

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

Report on the audit of the financial statements

Opinion

1. I have audited the financial statements of the Phumelela 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. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Phumelela 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 56 of 2003 (MFMA) and the Division of Revenue Act 16 of 2019 (Dora).

Basis for opinion

3. 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.
4. 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.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Material uncertainty relating to going concern

6. I draw attention to the matter below. My opinion is not modified in respect of this matter.
7. Note 44 to the financial statements indicates that the municipality's current liabilities exceeded its current assets by R306 550 478 (2019: R247 973 204). In addition, the municipality owed Eskom R148 070 971 (2019: R126 339 371) and the water board R101 868 593 (2019: R85 167 539) as at 30 June 2020, which is long overdue. These events or conditions, along with other matters as set forth in note 44, 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

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

Irregular expenditure

9. As disclosed in note 47 to the financial statements, the municipality incurred irregular expenditure of R14 593 643 (2019: R13 578 196), due to non-compliance with the supply chain management (SCM) requirements.

Fruitless and Wasteful expenditure

10. As disclosed in note 46 to the financial statements, fruitless and wasteful expenditure of R10 242 757 (2019: R2 762 401) was incurred, mainly due to interest on arrear payments to creditors.

Unauthorised expenditure

11. As disclosed in note 45 to the financial statements, unauthorised expenditure of R136 748 196 (2019: R86 641 066) was incurred, due to overspending a main division within the vote.

Restatement of corresponding figures

12. As disclosed in note 42 to the financial statements, the corresponding figures for 30 June 2019 were restated as a result of an error in the financial statements of the municipality at, and for the year ended, 30 June 2020.

Material losses

13. As disclosed in note 48 to the financial statements, material water distribution losses of R9 712 850 (2019 R7 017 466) and electricity distribution losses of R12 918 832 (2019: R15 211 328) were incurred by the municipality mainly due to leakages, burst water pipes, line losses, tampering and theft.

Material impairment

14. As disclosed in note 11 to the financial statements, consumer debtors were impaired by R320 118 768 (2019: R247 537 063).

Material uncertainty relating to claims against the municipality

15. With reference to note 40 to the financial statements, the municipality is the defendant in various claims against the municipality. The municipality is opposing these claims. The ultimate outcome of these matters could not be determined and no provision for any liabilities that may result were made in the financial statements.

Other matter

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

Unaudited disclosures note

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 thereon.

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 the 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 Phumelela 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

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 material findings on the reported performance information against predetermined objectives for the selected key performance area (KPA)

presented in the annual performance report. I was engaged to perform procedures to identify findings but not to gather evidence to express assurance.

23. I was engaged to evaluate 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 2020:

KPA	Pages in the annual performance report
Service delivery and infrastructure development	x – x

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

Service delivery and infrastructure development

Various indicators

25. I was unable to obtain sufficient appropriate audit evidence that clearly defined the predetermined source information and method of collection or that related systems and processes were established to enable consistent measurement and reliable reporting of the actual achievement of the indicators listed below. This was due to a lack of measurement definitions and processes. I was unable to test whether the indicator was well-defined and verifiable by alternative means. As a result, I was unable to audit the reliability of the achievements reported in the annual performance report for the following listed indicators:

Indicator description	Planned target	Reported achievement
Memel/Zamani electrification of 300 of 1211 sites (TS17)	100%	100%
Refurbishment of wastewater treatment plant and pump station in Vrede. (TS 7)	100%	28%
Ezenzeleni/Warden upgrading of outfall sewer and construction of a new pump station kilometres of roads repaired. (TS14)	100%	100%
Memel/Zamani construction of water supply line associated storage and pump station. (TS 2)	100%	58%
No of households with access to basic refuse removal services (removal at least one week) (FS.5)	12	12

No of HHS with access to basic electricity in formal areas (FS.4)	12	12
No of HHS with access to decent sanitation (FS.3)	12	12
No of HHS with access to portable water in formalised areas (yard metered connections) (FS.2)	12	12

Other matters

26. I draw attention to the matters below.

Achievement of planned targets

27. 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 paragraph 25 of this report.

Adjustment of material misstatements

28. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported information of service delivery 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 reported above.

Report on the audit of compliance with legislation

Introduction and scope

29. 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.

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

Annual financial statements, performance reports and annual reports

31. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of non-current assets, current assets, non-current liabilities, current liabilities, revenue, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.

32. The council failed to adopt an oversight report containing the council's comments on the 2018/19 annual report, as required by section 129(1) of the MFMA.

Conditional grants

33. Performance in respect of programmes funded by the municipal infrastructure grant was not evaluated within two months after the end of the financial year, as required by section 12(5) of the Division of Revenue Act (Act 1 of 2018) (Dora).
34. Performance in respect of programmes funded by the water services infrastructure grant was not evaluated within two months after the end of the financial year, as required by section 12(5) of the Dora.
35. Performance in respect of programmes funded by the regional bulk infrastructure grant was not evaluated within two months after the end of the financial year, as required by section 12(5) of the Dora.
36. Performance in respect of programmes funded by the financial management grant was evaluated within two months after the end of the financial year, as required by section 12(5) of the Dora.
37. Performance in respect of programmes funded by the integrated national electrification programme grant was not evaluated within two months after the end of the financial year, as required by section 12(5) of the Dora.
38. Performance in respect of programmes funded by the EPWP grant was not evaluated within two months after the end of the financial year, as required by section 12(5) of the Dora.
39. Performance in respect of programmes funded by the municipal disaster recovery grant was not evaluated within two months after the end of the financial year, as required by section 12(5) of the Dora.

Consequence management

40. 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.
41. Irregular expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as requested by section 32(2)(b) of the MFMA.
42. 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.

Expenditure management

43. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
44. Reasonable steps were not taken to prevent irregular expenditure amounting to R14 593 643 as disclosed in note 47 to the annual financial statements, as required by section 62(1)(d) of

the MFMA. The majority of the irregular expenditure was caused by non-compliance with SCM regulations.

45. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R10 242 757 as disclosed in note 46 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the fruitless and wasteful expenditure was caused by late payments and non-payment of outstanding amounts.
46. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R136 748 196 as disclosed in note 45 to the financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by the municipality exceeding its budget.

Procurement and contract management

47. The preference point system was not applied for some of the procurement of goods and services above R30 000, as required by section 2(1)(a) of the Preferential Procurement Policy Framework Act 5 of 2000.
48. Some of the contracts were awarded to bidders based on points given for criteria that differed from those stipulated in the original invitation for bidding, in contravention of SCM regulations 21(b) and 28(1)(a)(i) and the Preferential Procurement Regulations.
49. Some of the contracts were extended or modified without the approval of a properly delegated official, in contravention of SCM regulation 5.

Strategic planning and performance management

50. The performance management system and related controls were not adequate as it did not describe how the performance measurement processes should be conducted, organised and managed, as required by municipal planning and performance management regulation 7(1).

Other information

51. 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 those selected KPA presented in the annual performance report that have been specifically reported in this auditor's report.
52. 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.
53. 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.

54. 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 with those charged with governance and request that other information be 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

55. 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 findings on the annual performance report and the findings on compliance with legislation included in this report.
56. Management did not implement adequate controls to ensure compliance with laws, regulations. As a result, material non-compliance matters were noted.
57. Management did not implement effective human resource management measures to ensure that vacancies were filled, and sufficiently skilled resources were in place to ensure effective controls over daily and monthly processing and reconciling of transactions. This resulted in significant misstatements in the financial statements and performance information that had to be corrected.
58. Management did not implement a proper record management system to maintain information that support the reported performance information in the annual performance report. This include information that relates to the collection, collation, verification, storing and reporting of performance management information.

Auditor - General

Bloemfontein

28 February 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 financial statements and the procedures performed on reported performance information for selected KPA and on the municipality’s compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the financial statements as described in this auditor’s report, I also:
 - identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error; design and perform audit procedures responsive to those risks; and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control
 - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality’s internal control
 - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer
 - conclude on the appropriateness of the accounting officer’s use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists relating to events or conditions that may cast significant doubt on the ability of the Phumelela 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 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.