

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

Report on the audit of the financial statements

Disclaimer of opinion

1. I was engaged to audit the financial statements of the Ingquza Hill Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2020, 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. I do not express an opinion on the financial statements of the municipality. Because of the significance of the matters described in the basis for disclaimer of opinion section of this auditor's report, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.

Basis for disclaimer of opinion

Property plant and equipment

3. The municipality did not account for property, plant and equipment in accordance with the South African Standards of Generally Recognised Accounting Practices (SA Standards of GRAP) 17, *Property, plant and equipment*. Assets owned by the municipality were not recorded in the financial statements and certain assets were not recorded at correct values. Consequently, property, plant and equipment was overstated by R3,1 million (2019: R20,7 million). Additionally, there was an impact on the surplus for the period and on the accumulated surplus in the financial statements.
4. I was also unable to obtain sufficient appropriate audit evidence for property, plant and equipment due to the status of accounting records and not being able to physically verify certain assets. I was unable to confirm the property, plant and equipment by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to property, plant and equipment, stated at R696,2 million (2019: R649,1 million) in note 4 to the financial statements, and depreciation, stated at R53,2 million (2019: R47,8 million) in note 42 to the financial statements.

Public contributions and donations

5. The municipality did not account for public contributions and donations as required by GRAP 23, *Revenue from non-exchange transactions*. Donations received were not recorded at the fair value as at the date of acquisition. Consequently, public contributions and donations disclosed in note 41 to the financial statements was overstated by R4,5 million, while surplus and accumulated surplus were overstated by the same amount.

Government grants and subsidies

6. During 2019, I was unable to obtain sufficient appropriate audit evidence for government grants and subsidies and to confirm the expenditure by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to government grants and subsidies stated at R301,6 million. My audit opinion on the financial statements for the prior was modified accordingly. My opinion on the current year financial statements was also modified because of the possible effect of this matter on the comparability of the government grants and subsidies for the current period.

Cash and cash equivalents

7. I was unable to obtain sufficient appropriate audit evidence for cash and cash equivalents due to the status of accounting records. I was unable to confirm this balance by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to cash and cash equivalents, stated at R138 million (2019: R90,2 million) in note 11 to the financial statements.

Receivables from non-exchange transactions

8. I was unable to obtain sufficient appropriate audit evidence for receivables from non-exchange transactions due to the status of the accounting records. I was unable to confirm this balance by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to receivables from non-exchange transactions stated at R29,3 million (2019: R14,8 million) in note 8 to the financial statements, and the increase in provision for impairment stated at R6,2 million (2019: R15,5 million) in the statement of financial performance.

Unspent conditional grants and receipts

9. I was unable to obtain sufficient appropriate audit evidence for unspent conditional grants and receipts due to the status of accounting records. I could not confirm the amounts by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to unspent conditional grants and receipts of R17,1 million (2019: R4,4 million) disclosed in note 14 to the financial statements.

Payables from exchange transactions

10. Included in payables from exchange transactions are trade payables and prepaid income. I was unable to obtain sufficient appropriate audit evidence for these balances due to the status of the accounting records. I was unable to confirm these balances by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to trade payables, stated at R12,4 million (2019: R6,6 million) and prepaid income, stated at R4 million (2019: R4 million) in note 13 to the financial statements.

Receivables from exchange transactions

11. I was unable to obtain sufficient appropriate audit evidence for receivables from exchange transactions due to the status of the accounting records. I was unable to confirm this balance by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to receivables from exchange transactions stated at R10,6 million (2019: R10,6 million) in note 7 to the financial statements, and the increase in provision for impairment stated at R6,2 million (2019: R15,5 million) in the statement of financial performance.

VAT receivable

12. I was unable to obtain sufficient appropriate audit evidence for VAT receivable due to the status of accounting records. I was unable to confirm this balance by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to VAT receivables, stated at R6,8 million (2019: nil) in note 10 to the financial statements.

General expenses

13. The municipality did not account for general expenses as required by GRAP 1, *Presentation of financial statements*, as expenditure was not recorded in the period it was incurred and was not recorded in the correct accounts. Consequently, general expenditure disclosed in the statement of financial performance and note 26 to the financial statements was understated by R7,5 million, while surplus and accumulated surplus were overstated by the same amount. In addition, I was unable to obtain sufficient appropriate audit evidence for general expenses due to the status of accounting records. I could not confirm the amounts by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to general expenses, stated at R65,5 million (2019: R55,1 million) in note 26 to the financial statements.

Remuneration of councillors

14. The municipality did not account for remuneration of councillors as required by GRAP 1, *Presentation of financial statements*, as the expenditure was not recorded at correct values. Consequently, remuneration of councillors disclosed in note 23 to the financial statements was overstated by R5,4 million while surplus and accumulated surplus was understated by the same amount.

Financial instruments disclosure

15. The municipality did not correctly disclose financial instruments as required by GRAP 104, *Financial Instruments*. The amounts disclosed as financial instruments did not agree with the amounts on the statement of financial position and the municipality did not account for the effect of discounting in the financial statements. Consequently, financial instruments as disclosed in note 30 to the financial statements were materially misstated.

Irregular expenditure

16. I was unable to obtain sufficient appropriate audit evidence for irregular expenditure incurred and condoned during the year as the municipality did not maintain accurate and complete records. I could not confirm the amounts by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to irregular expenditure incurred, stated at R1,4 million (2019: R7,5 million) and irregular expenditure condoned, stated at R7,3 million in note 36 to the financial statements.

Contingencies

17. The municipality did not account for contingent liabilities as required by GRAP 19, *Provisions, contingent liabilities and contingent assets*. The municipality did not disclose all the cases that met the definition of contingent liabilities in the financial statements. Consequently, contingent liabilities disclosed in note 31 to the financial statements was understated by R13,5 million.
18. I was also unable to obtain sufficient appropriate audit evidence for contingencies in the prior year due to the status of accounting records. I was unable to confirm these contingencies by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to the corresponding figures of contingencies disclosed in note 31 to the financial statements.

Cash flow statements

19. The municipality did not prepare a cash flow statement in accordance with GRAP 2, *Cash flow statements*. The municipality incorrectly calculated the net cash flows from operating activities and the net cash flows from investing activities in the current and prior year. Consequently, the cash flow statement for the current and prior year was materially misstated.

Statement of comparison of budget and actual amounts

20. The municipality did not prepare the statement of comparison of budget and actual amounts in accordance with GRAP 24, *Presentation of budget information in financial statements*. Material differences were identified between the budget amounts disclosed and the approved budget, and differences were identified between the actual amounts disclosed in the statement and amounts presented on the face of the financial statements. Consequently, the statement of comparison of budget and actual amounts was materially misstated. Additionally, an explanation of material differences between the budget and actual amounts was not disclosed or referred to in the notes to the financial statements.

Prior period errors

21. The municipality did not correctly disclose prior period errors as required by GRAP 3, *Accounting policies, estimates and errors*. The nature and the amount of the correction for each financial statement item affected and the amount of the correction at the beginning of the earliest previous period were not disclosed. In addition, I was unable to obtain sufficient appropriate audit evidence for the prior period errors disclosed as the supporting information was not provided. I was unable to confirm these disclosures by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to the prior period errors disclosed in note 44 to the financial statements.

Related parties

22. The municipality did not disclose the remuneration of management in accordance with GRAP 20, *Related-party disclosures*. The municipality did not disclose the remuneration of all the directors and the audit committee members of the municipality. Consequently, remuneration of management disclosed in note 22 to the financial statements was understated by R5,3 million.

Additional disclosure in terms of the Municipal Finance Management Act

23. The municipality did not correctly disclose the total amounts paid in audit fees, taxes, levies, duties and pension, and medical aid contributions, as required by section 125(1)(c) of the Municipal Finance Management Act 56 of 2003 (MFMA). Consequently, the disclosures in note 45 to the financial statements were misstated as follows:

- Audit fees, stated at R2,8 million, was understated by R1 million.
- Paye, UIF and SDL, stated at R22,1 million, was understated by R3,7 million.
- Medical aid, stated at R10,8 million, was overstated by R5,5 million.
- Pension and provident fund, stated at R14,2 million, was overstated by R2,7 million.

Unauthorised expenditure

24. The municipality did not include unauthorised expenditure in the notes to the financial statements, as required by section 125(2)(d) of the MFMA. This was due to payments made in excess of the approved budget. Consequently, unauthorised expenditure was understated by R10,9 million.

Commitments

25. The municipality did not account for commitments in terms of GRAP 17, *Property, plant and equipment*. The municipality did not disclose commitments on capital projects in progress. Consequently, commitments was understated by R59,9 million in the notes to the financial statements.

26. I was also unable to obtain sufficient appropriate audit evidence for commitments in the prior year due to the status of accounting records. I was unable to confirm these commitments by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to the financial statements.

Accumulation of immaterial uncorrected misstatements

Total revenue

27. In addition to the individually material uncorrected misstatement on government grants and subsidies during 2019, revenue was materially misstated by R3,5 million due to the cumulative effect of individually immaterial uncorrected misstatements, which had an impact of the corresponding figures for the current year. My audit opinion on the financial statements for the prior year was modified accordingly. My opinion on the current year financial statements was also modified because of the possible effect of the matters below on the comparability for the current period:

- Property rates, stated at R22,4 million, was overstated by R2,8 million.
- Interest received, stated at R8,5 million, was overstated by R0,7 million.

Total expenditure

28. In addition to the individually material uncorrected misstatement on general expenses during 2019, expenditure was materially misstated by R3 million due to the cumulative effect of individually immaterial uncorrected misstatements, which had an impact of the corresponding figures for the current year. My audit opinion on the financial statements for the prior year was modified accordingly. My opinion on the current year financial statements was also modified because of the possible effect of the matters below on the comparability for the current period:

- Loss on disposal of assets and liabilities, stated at R2,5 million, was understated by R1,5 million.
- Employee-related costs, stated at R116 million, was understated by R1 million.
- Repairs and maintenance, stated at R11,3 million, was understated by R0,8 million.
- Councillors' remuneration, stated at R22,6 million, was overstated by R0,2 million.

Emphasis of matter

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

Underspending of the conditional grant

30. As disclosed in note 20 to the financial statements, the municipality materially underspent the municipal infrastructure grant by R12,7 million.

Other matters

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

Unaudited disclosure note

32. 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.

Withdrawal from the audit engagement

33. Due to the limitation imposed on the scope of the audit by management, I have disclaimed my opinion on the financial statements. Were it not for the legislated requirement to perform the audit of the municipality, I would have withdrawn from the engagement in terms of the International Standards on Auditing (ISAs).

Responsibilities of the accounting officer for the financial statements

34. 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 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.
35. In preparing the financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

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

36. My responsibility is to conduct an audit of the financial statements in accordance with the ISAs and to issue an auditor's report. However, because of the matters described in the basis for disclaimer of opinion section of this auditor's report, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these financial statements.
37. 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 the other ethical requirements relevant to my audit of the financial statements in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.

Introduction and scope

38. 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 key performance areas presented in the annual performance report. I performed procedures to identify material findings but not to gather evidence to express assurance.

39. My procedures address the usefulness and reliability of the reported performance information, which must be based on the municipality's approved performance-planning documents. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures do not examine whether the actions taken by the municipality enabled service delivery. My procedures also 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.

40. 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 key performance area presented in the municipality's annual performance report for the year ended 30 June 2020:

Key performance area (KPA)	Pages in the annual performance report
KPA 1 – basic services delivery	x – x

41. 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.

42. I did not identify material findings on the usefulness and reliability of the reported performance information for KPA 1 – basic services delivery.

Other matter

43. I draw attention to the matter below.

Achievement of planned targets

44. Refer to the annual performance report on pages ... to ... for information on the achievement of planned targets for the year.

Report on the audit of compliance with legislation

Introduction and scope

45. 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.

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

Annual financial statements

47. 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 identified by the auditors in the submitted financial statements were not adequately corrected and the supporting records could not be provided subsequently, which resulted in the financial statements receiving a disclaimer of audit opinion.

Revenue management

48. An adequate management, accounting and information system that accounts for debtors was not in place, as required by section 64(2)(e) of the MFMA.

49. An effective system of internal control for debtors was not in place, as required by section 64(2)(f) of the MFMA.

50. Revenue due to the municipality was not calculated monthly, as required by section 64(2)(b) of the MFMA.

51. Interest was not charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.

Expenditure management

52. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The full extent of the irregular expenditure could not be quantified as indicated in the basis for qualification paragraph.

53. Expenditure was incurred in excess of the approved budget, in contravention of section 87(8) of the MFMA.

54. An adequate management, accounting and information system that recognised expenditure when it was incurred and accounted for payments made was not in place, as required by section 65(2)(b) of the MFMA.

Strategic planning and performance management

55. The service delivery and budget implementation plan for the year under review did not include monthly revenue projections by source of collection and the monthly operational and capital expenditure by vote, as required by section 1 of the MFMA.

Consequence management

56. Irregular expenditure incurred by the municipality was not investigated to determine whether any person was liable for the expenditure, as required by section 32(2)(b) of the MFMA.
57. The condonation of irregular expenditure of R7,2 million was not approved by the appropriate relevant authority, as required by sections 1 and 170 of the MFMA.
58. I was unable to obtain sufficient appropriate audit evidence that losses resulting from irregular expenditure were recovered from the liable person, as required by section 32(2) of the MFMA. This was because proper and complete records were not maintained as evidence to support the investigations into irregular expenditure.
59. I was unable to obtain sufficient appropriate audit evidence that losses resulting from irregular expenditure were written off as irrecoverable after being certified by council as irrecoverable, in contravention of section 32(2)(b) of the MFMA.
60. I was unable to obtain sufficient appropriate audit evidence that losses resulting from irregular expenditure were certified by council as irrecoverable after having conducted an investigation to determine the recoverability of the expenditure, in contravention of section 32(2)(b) of the MFMA.
61. I was unable to obtain sufficient appropriate audit evidence that cases of irregular expenditure that constituted a criminal offence were reported to the South African Police Service, as required by section 32(6) of the MFMA.

Asset management

62. An adequate management, accounting and information system that accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.
63. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.
64. Capital assets were disposed of without the municipal council having, in a meeting open to the public, decided on whether the assets were still needed to provide the minimum level of basic municipal services as required by section 14(2)(a) of the MFMA.

Other information

65. 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 key performance area presented in the annual performance report that has been specifically reported in this auditor's report.
66. 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 on it.
67. 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 key performance areas presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
68. 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

69. 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 disclaimer of opinion, and the findings on compliance with legislation included in this report
70. Leadership of the municipality did not adequately discharge its oversight responsibilities with regard to implementing and monitoring internal controls to ensure sound financial management and compliance with legislation. This resulted in numerous repeat findings in the financial statements and the audit of compliance with laws and regulations.
71. Management did not implement daily and monthly financial controls to ensure that the financial statements were supported by accurate and complete underlying records.
72. The municipality did not implement proper record management practices to ensure that information supporting the financial statements was readily available when requested for audit. As a result, sufficient and appropriate audit evidence was not obtained for the majority of the disclosures in the financial statements.

73. Non-compliance with legislation could have been prevented had compliance been properly reviewed and monitored.

Auditor General
East London

13 April 2021



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence