



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence



KING SABATA DALINDYEBO LOCAL MUNICIPALITY

Audit Report

For the year ended 30 June 2019



**AUDITOR - GENERAL
SOUTH AFRICA**

Auditing to build public confidence

Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on the King Sabata Dalindyebo Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the King Sabata Dalindyebo Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2019, 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 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 King Sabata Dalindyebo Local Municipality as at 30 June 2019, and its financial performance and cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act no. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2018 (Act no.1 of 2018) (Dora).

Basis for qualified opinion

Property, plant and equipment

3. The municipality did not account for its property, plant and equipment in accordance with GRAP 17, *Property plant and equipment* as completed projects were incorrectly disclosed as work in progress. As a result, work in progress is overstated and infrastructure assets understated by R18,1 million, as disclosed in note 9 to the financial statements.
4. Further, the municipality incorrectly included residual values on roads infrastructure when calculating depreciation. As a result, accumulated depreciation on infrastructure assets disclosed in note 9 to the financial statements and depreciation and amortisation included in the statement of financial performance is understated by R14,8 million.

Expenditure: bulk purchases

5. I was unable to obtain sufficient appropriate audit evidence for bulk purchases, as internal controls had not been established to verify the monthly amounts billed by the electricity supplier. I could not confirm whether bulk purchases had been correctly recorded by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to bulk purchases of R268,3 million disclosed in note 33 to the financial statements and electrical distribution losses of R21,2 million disclosed in note 47 to the financial statements.

Employee related costs

6. The municipality did not account for employee related costs in accordance with of GRAP 1, *Presentation of financial statements*. A number of individually immaterial misstatements were identified relating to overtime payments, acting allowances, unemployment insurance fund and skills development levy as disclosed in note 27 to the financial statements, the cumulative effect thereof resulted in a material misstatement. Consequently, employee related costs in the statement of financial performance was overstated by an amount of R14,4 million. This also has an impact on the surplus for the period and on the accumulated surplus.

Inventory

7. I was unable to obtain sufficient appropriate audit evidence for the restatement of the corresponding figure for inventory. As disclosed in note 53 to the financial statements, the restatement of R12,1 million was made to rectify a previous year misstatement, but the restatement could not be substantiated by supporting evidence. I was unable to confirm the restatement by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the inventory corresponding figure stated at R 3,2 million in the financial statements.

Fines, penalties and forfeits

8. The municipality did not recognise all outstanding traffic fines in accordance with GRAP 23, *Revenue from non-exchange transactions* as the municipality did not maintain adequate records of outstanding traffic fines received but not yet paid at year-end. I was unable to determine the full extent of the understatement of fines, penalties and forfeits and the impact on receivables from non-exchange transactions, as it was impracticable to do so. Consequently, I was unable to determine whether any adjustments were necessary to fines, penalties and forfeits at R2,7 million in the statement of financial performance.

Context for the opinion

9. 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.
10. I am independent of the municipality in accordance with sections 290 and 291 of the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* and, parts 1 and 3 of the International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA codes) as well as the 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 codes.
11. 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

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

13. As disclosed in note 54 to the financial statements, the municipality is experiencing financial difficulties as its current liabilities exceed its current assets. The events or conditions disclosed in note 54, together with other matters set forth in the same note, indicate that material uncertainty exists that may cast significant doubt on the municipality's ability to continue to fund its existing level of operations.

Emphasis of matters

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

Significant uncertainty

15. As disclosed in note 42 to the financial statements, the municipality is the defendant in a number of lawsuits. The municipality is opposing the claims and the ultimate outcome of the matters cannot presently be determined; however, provision has been made in the financial statements for any liabilities that may result.

Impairment loss

16. As disclosed in notes 4 and 5 to the financial statements, cumulative debt impairments of R307,8 million (2017-18: R265,1 million) and R273,7 million (2017-18: R232,2 million) were made to receivables from exchange and non-exchange transactions respectively as a result of slow recovery from debtors.

Restatement of corresponding figures

17. As disclosed in note 53 to the financial statements, the corresponding figures for 30 June 2018 were restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2019.

Other matters

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

Unaudited disclosure notes

19. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with this legislation. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion on it.

Unaudited supplementary information

20. The supplementary information set out on pages x to x does not form part of the annual performance report and is presented as additional information. I have not audited these schedules and, accordingly, do not report thereon.

Responsibilities of the accounting officer for the financial statements

21. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the SA 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.

22. In preparing the financial statements, the accounting officer is responsible for assessing the King Sabata Dalindyebo Local 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

23. 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.
24. 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

25. In accordance with the Public Audit Act of South Africa, 2004 (Act no. 25 of 2004) (PAA) and the general notice issued in terms thereof I have a responsibility to report material findings on the reported performance information against predetermined objectives for the selected development priority presented in the annual performance report. I was engaged to perform procedures to raise findings but not to gather evidence to express assurance.
26. 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 development priority presented in the annual performance report of the municipality for the year ended 30 June 2019:

Development priorities	Pages in the annual performance report
Basic services and infrastructure development	X – X

27. 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.

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

Basic service delivery and infrastructure development

Various indicators

29. I was unable to obtain sufficient appropriate audit evidence to validate the existence of a system and processes that enable reliable reporting of actual achievement against the indicators listed below. Sufficient appropriate audit evidence could not be provided in some instances while in other cases, the supporting evidence provided did not agree to the reported achievements in the annual performance report. Based on the supporting evidence provided, the achievement was different from those reported in the annual performance report, but I was unable to further confirm the reported achievements by alternative means. In addition, the reason for the variance between the planned target and the reported achievement was also not explained in the annual performance report. Consequently, I was unable to determine whether any further adjustments were required to the reported achievements of the indicators listed below.

Indicator number	Indicator description	Planned target	Reported achievement
3.1.2	50 000 m of Storm water infrastructure in the Urban Areas and roads rehabilitation	50 000m of Storm water infrastructure in the Urban Areas and roads rehabilitation	44 546
3.1.4	100km of roads constructed and rehabilitated by June 2019	100 km of roads constructed	0
3.1.5	1 212 households electrified by June 2019	808 household electrified in Mthatha West as part of phase 2, 404 households electrified in Maiden Farm extension as part project A	0
3.1.9	10 km of electrical infrastructure refurbished	10 km of electrical infrastructure refurbished	10 km done

Indicator number	Indicator description	Planned target	Reported achievement
3.1.16	Construction of 360 houses in Maydene Farm Ext. by June 2019	360 houses by June 2019	0
3.1.17	Kei rail 527 sites serviced	537 serviced sites	Done
3.1.18	New Brighton 131 units build	131 units build	0
3.5.68	No of EPWP Beneficiaries recruited	No target was included in APR	0
No number in annual performance report	% of completion of construction works of 2 Buy Back Centres	Establishment of 2 Buy Back Centre's in Ward 9 & Ward 24	0
3.5.71	No. of new households with access to refuse removal	5 250 households (Maydene Farm extension, Bongweni, Ncambedlana Extension & Payne	0
No number in annual performance report	% of completion of construction works	100% completion of deliverables as per allocated budget	80% complete
No number in annual performance report	No. of work opportunities created for coastal cleaning	70 work opportunities	30

Various indicators

30. The reported achievement in the annual performance report did not agree to the supporting evidence provided for the indicators listed below. The supporting evidence provided indicated that the achievements of these indicators were as follows:

Indicator number	Indicator description	Reported achievement	Audit value
3.1.1	50 000m ² , street repair/resealing of urban roads	30780	4 016
3.1.3	800 km rural roads maintenance /regraveling and blading	537	687

Various indicators

31. The source information, evidence and method of calculation for the achievement of the planned indicator were not clearly defined for the following indicators:

Indicator number	Indicator description	Planned target
3.1.1	50 000m ² , street repair/resealing of urban roads	50 000m ² roads, street repair / resealing of urban roads
3.1.2	50 000m of storm water infrastructure in the urban areas and roads rehabilitation	50 000m of storm water infrastructure in the urban areas and roads rehabilitation
3.1.3	800 km rural roads maintenance /regraveling and blading	800 km rural roads maintenance/re-gravelling and blading
3.1.4	100 km of roads constructed and rehabilitated by June 2019	100 km of roads constructed
3.1.5	1 212 households electrified by June 2019	808 household electrified in Mthatha West as part of phase 2 404 households electrified in Maiden Farm extension as part Project A
3.1.9	10 km of electrical infrastructure refurbished	10 km of electrical infrastructure refurbished
3.1.16	Construction of 360 houses in Maydene Farm Ext. by June 2019	360 houses by June 2019
3.1.17	Kei rail 527 sites serviced	537 serviced sites

Indicator number	Indicator description	Planned target
3.1.18	New Brighton 131 units build	131 units build
No number in annual performance report	% of completion of construction works	100% completion of deliverables as per allocated budget

Indicator number 3.5.68: No of EPWP beneficiaries recruited

32. The planned target for this indicator was not specific in clearly identifying the nature and required level of performance as it did not specify a target in the annual performance report.

Other matter

33. I draw attention to the matter below.

Achievement of planned targets

34. Refer to the annual performance report on pages ... to ... for information on the achievement of planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 28 to 32 of this report.

Report on the audit of compliance with legislation

Introduction and scope

35. 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.

36. The material findings on compliance with specific matters in key legislations are as follows:

Strategic and performance management

37. 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 conducted and managed, as required by municipal planning and performance management regulation 7(1).

Annual financial statements, annual performance report and annual report

38. 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 property, plant and equipment and irregular expenditure were subsequently corrected and the

supporting records were subsequently provided, but the uncorrected material misstatements resulted in the financial statements receiving a qualified opinion.

39. The oversight report adopted by the council on the 2017-18 annual report was not made public, as required by section 129(3) of the MFMA.

Expenditure management

40. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
41. Reasonable steps were not taken to prevent irregular expenditure of R43,8 million disclosed in note 46 to the financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by non-adherence to the SCM regulations and preferential procurement regulations.
42. Reasonable steps were not taken to prevent fruitless and wasteful expenditure of R12,8 million disclosed in note 45 to the 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 and penalties.
43. Reasonable steps were not taken to prevent unauthorised expenditure of R59,0 million disclosed in note 44 to the financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by spending exceeding the main segments within the budget.

Human resource management

44. Job descriptions were not established for all posts in which appointments were made, as required by section 66(1)(b) of the Municipal Systems Act.
45. The municipal manager did not sign performance agreements within the prescribed period, as required by section 57(2)(a) of the Municipal Systems Act

Consequence management

46. Irregular, fruitless and wasteful, and unauthorised expenditure 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.

Asset management

47. An effective system of internal control for assets (including an asset register) was not in place, as required by section 63(2)(c) of the MFMA.

Procurement and contract management

48. Some goods and services with a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).

49. Some bid documentation for procuring 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).

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 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 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 thereon.
52. 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 priority 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 of this other information, I am required to report that fact. I have nothing to report in this regard.

Internal control deficiencies

54. 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.
55. Leadership did not adequately oversee financial and performance reporting and compliance with legislation. In this regard, leadership did not appropriately monitor the implementation of policies and procedures to support the achievement of credible reporting and compliance with legislative requirements. Progress on the municipality's audit intervention plan was slow to adequately address issues raised in the previous year.
56. Management did not prepare regular, accurate and complete financial and performance reports that were supported and evidenced by reliable information, as material misstatements were identified in the annual financial statements and material findings were raised on the annual performance report. The lack of a properly functioning control environment resulted in deficiencies in the record management system and underlying records.

Other reports

57. I draw attention to the following engagements conducted by various parties that 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.
58. The Special Investigation Unit (SIU) was investigating matters that arose in previous years, including the costs incurred for the funeral of former president Nelson Mandela. This investigation is still in progress.
59. A forensic investigation was concluded by PWC on behalf of the Department of Cooperative Governance and Traditional Affairs (Cogta) into grievances raised by staff members, which extends to task payments made by the municipality in the previous financial cycle.

Auditor - General

East London

30 November 2019



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