

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

## Report on the audit of the financial statements

### Qualified opinion

1. I have audited the financial statements of the Mantsopa 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 Mantsopa 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. I was unable to obtain sufficient appropriate audit evidence that property, plant and equipment had been properly accounted for, as the municipality did not provide adequate supporting documentation for a project that has been transferred from work-in-progress to complete water infrastructure assets during the year. In addition, the municipality did not determine recoverable amounts for roads and sanitation infrastructure assets where indicators of impairment were identified and the municipality did not assess the useful lives and residual values of assets in accordance with *GRAP 17, Property, plant and equipment*. I was unable to determine the impact on the net carrying amount of infrastructure assets as it was impracticable to do so. I was unable to confirm the property, plant and equipment by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the property, plant and equipment stated at R861 884 663 in note 9 to the financial statements. There was also a resultant impact on the disclosure of expenditure incurred to repairs and maintenance of property, plant and equipment as disclosed in note 9 to the financial statements for the municipality did not provide supporting evidence for these internal wage costs.

#### Service charges

4. I was unable to obtain sufficient appropriate audit evidence that service charges had been properly accounted for due to the status of the accounting records. The municipality used flat rates and estimates without evidence that the rate charged was appropriate per the tariff policy. The municipality incorrectly levied charges to vacant stands resulting in trade

receivables from exchange transactions, service charges and value-added tax (vat) receivable from exchange transactions being overstated by R4 195 567,96, R3 725 192,59 and R470 375, respectively. In addition, the municipality had in the prior year incorrectly calculated and levied service charges on consumer accounts, which were not corrected, resulting in service charges, interest earned and receivables from exchange being understated by an undeterminable amount. I was unable to confirm service charges by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to service charges stated at R110 971 754 as disclosed in note 22 to the financial statements.

### Trade receivables from exchange transactions

5. I was unable to obtain sufficient appropriate audit evidence that trade receivables from exchange transactions had been properly accounted for due to the status of the accounting records and because the municipality could not confirm the balances owing and the restatements made. The municipality could not provide supporting documents to confirm the validity of consumers, the recalculation of the gross debtor and the restatement of comparative figures. I was unable to confirm the trade receivables from exchange transactions by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to trade receivables stated at R78 429 396 (2018: R55 886 476) in note 13 to the financial statements.

### Investment property

6. The municipality did not split the value of land and buildings for its investment property in accordance with GRAP 16, *Investment property*. The municipality used the valuation roll to value municipal land; however, the value in the valuation roll included values of structures not belonging to the municipality, which resulted in the overstatement of investment property. I was unable to determine the full extent of the misstatement of investment property and the fair value adjustment as it was impracticable to do so.

### General expenses

7. I was unable to obtain sufficient appropriate audit evidence for general expenses due to the status of accounting records and an inadequate system to account for consumables. The municipality could not confirm that items of expenditure had been received and that consumables were used for the stated purpose. In addition, the municipality recognised certain items of expenditure in an incorrect reporting period, resulting in general expenses being understated by R12 492 383 and payables from exchange by R3 184 861 (2018: R9 297 522). I could not confirm general expenses by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to the general expenses stated at R40 598 025 (2018: R39 342 547) as disclosed in note 35 to the financial statements.

### Payables from exchange transactions

8. I was unable to obtain sufficient appropriate audit evidence for payables from exchange transactions due to the poor status of the accounting records. The municipality did not have sufficient evidence to support creditor balances at year-end and suspense accounts were not timeously cleared. In addition, the municipality restated the prior year balance without providing evidence that the whole population had been investigated. I could not confirm the payables from exchange transactions by alternative means. Consequently, I was unable to

determine whether any adjustments were necessary to payables from exchange transactions stated at R273 615 917 (2018: 213 874 058) in note 18 to the financial statements.

### Trade receivables from non-exchange transactions

9. I was unable to obtain sufficient appropriate audit evidence that trade receivables from non-exchange transactions for the current year had been properly accounted for due to the status of the accounting records and because the municipality could not confirm the year-end balances. I was unable to confirm the amounts owing by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to trade receivables stated at R18 016 859 in note 42 to the financial statements.

### Provisions

10. The municipality did not recognise the environmental rehabilitation provision based on the contaminated area as at year-end in accordance with GRAP 19, *Provisions, contingent liabilities and contingent assets*. The provision was calculated using the total landfill area, not only the contaminated area, and without considering monitoring and closure costs. I was unable to determine the full extent of the misstatement in provisions as disclosed in note 17 to the financial statements, as it was impracticable to do so.

### Repairs and maintenance

11. I was unable to obtain sufficient appropriate audit evidence for repairs and maintenance due to the status of accounting records and an inadequate system to account for consumables as the municipality incorrectly classified consumables as repairs and maintenance. The municipality could not confirm that items of expenditure had been received and that consumables were used for the stated purpose. I was unable to confirm the repairs and maintenance by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to repairs and maintenance stated at R4 417 488 in notes 8 and 9 to the financial statements.

### Irregular expenditure

12. The municipality did not include all amounts of irregular expenditure incurred in the current year in note 48 to the financial statements, as required by section 125(2)(d) of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA). The municipality incurred expenditure in contravention of the supply chain management requirements, resulting in irregular expenditure amounting to R30 309 378. In addition, the municipality wrote off irregular expenditure even though the investigations performed were not in accordance with section 32(2) of the MFMA. The investigation report did not indicate whether the municipality suffered a loss or not, nor did it indicate that the municipality could not recover the amount from the responsible official before the amount can be recommended for write-off to council, resulting in irregular expenditure being understated by R8 510 362.

### Unauthorised expenditure

13. The municipality wrote off unauthorised expenditure even though the investigations performed were not in accordance with section 32(2) of the MFMA. The investigation report and the register for unauthorised expenditure did not indicate how the investigation was performed,

resulting in unauthorised expenditure being understated by R266 457 232 in note 46 of the financial statements.

### **Fruitless and wasteful expenditure**

14. The municipality wrote off fruitless and wasteful expenditure even though the investigations performed were not in accordance with section 32(2) of the MFMA. The investigation report recommended the write-off of the amount by the council and recovery from the responsible officials, resulting in fruitless and wasteful expenditure being understated by R20 233 384 in note 47 to the financial statements.

### **Total expenditure**

15. Total expenditure was materially misstated by R1 548 006 due to the cumulative effect of individually immaterial uncorrected misstatements in the following item:

- Indigent support stated at R1 548 006 was overstated by R1 548 006

In addition, I was unable to obtain sufficient appropriate audit evidence and to confirm total expenditure by alternative means:

- Bulk purchases of R1 849 087 as included in the disclosed balance of R44 426 391
- Contracted services of R2 785 181 as included in the disclosed balance of R2 785 181

Consequently, I was unable to determine whether any further adjustment was necessary to total expenditure.

### **Context for the opinion**

16. 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.
17. 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.
18. 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**

19. I draw attention to the matter below. My opinion is not modified in respect of this matter.
20. Note 45 to the financial statements indicates that the municipality incurred a net loss of R40 952 720 during the year ended 30 June 2019 and that, as of that date, the municipality's

current liabilities exceeded its current assets by R154 463 915. The municipality has been deducting pension, medical aid and pay-as-you-earn from employees' salaries, but was unable to pay over R3 067 489 (2018: R11 979 826) of these amounts to the relevant third parties as disclosed in note 49. In addition, the municipality owed Eskom R179 133 293 (2018: R135 354 844) and Bloemwater R1 717 800 (2018: R293 770) as at 30 June 2019, which amounts are long overdue. These events or conditions, along with other matters as set forth in note 45, 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**

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

### **Restatement of corresponding figures**

22. As disclosed in notes 43 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 losses**

23. As disclosed in note 51 to the financial statements, water distribution losses of R1 573 394 (2018: R1 910 291) and electricity distribution losses of R14 481 826 (2018: R13 348 706) were incurred, which represent 37% (2018: 47%) and 34% (2018: 31%) of the total water and electricity purchased, respectively. These losses incurred by the municipality were mainly due to illegal connections, leakages, burst water pipes, line losses, tampering and theft.

### **Material impairments**

24. As disclosed in note 4, 5, 13 and 42 to the financial statements, consumers and other receivables were impaired by R375 311 670 (2018: R291 984 600).

## **Other matters**

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

### **Unaudited disclosure notes**

26. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose the 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 thereon.

### **Unaudited supplementary schedule**

27. The supplementary information set out on pages ... to ... 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 thereon.

## **Responsibilities of the accounting officer for the financial statements**

28. 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 the Division of Revenue Act of South Africa, 2018 (Act No. 1 of 2018) (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.
29. In preparing the financial statements, the accounting officer is responsible for assessing the Mantsopa 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**

30. 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.
31. 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**

32. 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 selected development priorities presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
33. 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.
34. 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:

Development priorities	Pages in the annual performance report
KPA 1 – Basic services and infrastructure development	x – x

35. 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.

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

### **KPA 1 – Basic service delivery and infrastructure development**

#### **Weekly collection of refuse in all towns and townships**

37. The planned target for this indicator was not specific in clearly identifying the nature and required level of performance and measurability.

#### **Percentage of progress made on construction of toilet top structures at Manyatseng Ext. 9**

38. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of the target. This was due to limitations on the scope of my work. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement of 100% for progress made on construction of toilet top structures at Manyatseng Ext. 9.

### **Other matters**

39. I draw attention to the matters below.

#### **Achievement of planned targets**

40. 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 and reliability of the reported performance information in paragraphs 37 to 38 of this report.

#### **Adjustment of material misstatements**

41. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information of KPA 1 – Basic services and infrastructure development. 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.

### Introduction and scope

42. 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.
43. The material findings on compliance with specific matters in key legislations are as follows:

#### Annual financial statements and annual report

44. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1). Material misstatements of current, non-current assets, liabilities, and revenue, expenditure 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.

#### Asset management

45. An effective system of internal control over assets (including an asset register) was not in place, as required by section 63(2)(c) of the MFMA.
46. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2) (a) of the MFMA.

#### Consequence management

47. Some of the losses resulting from unauthorised expenditure were written off as irrecoverable without being certified by council as irrecoverable, in contravention of section 32(2)(a)(ii) of the MFMA.
48. Some of the losses resulting from irregular expenditure were written off as irrecoverable without being certified by council as irrecoverable, in contravention of section 32(2)(b) of the MFMA.
49. Some of the losses resulting from fruitless and wasteful expenditure were written off as irrecoverable without being certified by council as irrecoverable, in contravention of section 32(2)(b) of the MFMA.

#### Expenditure management

50. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
51. An adequate management, accounting and information system which recognised expenditure when it was incurred was not in place, as required by section 65(2)(b) of the MFMA.
52. Reasonable steps were not taken to prevent irregular, unauthorised and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA. The expenditure disclosed does not

reflect the full extent of the, irregular, unauthorised and fruitless and wasteful expenditure incurred as indicated in the basis for qualification paragraphs.

### Revenue management

53. An adequate management, accounting and information system which accounts for revenue / debtors was not in place, as required by section 64(2)(e) of the MFMA.
54. An effective system of internal control for debtors / revenue was not in place, as required by section 64(2)(f) of the MFMA.

### Human resource management

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

### Conditional grants

56. Performance in respect of programmes funded by the Municipal Infrastructure Grant (MIG) and Water Services Infrastructure Grant (WSIG) was not evaluated within two months after the end of the financial year, as required by section 12(5) of Dora.
57. The financial management grant was not spent for its intended purposes in accordance with the applicable grant framework, as required by section 17(1) of the Division of Revenue Act (Act 1 of 2018).

<h3>Other information</h3>
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58. 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.
59. 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.
60. 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.
61. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, and 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

62. 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.
63. Management did not implement proper record keeping for financial statements, reporting of performance information and compliance with legislation. This resulted in information not being submitted timeously for audit and some information submitted not being sufficient to support the information audited. Material limitation misstatements were identified in the financial, reporting of performance information and compliance testing, some of which were corrected. Those not corrected resulted in the entity receiving a qualified audit opinion.
64. Management did not in all instances implement daily and monthly processing and reconciliation of transactions, including the clearing of suspense accounts. This resulted in the financial statements submitted for audit excluding some of the supporting schedules. In addition, differences were identified between the financial statements submitted for audit and the supporting schedules, some of which could be corrected.
65. Management did not in all instances effectively review and monitor the municipality's compliance with legislation due to their slow response in addressing the drivers of the compliance findings identified in the prior year. As a result, repeat instances of material non-compliance, which could have been prevented, were identified.
66. The internal audit function of the municipality is not adequately resourced and capacitated for the nature, size and complexity of the municipality. This in turn affected the efficiency and effectiveness of the audit committee which could not perform its duties per the acceptable norms and standards.
67. Management did not prepare an IT governance framework that supports and enables the business, delivers value and improves performance, as the current plan is not in line with the municipality's needs. Resources within the IT environment are not trained to meet the level of competence required for their duties, as training or skills gap analysis was not performed, resulting in significant internal control deficiencies in user access management, security management and service continuity. In addition, similar findings were raised in the previous audits.
68. Management relied on work performed by consultants in the preparation of the annual financial statements. However, work performed by the consultants was not thoroughly reviewed by management to assess the accuracy and completeness thereof, resulting in material misstatements being identified in the annual financial statements.

*Auditor-General*

Bloemfontein

08 April 2020



**A U D I T O R - G E N E R A L**  
**S O U T H A F R I C A**

*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 related to events or conditions that may cast significant doubt on the Mantsopa 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 operating 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
  - obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group to express an opinion on the consolidated financial statements. I am responsible for the direction, supervision and performance of the group audit. I remain solely responsible for my audit opinion.

### **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.