

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

## Report on the audit of the financial statements

### Qualified opinion

1. I have audited the financial statements of the King Sabata Dalindyebo Local Municipality set out on pages xx to xx, which comprise the statement of financial position as 30 June 2020, statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the effects of the matters described in the basis for qualified opinion section of this auditor's report, the financial statements present fairly, in all material respects, the financial position of the King Sabata Dalindyebo Local Municipality as at 30 June 2020, 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, 2019 (Act No.16 of 2019) (Dora).

### Basis for qualified opinion

#### Receivables from Exchange transactions

3. The municipality did not have adequate controls to ensure that rental is only charged on properties owned by the municipality. This resulted in consumer debtors-rentals being overstated by R21,8 million (2018-19: R23,5 million). This also impacted on the surplus for the period and on the accumulated surplus. In addition, I was unable to obtain sufficient appropriate audit evidence for the amounts disclosed for consumer debtors – rental in note 4 to the financial statements. I could not confirm the consumer debtors – rentals by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the consumer debtors – rentals. stated at R165,3 million (2018-19: R145,6 million) in note 4 to the financial statements.

#### General expenses

4. The municipality did not have adequate processes in place to ensure that all general expenses in the financial statements were recorded in terms of GRAP 1, Presentation of financial statements. Subsistence and travelling was incorrectly disclosed as repairs and maintenance. As a result, repairs and maintenance was overstated and subsistence and travelling was understated by R13,8 million as disclosed in note 40 to the financial statements.

## Corresponding figures

5. I was unable to obtain sufficient appropriate audit evidence regarding the following items in the corresponding figures, which had a cumulative effect on total revenue and expenditure in the statement of financial performance:

- Bulk purchases disclosed as R257,3 million.
- Fines, penalties and forfeits disclosed as R2,1 million.

In addition, revenue from exchange was overstated by R5,4 million in the corresponding figures.

I was unable to confirm total revenue and expenditure by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the corresponding figures for revenue and expenditure as disclosed in the statement of financial performance.

## 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 Code of ethics for professional accountants and parts 1 and 3 of the International Code of Ethics for Professional Accountants (including International Independence Standards) of the International Ethics Standards Board for Accountants (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. I draw attention to note 58 to the financial statements which indicates that the municipality is experiencing financial difficulties as its current liabilities exceed its current assets. The events or conditions disclosed in note 58 together with other matters set forth in the same note indicate that material uncertainty exists that may cast significant doubt on the municipality's ability to continue to fund its existing level of operations.



## **Emphasis of matters**

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

### **Material electricity distribution losses**

12. As disclosed in note 51 to the financial statements, material electricity distribution losses of R48.5 million was incurred, which represents 16.9% of total electricity purchased, this was mostly due to illegal connections.

### **Significant uncertainty**

13. As disclosed in note 46 to the financial statements, the municipality is the defendant in a number of lawsuits. The municipality is opposing the claims and the ultimate outcome of the matters cannot presently be determined, however, provision has been made in the financial statements for any liabilities that may result.

### **Impairment loss**

14. As disclosed in notes 4 and 5 to the financial statements, cumulative debt impairments of R380,4 million (2018-19: R307,8 million) and R318,1 million (2018-19: R273,7 million) were made to receivables from exchange and non-exchange transactions respectively as a result of slow recovery from debtors.

### **Restatement of corresponding figures**

15. As disclosed in note 57 to the financial statements, the corresponding figures for 30 June 2019 were restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2020.

## **Other matter**

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

### **Unaudited disclosure notes**

17. 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.

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

18. 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.

19. 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**

20. 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.

21. 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**

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

23. 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.

24. 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:

<b>Development priority</b>	<b>Pages in the annual performance report</b>
KPA 1 – Basic Service Delivery and Infrastructure Development	x – x



25. 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.

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

### Basic Service and Infrastructure Development

#### Various indicators

27. The planned targets for the indicators listed below were not specific in clearly identifying the nature and required level of performance.

Indicator Description	Planned target
3.1.1. Number of surfaced streets to be repaired and maintained	80 surfaced streets repaired and maintained
3.1.2. Number of meters of Storm water infrastructure unblocked and maintained	50000m of Storm water infrastructure unblocked and maintained
3.1.3. Number of km of gravel roads in the KSD repaired and maintained	800km of gravel roads in the KSD repaired and maintained
3.1.6. 3 km of 66kv overhead line constructed and upgrade	7 km of 66kv overhead line constructed and upgrade
3.1.8. Number of substations constructed and commissioned	1 substation constructed and commissioned by June 2020
3.1.21. No of new households with access to refuse removal using communal skips	7 000 households

## Various indicators

28. The achievement of the indicators listed below were reported against targets in the annual performance report. However, the supporting evidence provided differed materially from the reported achievement.

<b>Indicator Description</b>	<b>Planned target</b>	<b>Reported achievement</b>
3.1.2. Number of meters of Storm water infrastructure unblocked and maintained	50000m of Storm water infrastructure unblocked and maintained	34738m of Storm water infrastructure unblocked and maintained
3.1.3. Number of km of gravel roads in the KSD repaired and maintained	800km of gravel roads in the KSD repaired and maintained	516,09km of gravel roads maintained
3.1.5. Number of households connected to the grid in Mthatha West, Bongweni and Maiden Farm by June 2020	1500 households connected to the grid in Mthatha West, Bhongweni and Maiden Farm	870 households connected to the grid in Mthatha West, Bhongweni and Maiden Farm

## Various indicators

29. I was unable to obtain sufficient appropriate audit evidence for the achievement against reported targets in the annual performance report. This was due to the lack of accurate and complete records. 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 for the targets listed in the table below.

<b>Indicator Description</b>	<b>Planned target</b>	<b>Reported achievement</b>
3.1.4. Number of km of roads constructed and rehabilitated by June 2020	20 km of roads constructed and rehabilitated	80 km of roads constructed and rehabilitated in June 2020
3.1.6. Number of km of 66kv overhead line constructed and upgraded	3 km of 66kv overhead line constructed and upgrade	7 km of 66kv overhead line constructed and upgrade



## Various indicators

30. I was unable to obtain sufficient appropriate audit evidence to support the measures taken to improve performance against the target as reported in the annual performance report. This was due to limitations placed on the scope of our work as measures taken to improve performance were not supported by corroborating evidence. I was unable to confirm the reported measures taken by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported measures taken to improve performance for the indicators listed below:

Indicator Description	Planned target	Reported achievement
3.1.5. Number of households connected to the grid in Mthatha West, Bongweni and Maiden Farm by June 2020	1500 households connected to the grid in Mthatha West, Bhongweni and Maiden Farm	870 households connected to the grid in Mthatha West, Bhongweni and Maiden Farm
3.1.7. Number of transformer bays constructed and commissioned	1 transformer and a contractor procured and transformer delivered or Thornhill substation	0 constructed
3.1.8. Number of substations constructed and commissioned	1 substation constructed and commissioned by June 2020	0 Substation constructed
3.1.9. Number of km of 11kV overhead line constructed	12 km of 11 KV overhead line contracted between Thornhill substation and Mthatha Dam	0km overhead 11kv line constructed

## Other matters

31. I draw attention to the matters below.

### Achievement of planned targets

32. Refer to the annual performance report on pages ... to ... for information on the achievement of planned targets for the year and explanations provided for the under/over achievement of a significant number of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 27 to 30 of this report.

### Adjustment of material misstatements

33. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information of the basic service delivery and infrastructure development priority. 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

34. 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.

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

### Annual financial statements, annual performance report and annual report

36. 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 in non-current assets, current assets, current liabilities, revenue, expenditure and disclosure identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were subsequently provided, but the uncorrected material misstatements resulted in the financial statements receiving a qualified opinion.

### Strategic planning and performance management

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

38. The strategic development budget implementation plan (SDBIP) for the year under review did not include monthly revenue projections by source of collection and/or the monthly operational and capital expenditure by vote, and/or the service delivery targets and performance indicators for each quarter as required by section 1 of the MFMA.

### Expenditure management

39. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.

40. Reasonable steps were not taken to prevent irregular expenditure of R23,5 million disclosed in note 50 to the financial statements, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by non-adherence to the supply chain management (SCM) legislations.

41. Reasonable steps were not taken to prevent fruitless and wasteful expenditure of R23,6 million disclosed in note 49 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.



42. Reasonable steps were not taken to prevent unauthorised expenditure of R144,8 million disclosed in note 48 to the financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by spending exceeding the main segments within the budget and not budgeting for non-cash items.

#### Asset management

43. 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.

#### Consequence management

44. Unauthorised expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a) of the MFMA.

45. Fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.

46. Irregular expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.

#### Procurement and contract management

47. The performance of some of the contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.

48. 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.

#### Other information

49. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report, which includes the directors' report, the audit committee's report. The other information does not include the financial statements, the auditor's report and the selected development priority presented in the annual performance report that have been specifically reported in this auditor's report

50. 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.

51. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected development priority presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

52. 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

53. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

- Leadership did not adequately oversee financial and performance reporting nor compliance with legislation. In this regard, leadership did not appropriately monitor the implementation of policies and procedures to support the achievement of credible reporting and compliance with legislative requirements. Progress on the municipality's audit intervention plan was slow to adequately address issues raised in the previous year.
- The submitted financial statements and annual performance report contained material misstatements that were not all corrected. The portfolios of evidence and supporting schedules used to support the financial statements and actual achievement of targets were not complete and accurate in all instances.
- Monitoring activities were inadequate to ensure that identified risks were effectively addressed and this is evident by repeat findings in the current year audit.

### Material irregularities

54. In accordance with the PAA and the Material Irregularity Regulations, I have a responsibility to report on material irregularities identified during the audit.

#### **Material irregularities identified during the audit**

55. The material irregularities identified are as follows:

#### **Material irregularities in progress**

56. I identified a material irregularity during the audit and notified the accounting officer of this, as required by material irregularity regulation 3(2). By the date of this auditor's report, I had not yet completed the process of evaluating the responses from the accounting officer. This material irregularity will be included in the next year's auditor's report.

57. I identified another material irregularity during the audit and notified the accounting officer, as required by material irregularity regulation 3(2). By the date of this auditor's report, the response of the accounting officer was not yet due. This material irregularity will be included in the next year's auditor's report.



## Other reports

58. In addition to the investigations relating to material irregularities, I draw attention to the following engagements conducted by various parties which had, or could have, an impact on the matters reported in the municipality's financial statements, reported performance information, compliance with applicable legislation and other related matters. These reports did not form part of my opinion on the financial statements or my findings on the reported performance information or compliance with legislation.
59. The Special Investigation Unit (SIU) was investigating matters that arose in previous years, including the costs incurred for the funeral of former president Nelson Mandela. This investigation is still in progress.
60. A forensic investigation was concluded into grievances raised by staff members, which extends to task payments made by the municipality in the previous financial cycle.
61. The South African Police Services (SAPS) was investigating allegations of an employee who submitted a fraudulent claim form to the pension fund. This investigation is still in progress.

Auditor-General.

East London

6 April 2021



AUDITOR - GENERAL  
SOUTH AFRICA

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## **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 priority 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 relating to events or conditions that may cast significant doubt on the ability of the King Sabata Dalindyebo Local Municipality’s 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 my 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 determine 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, the actions taken to eliminate threats or the safeguards applied.