

Report of the auditor-general to the Free State Legislature and the council on the Setsoto Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Setsoto 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 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 Setsoto 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 recognise all items of property, plant and equipment in accordance with GRAP 17, *Property, plant and equipment* as assets still in use were incorrectly written off. Consequently, property, plant and equipment was understated and the total expenditure was overstated by R496 324 822. Additionally, I was unable to obtain sufficient appropriate audit evidence for property, plant and equipment due to the status of the accounting records as I could not confirm that the municipality only recognised assets under their control in the fixed assets register. Consequently, I was unable to determine whether any adjustments were necessary to property, plant and equipment stated at R2 483 731 590 (2018: R3 145 203 126) in note 11 to the financial statements.

Service charges

4. I was unable to obtain sufficient appropriate audit evidence for service charges as the municipality did not have adequate systems in place to account for the billing of service. I was unable to confirm the service charges by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to service charges stated at R178 270 347 in note 22 to the financial statements.

Receivables from non-exchange transactions

5. I was unable to obtain sufficient appropriate audit evidence for sundry debtors as the municipality did not have adequate systems in place to account for the sundry debtors. I was

unable to confirm the sundry debtors by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to sundry debtors stated at R6 812 522 in note 7 to the financial statements.

Context for the opinion

6. 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.
7. 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.
8. 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

9. I draw attention to the matter below. My opinion is not modified in respect of this matter.
10. Note 53 to the financial statements indicates that the municipality incurred a net loss of R644 326 365 during the year ended 30 June 2019. The municipality deducted pay as you earn from employee's salaries, but did not pay over R12 654 718 (2018 R14 976 672) of these amounts deducted to the relevant third parties at year end as disclosed in note 16. In addition, the municipality owed Eskom R25 110 583 (2018: R15 478 508) as at 30 June 2019 which was long overdue. These events or conditions, along with other matters set forth in note 53, indicate that a material uncertainty exists that may cast significant doubt on the municipality's ability to continue as a going concern.

Emphasis of matters

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

Irregular expenditure

12. As disclosed in note 46 to the financial statements, irregular expenditure of R76 933 103 (2018: R98 765 998) was incurred due to non-compliance with supply chain management (SCM) requirements.

Unauthorised expenditure

13. As disclosed in note 44 to the financial statements, unauthorised expenditure of R616 848 443 (2018: R17 301 739) was incurred, due to overspending a main division within the vote.

Fruitless and wasteful expenditure

14. As disclosed in note 45 to the financial statements, fruitless and wasteful expenditure of R2 979 591 (2018: R3 350 092) was incurred, mainly due to interest on arrear payments to creditors.

Restatement of corresponding figures

15. As disclosed in note 57 to the financial statements, the corresponding figures for 30 June 2018 were restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2019.

Material uncertainty relating to claims against the municipality

16. With reference to note 54 to the financial statements, the municipality is the defendant in various lawsuits. The ultimate outcome of these matters could not be determined and no provision for any liabilities that may result were made in the financial statements.

Material losses

17. As disclosed in note 48 to the financial statements, material water distribution losses of R15 342 187 (2018: R7 044 679) and electricity distribution losses of R8 928 564 (2018: R2 871 219) were incurred by the municipality mainly due to leakages, burst water pipes, line losses, tampering and theft.

Material impairment

18. As disclosed in note 5 to the financial statements, consumer receivables was impaired by R176 469 525 (2018: R157 730 763).

Other matter

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

Unaudited disclosure notes

20. 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.

Unaudited supplementary schedules

21. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion on thereon.

Responsibilities of the accounting officer for the financial statements

22. 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.

23. In preparing the financial statements, the accounting officer is responsible for assessing the Setsoto 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

24. 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.
25. 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

26. 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 key performance area (KPA) presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
27. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators/ measures included in the planning documents. 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.
28. 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 KPA presented in the annual performance report of the municipality for the year ended 30 June 2019:

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

29. 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.

The material findings in respect of the usefulness and reliability of the selected KPA are as follows:

Percentage of unplanned water interruptions and sewer blockages complaints/callouts responded to within required timeframe

30. The reported achievement of 100% for the target of 100% is not reliable as the municipality did not maintain adequate records to enable reliable reporting on the achievement of targets. As a result, I was unable to obtain sufficient appropriate audit evidence in some instances while in other cases the supporting evidence provided did not agree with the reported achievement. Based on the supporting evidence that was provided, the achievement was 88%, but I was unable to further confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any further adjustments were required to the reported achievement.

Various indicators

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

Indicator description	Reported achievement	Audited value
Km of re-gravelled	30 108	102.57
Percentage of sewer network infrastructure maintained	100%	90%

Various indicators

32. The source information or evidence for achieving the following planned indicators were not clearly defined:

Section	Indicator description
Electricity	Percentage unplanned outages restored within required timeframe
Water and Waste water Operations and Maintenance services	Percentage of unplanned water interruptions and sewer blockages complaints/callouts responded to within required timeframe
Development Planning and Social Security	Percentage protest complaints reported and resolved within required timeframe

Section	Indicator description
Development Planning and Social Security	Percentage firefighting, disaster and emergencies incidents attended to within the required timeframe
Local Economic Development and Tourism	Percentage business license applications and permits processes and approved within the required timeframe
Waste Management	Percentage external and internal audit queries responded to and addressed within timeframe
Security Services and Property Management	Percentage external and internal audit queries responded to and addressed within timeframe
Disaster Management and Fire Services	Percentage external and internal audit queries responded to and addressed within timeframe
Local Economic Development and Tourism	Percentage external and internal audit queries responded to and addressed within timeframe.
Planning and Property Management	Number of illegal land use reports

Various indicators

33. The indicators listed below were approved in the service delivery and budget implementation plan (SDBIP) but were not included in the annual performance report.

Indicator description	Planned target
Percentage of road infrastructure network maintained	100%
Percentage protest complaints reported and resolved within required timeframe	100%
Percentage firefighting, disaster and emergencies incidents attended to within the required timeframe	100%
Percentage of household with subsidized housing	70%

Other matters

34. I draw attention to the matters below.

Achievement of planned targets

35. 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 30 to 33 of this report.

Adjustment of material misstatements

36. 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 reported above.

Report on the audit of compliance with legislation

Introduction and scope

37. 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.
38. The material findings on compliance with specific matters in key legislation are as follows:

Annual financial statements, performance and annual report

39. The financial statements were not submitted to the Auditor-General, for auditing, within two months after the end of the financial year, as required by section 126(1)(a) of the MFMA.
40. The financial statements were not submitted to the Auditor-General within two months after the end of the financial year and a written explanation setting out the reasons for the failure was not tabled in council as required by section 133(1)(a) of the MFMA.
41. 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, current assets 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.

Expenditure management

42. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
43. Reasonable steps were not taken to prevent irregular expenditure of R76 933 103 as disclosed in note 46 to the annual financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by non-compliance with the SCM requirements.
44. Reasonable steps were not taken to prevent fruitless and wasteful expenditure of R2 979 591, 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 levied by creditors.
45. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R616 848 443, 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 depreciation on revalued assets.

Revenue management

46. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.
47. Revenue due to the municipality was not calculated on a monthly basis, as required by section 64(2)(b) of the MFMA.

Procurement and contract management

48. Goods and services with a transaction value below R200 000 were procured without obtaining the required price quotations, in contravention of SCM regulation 17(a) and (c). Similar non-compliance was reported in the previous year.
49. Some quotations were accepted from bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c). Similar non-compliance was reported in the previous year.
50. Some quotations were accepted from bidders whose tax matters had not been declared by the South African Revenue Service to be in order, in contravention of SCM regulation 43. Similar non-compliance was reported in the previous year.
51. Some goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1). Similar non-compliance was reported in the previous year.
52. Some invitations for competitive bidding were not advertised for a required minimum period of days, in contravention of SCM regulation 22(1) and 22(2). This non-compliance was identified in the procurement processes for the upgrading of the wastewater treatment works in Clocolan (T03 2018/19) and the conversion of 969 VIP toilets (T04 2018/19).
53. Contracts were awarded to bidders based on pre-qualification criteria that differed from those stipulated in the original invitation for bidding, in contravention of the 2017 preferential procurement regulation 4(1) and 4(2). This non-compliance was identified in the procurement processes for the construction of 500mm diameter pump line from DE-PUT water treatment works in Senekal/Matwabeng (T17 2018/19) and the construction of a 11ml reinforced concrete reservoir in Senekal (T18 2018/19).

Asset management

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

Human resources management

55. Appropriate systems and procedures to monitor, measure and evaluate staff performance were not developed and adopted, as required by section 67(1)(d) of the Municipal Systems Act.

Strategic planning and performance management

56. The internal controls processes relating to the performance monitoring, measurement, review and reporting were not adequately performed, as required by municipal planning and performance management regulation 7(1).

Other information

57. 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 KPA presented in the annual performance report that have been specifically reported in this auditor's report.
58. 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.
59. 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 KPA presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
60. 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

61. 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, findings on the annual performance report and the findings on compliance with legislation included in this report.
62. In certain circumstances, management did not exercise oversight, to ensure that accurate and reliable information is submitted on time, as there were material misstatements in the financial statements and annual performance report that required adjustments during the audit.
63. Leadership did not adequately address the root causes of irregular expenditure identified in the previous year's resulting in irregular expenditure again in the current financial year.
64. Management did not adequately review and monitor compliance with legislation as there were material repeat findings on compliance identified in the current financial year.

65. Management did not implement effective human resource management to ensure that adequate and sufficiently skilled resources are in place and that performance for junior employees is monitored. There were significant vacancies of key management as well as support staff in the finance and SCM units during the financial year.

Auditor - General

Bloemfontein

06 December 2019



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 KPA 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 related to events or conditions that may cast significant doubt on the Setsoto 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 this auditor’s report. However, future events or conditions may cause a municipality to cease continuing 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.