

Report of the auditor-general to the Eastern Cape Provincial Legislature and council on the Raymond Mhlaba Local Municipality

Report on the audit of the consolidated and separate financial statements

Qualified opinion

1. I have audited the consolidated and separate financial statements of the Raymond Mhlaba Local Municipality set out on pages ... to ..., which comprise the consolidated and separate statement of financial position as at 30 June 2020, consolidated and separate statement of financial performance, consolidated and separate statement of changes in net assets, consolidated and separate cash flow statement and consolidated and separate statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the consolidated and separate financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the effects of the matters described in the basis for qualified opinion section of this auditor's report, the consolidated and separate financial statements present fairly, in all material respects, the consolidated and separate financial position of the Raymond Mhlaba Local Municipality as at 30 June 2020, and its consolidated and separate financial performance and consolidated and separate 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 56 of 2003 (MFMA) and Division of Revenue Act 16 of 2019 (Dora).

Basis for qualified opinion

Investment property

3. The municipality did not correctly classify their immovable property in accordance with GRAP 16, *Investment properties* and GRAP 17, *Property, plant and equipment*. Investment property was incorrectly classified as property, plant and equipment and property, plant and equipment was incorrectly classified as investment property. Consequently, investment property as disclosed in the consolidated and separate financial statements was overstated by R6,8 million and property, plant and equipment as disclosed in the consolidated and separate financial statements was understated by the same amount.

Property, plant and equipment – Work in progress

4. I was unable to obtain sufficient appropriate audit evidence for work in progress as management had not assessed the long-outstanding work in progress for impairment, and physical inspection of the projects revealed that there were impairment indicators. I was unable to confirm the value of the impairment by alternative means.
5. In addition, management could not provide supporting evidence for the previous year adjustments made to work in progress in the current financial year. I was unable to confirm the restatement by alternative means. As a result, I was unable to determine whether any

adjustment was necessary to work in progress of R218 million (2019: R207 million) in note 9.1 to the consolidated and separate financial statements and the prior period adjustment to property, plant and equipment in note 46.4 to the consolidated and separate financial statements.

Government grants and subsidies – capital

6. The municipality did not account for revenue from government grants and subsidies – capital in accordance with the requirements of GRAP 23, *Revenue from non-exchange transactions*, as revenue that accrued in the previous year was incorrectly recorded in revenue of the current financial year. As a result, government grants and subsidies – capital was overstated by R7,3 million and accumulated surplus was understated by the same amount in the consolidated and separate financial statements.

Bulk purchases

7. I was unable to obtain sufficient appropriate audit evidence to confirm that bulk purchases were actually received by the municipality due to the lack of adequate systems and processes in place to verify the units purchased. I could not confirm the expenditure on bulk purchases by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to bulk purchases, stated at R65,7 million (2019: R59,3 million) in the consolidated and separate financial statements and the related electricity distribution losses of R13,6 million (2019: R25,0 million) as disclosed in note 51.1 to the consolidated and separate financial statements.

Other expenditure

8. The municipality did not account for other expenditure in accordance with the requirement of GRAP 1, *Presentation of financial statements*, as expenditure that accrued in the previous year was incorrectly recorded in current year expenditure. Amounts were also identified that did not agree with the supporting documents. As a result, other expenditure was overstated by R18,9 million, accumulated surplus was overstated by R21,2 million and payables from exchange transactions overstated by R2,3 million in the consolidated and separate financial statements.

Irregular expenditure

9. The municipality did not have proper systems in place to identify and disclose all irregular expenditure as required by section 125(2)(d) of the MFMA. This expenditure resulted from payments made in contravention of the supply chain management (SCM) regulations. I was unable to confirm the amount of irregular expenditure by alternative means. It was impracticable to determine the full extent of the understatement of irregular expenditure, disclosed at R261,4 million and R259,5 million in note 50.3 to the consolidated and separate financial statements, respectively.

Prior period adjustments – Payables from exchange transactions

10. The municipality did not recognise all outstanding amounts meeting the definition of a liability in accordance with GRAP 1, *Presentation of financial statements* as part of the prior period adjustment in note 46.6 to the consolidated and separate financial statements. The prior period

adjustment for payables from exchange transactions did not include all the required restatements, as expenditure incurred in the previous year was incorrectly included in the current year. I was unable to determine the full extent of the understatement of the payables from exchange transactions corresponding figure in the financial statements, as well as the prior period adjustment disclosed in note 46.6 to the consolidated and separate financial statements as it was impracticable to do so.

Context for the opinion

11. 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 consolidated and separate financial statements section of this auditor's report.
12. 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.
13. 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 financial sustainability

14. I draw attention to the matter below. My opinion is not modified in respect of this matter.
15. I draw attention to note 62 to the consolidated and separate financial statements, which indicates that the municipality's current liabilities at 30 June 2020 exceeded the current assets. This situation, along with other matters as set forth in note 62, indicates the existence of a material uncertainty that may cast significant doubt on the municipality's ability to continue as a going concern.

Emphasis of matter

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

Fruitless and wasteful expenditure

17. Fruitless and wasteful expenditure of R78,5 million and R77,6 million (2019: R58,8 million and R58,3 million) that had accumulated over a number of years and had not been recovered, written off or condoned, is disclosed in note 50.2 to the consolidated and separate financial statements, respectively. Fruitless and wasteful expenditure of R19,7 and R19,4 million (2019: R16,1 million and R16 million) incurred during the current year is included in the amount disclosed in the consolidated and separate financial statements, respectively, and is a result of penalties levied by the South African Revenue Service and interest charged on overdue accounts.

Unauthorised expenditure

18. Unauthorised expenditure of R234,1 million (2019: R234,1 million) that had accumulated over a number of years and had not been recovered, written off or condoned, is disclosed in note 50.1 to the consolidated and separate financial statements.

Impairments

19. As disclosed in notes 3 and 4 to the consolidated and separate financial statements respectively, material losses of R420,3 million and R420 million (2019: R332,9 million and R332,6 million) were incurred as a result of the allowance for impairment on receivables from exchange transactions and non-exchange transactions.

Other matters

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

Unaudited disclosure note

21. 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 consolidated and separate financial statements. This disclosure requirement did not form part of the audit of the consolidated and separate financial statements and, accordingly, I do not express an opinion on it.

Unaudited supplementary schedules

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

Responsibilities of the accounting officer for the financial statements

23. The accounting officer is responsible for the preparation and fair presentation of the consolidated and separate financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA, and for such internal control as the accounting officer determines is necessary to enable the preparation of consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.
24. In preparing the consolidated and separate financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the consolidated and separate financial statements

25. My objectives are to obtain reasonable assurance about whether the consolidated and separate 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 consolidated and separate financial statements.

26. A further description of my responsibilities for the audit of the consolidated and separate financial statements is included in the annexure to this auditor’s report.

Report on the audit of the annual performance report

Introduction and scope

27. In accordance with the Public Audit Act 25 of 2004 (PAA) and the general notice issued in terms thereof, I have a responsibility to report on the usefulness and reliability of the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report. I performed procedures to identify material findings but not to gather evidence to express assurance.
28. 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/measures included in the planning documents. My procedures do not examine whether the actions taken by the municipality enabled service delivery. My procedures also do 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.
29. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected development priority presented in the municipality’s annual performance report for the year ended 30 June 2020:

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

30. 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.
31. The material findings in respect of the usefulness and reliability of the selected development priority are as follows:

Various indicators

32. The source information for measuring the planned indicator was not clearly defined and related systems and processes were not adequate to enable consistent measurement and reliable reporting of performance against the predetermined indicator definitions. As a result, limitations were placed on the scope of my work and I was unable to audit the reliability of the achievement of the following indicators reported against their respective targets in the annual performance report:

Indicator no.	KPI name	Target
KPI 6	Number of refuse removal collected from formal households	96
KPI 12	% of new connections and reconnections completed	100%
KPI 14	Number of storm water draining maintained	100
KPI 15	% MIG capital project implemented	100%

Various indicators

33. The planned targets were not consistent with the actual achievements reported in the Service Delivery Budget Implementation Plan (SDBIP) for the following indicators:

Indicator no.	KPI name	Planned target as per SDBIP	Reported actual achievement per annual performance report
KPI 6	Number of refuse removal collected from formal households	96	Not achieved: 88 monthly reports were developed for the review on waste removal
KPI 11	Number of illegal connection audits conducted	12	Achieved: 17 electricity audits were conducted
KPI 13	% of INEP projects implemented	100%	Not achieved: 4 projects registered under INEP, all still under construction towards completion; R85 128 000 had been spent as at the year-end, which represents 70,94% of overall expenditure in contrast to work done
KPI 15	% MIG capital project implemented	100%	Not Achieved: 25% of overall MIG projects have been completed as at year end

Other matter

34. I draw attention to the matter 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 32 to 33 of this report.

Report on the audit of compliance with legislation

Introduction and scope

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

Financial statements, performance report and annual report

38. The consolidated and separate 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 identified by the auditors in the submitted consolidated and separate financial statements were not adequately corrected and the supporting records could not be provided subsequently, which resulted in the consolidated and separate financial statements receiving a qualified audit opinion.
39. The 2018-19 annual report was not tabled in the municipal council after the end of the financial year, as required by section 127(2) 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. An adequate management, accounting and information system that recognised expenditure when it was incurred and accounted for creditors was not in place, as required by section 65(2)(b) of the MFMA.
42. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The expenditure disclosed does not reflect the full extent of the irregular expenditure incurred as indicated in the basis for qualification paragraph. The majority of the disclosed irregular expenditure was caused by non-compliance with SCM regulations.
43. Reasonable steps were not taken to prevent fruitless and wasteful expenditure of R19,7 million, as disclosed in note 50.2 to the consolidated and separate 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 on late payments.

Asset management

44. 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.

Strategic planning and performance management

45. The performance management system and related controls were inadequate as they did not describe how the performance planning, monitoring, measurement, review and reporting processes should be conducted and managed, as required by municipal planning and performance management regulation 7(1).

Consequence management

46. Unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure incurred by the municipality were not investigated to determine whether any person was liable for the expenditure, as required by section 32(2)(a) and (b) of the MFMA.

Procurement and contract management

47. Some goods and services with a transaction value below R200 000 were procured without obtaining the required price quotations, in contravention of SCM regulation 17(1)(a) and (c). Similar non-compliance was also reported in the prior year.
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). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).
49. Some contracts were awarded to bidders based on points given for criteria that differed from those stipulated in the original invitation for bidding and quotations, in contravention of SCM regulations 21(b) and 28(1)(a)(i) and the Preferential Procurement Regulations. Similar non-compliance was also reported in the prior year.
50. The performance of some contractors or providers was not monitored monthly, as required by section 116(2)(b) of the MFMA. This non-compliance was also identified in the procurement processes for Turnkey Service for the design and upgrade of electrical infrastructure in Adelaide and paving of Takalani, Tyoks and Mpolweni internal streets ward.
51. The contract performance and monitoring measures and methods were not sufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA.
52. Awards were made to providers who were in the service of other state institutions or whose directors / principal shareholders were in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulation 44. Similar awards were identified in the previous year and no effective steps were taken to prevent or combat the abuse of the SCM process, as required by SCM regulation 38(1).

Other information

53. 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 consolidated and separate 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.
54. My opinion on the consolidated and separate financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion on it.
55. 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 consolidated and separate financial statements and the selected development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
56. 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.
57. I have nothing to report in this regard.

Internal control deficiencies

58. I considered internal control relevant to my audit of the consolidated and separate 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 report and the findings on compliance with legislation included in this report.
59. Leadership has not instituted all the disciplines necessary to enable oversight and monitoring that promotes efficiency and effectiveness in financial management, service delivery reporting and compliance with laws and regulations. This did not set the correct tone in building a high performance environment that promotes accountability as well as establishing a culture of ethical performance.
60. The municipality does not have a proper record management system that provides for the maintenance of information that supports the consolidated and separate financial statements and reported performance information. This was evidenced during the audit process when requested information was either not submitted for audit purposes or was not submitted within the agreed timeframes, resulting in significant delays in the audit process. Management did not design or implement daily and monthly controls to ensure that the consolidated and separate financial statements and reported performance information were supported by reliable and credible supporting documentation.

61. The lack of appropriately approved policies and procedures governing the operations of the municipality led to numerous instances of material non-compliance.
62. Leadership responded slowly in terms of applying consequence management as the cases of irregular and fruitless and wasteful expenditure reported in the current year were recurrences from previous years.
63. The internal audit and audit committee's recommendations were not adequately implemented by management. This limited the effectiveness of these structures in improving the municipality's control environment.

Auditor General

East London

31 March 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 consolidated and separate 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 consolidated and separate financial statements as described in this auditor’s report, I also:
 - identify and assess the risks of material misstatement of the consolidated and separate 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 consolidated and separate financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists relating to events or conditions that may cast significant doubt on the ability of the Raymond Mhlaba Local Municipality to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor’s report to the related disclosures in the consolidated and separate financial statements about the material uncertainty or, if such disclosures are inadequate, to modify my opinion on the consolidated and separate 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 consolidated and separate financial statements, including the disclosures, and determine whether the consolidated and separate 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, the actions taken to eliminate threats or the safeguards applied.