outstanding balances.
37. Reasonable steps were not taken to prevent irregular expenditure of R209 770 249 as disclosed in note 42 to the financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was due to non-compliance with SCM regulation 29(2).

Procurement and contract management

38. Persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e).

Consequence management

39. Unauthorised, irregular and 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) of the MFMA.

Other information

40. 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 thereon and those selected programmes presented in the annual performance report that have been specifically reported on in this auditor's report.
41. 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 thereon.
42. 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 programmes presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
43. 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 in this regard.

Internal control deficiencies

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

    - Leadership's involvement relating to the internal control environment remains lacking as material findings continue to arise in the submitted financial statements and performance report. Monitoring of internal controls, review processes and action plans are still not adequate to reduce findings in financial and performance reporting and compliance with laws and regulations. An effective consequence management process is not in place to reduce and eliminate recurring SCM transgressions.
    - Management's responsibilities as indicated previously revolved around the preparation of accurate and complete financial and performance reports supported by reliable information. This achievement depends on regular reporting, functioning internal controls and oversight. Skills transfer is not sufficient to eliminate reliance on consultants.
    - Risk assessments on all spheres of financial reporting and compliance monitoring will identify weaknesses in control systems. Internal audit and the audit committee should assist in the development of internal control procedures to address these risks.

Material irregularities

45. 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.

Material irregularities identified during the audit

46. The material irregularities identified are as follows:

Investment of funds in contradiction of the Municipal Investment Regulations

47. During 2018, the municipality invested funds in a 32-day notice account with a mutual bank that was not registered in terms of the Banks Act 94 of 1990, which is a contravention of Municipal Investment Regulation 6(c). As the mutual bank was placed under curatorship on 11 March 2018, the non-compliance is likely to result in a material financial loss if the municipality cannot obtain a refund on these deposits made. During the 2019-20 financial year, the municipality impaired the investment of R83 440 312 (including interest).

48. The accounting officer was notified of the material irregularity on 24 February 2021. The following actions have been taken to resolve the material irregularity:

- The municipality successfully lodged a claim against the estate of mutual bank on 13 November 2018 in the Gauteng High Court. The claim and the process to recover the deposits from the estate of the mutual bank is still in progress.
- An investigation into the matters was finalised concluding that the previous accounting officer was responsible for the non-compliance and the related financial loss. The municipality instituted disciplinary actions against the previous accounting officer resulting in his dismissal.
- Criminal proceedings were instituted against the precious accounting officer, he appeared in the Molopo Magistrate Court on 11 August 2021 and 6 November 2021. The criminal proceedings are ongoing.

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

Additional finance charges on INCA loan

50. The municipality entered into a loan agreement with a financial institution on 8 April 2008 where the loan is repayable over 20 years. The municipality is required to make bi-annual installments to repay the loan. The accounting officer did not take reasonable steps to ensure that the bi-annual repayments were made on June 2019, December 2019 and June 2020 which is in contravention of section 65(2)(e) of the MFMA. The non-compliance resulted in a material financial loss of R3 509 090 as a result of penalty interest due to the non-payment.

51. The accounting officer was notified of the material irregularity on 24 February 2021 and was invited to make a written submission on the actions taken and that will be taken to address the matter. The accounting officer failed to make the written submission within the stipulated period.

52. I recommend that the accounting officer should take the following actions to address the material irregularity, which should be implemented by 28 February 2022:

- Appropriate action should be taken for the council investigation to commence in order to determine if the financial loss should be recovered from any person(s) liable for the fruitless and wasteful expenditure as required by section 32(2)(b) of the MFMA.
- The non-compliance should be investigated to determine if any official might have committed an act of financial misconduct or an offence in terms of chapter 15 of the MFMA.
- Disciplinary or, when appropriate, criminal proceeding should commence against any official who has allegedly committed an act of financial misconduct or an offence, as required by section 62(1)(e) of the MFMA and in the manner prescribed by the Municipal Regulations on Financial misconduct procedures and criminal proceedings.

53. The municipality has subsequently entered into a settlement agreement with the financial institution in terms of which the municipality will be released from the obligation to pay the penalty interest. I will follow up on this settlement agreement and implementation of these recommendations by the due date.

Auditor General

Potchefstroom

14 December 2021

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 municipality’s financial statements, and the procedures performed on reported performance information for selected programmes 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 the 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 related to events or conditions that may cast significant doubt on the Mahikeng Local Municipality’s ability 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 the opinion on the financial statements. My conclusions are based on the information available to me at the date of the auditor’s report. However, future events or conditions may cause a municipality to cease to continue as a going concern.
   - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and 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 confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and where applicable, related safeguards.