

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

## Report on the audit of the financial statements

### Qualified opinion

1. I have audited the financial statements of the Metsimaholo Local Municipality set out on pages XX to XX, 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 information and actual information 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 and the possible effects of the matters described in the basis for qualified opinion section of this auditor's report, the financial statements present fairly, in all material respects, the financial position of the Metsimaholo 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 qualified opinion

#### Property plant and equipment

3. I was unable to obtain sufficient appropriate audit evidence for property, plant and equipment as the municipality did not maintain an adequate asset register and could not provide supporting records for disposals. I was unable to confirm 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 R1 225 813 747 (2019: R1 223 944 817) in note 4 to the financial statements.
4. The municipality did not account for property, plant and equipment in accordance with GRAP 17, *Property, plant and equipment*. Various movable assets and additions on infrastructure disclosed in the asset register did not physically exist, resulting in property, plant and equipment being overstated by R35 820 335. This has a resultant impact on the surplus for the period and the accumulated surplus. The municipality also incorrectly classified land as buildings, resulting in land being overstated and buildings understated by R12 722 235 in note 4 to the financial statements.
5. The municipality did not correctly classify community assets, resulting in property, plant and equipment being overstated and investment property being understated by R13 196 552. In addition, infrastructure projects that had been finalised as at 30 June 2020 were incorrectly included in the closing balance of work-in-progress, as reflected in the reconciliation of work-

in-progress in note 4 to the financial statements. Consequently, work-in-progress was overstated by R23 740 444 (2019: R123 353 761).

### Investment property

6. I was unable to obtain sufficient appropriate audit evidence for investment property as the municipality did not maintain an adequate asset register and could not provide the required supporting documentation. In addition, adequate supporting documentation could not be provided to confirm the restatement made to the investment property opening balance. I was unable to confirm investment property by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to investment property, stated at R444 879 258 (2019: R445 937 342) in note 3 to the financial statements.

### Payables from exchange transactions

7. I was unable to obtain sufficient appropriate audit evidence for payables from exchange transactions as the required supporting documents were not provided. I could not confirm payables from exchange transactions by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to payables from exchange transactions, stated at R281 446 155 in note 19 to the financial statements. In addition, the municipality did not account for payables in accordance with GRAP 1, *Presentation of financial statements*. Payables from exchange transactions were accounted for in an incorrect accounting period, resulting in payables from exchange transactions and operating expenditure being overstated by R17 644 733. Additionally, there was an impact on the surplus for the period and on the accumulated surplus.

### Irregular expenditure

8. The municipality did not disclose all instances of irregular expenditure incurred in the notes to the financial statements, as required by section 125(2)(d) of the MFMA. The municipality made payments in contravention of the supply chain management (SCM) requirements, which were not disclosed. I was unable to determine the full extent of the understatement of irregular expenditure as disclosed in note 53 to the financial statements, as it was impracticable to do so.

### Operating expenditure

9. I was unable to obtain sufficient appropriate audit evidence for operating expenditure. Adequate supporting documentation could not be provided to confirm that the goods and services were actually received and at the correct quantity, quality and price. I could not confirm operating expenditure by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to operating expenditure, stated at R92 293 507 in note 38 to the financial statements. In addition, the municipality did not classify transactions in accordance with GRAP 1, *Presentation of financial statements* as items relating to assets were incorrectly classified as operating expenditure (inventory consumables). This resulted in inventory consumables being overstated and property, plant and equipment being understated by R10 101 436. This also has an impact on the surplus for the period and on the accumulated surplus.

## Contracted services

10. I was unable to obtain sufficient appropriate audit evidence relating to contracted services. Adequate supporting documentation could not be provided to confirm that the goods and services were actually received and at the correct quantity, quality and price. I could not confirm contracted services by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to contracted services, stated at R79 498 478 in note 37 to the financial statements.

## Depreciation and amortisation

11. During 2019, the municipality did not correctly provide for depreciation on items of property, plant and equipment in accordance with GRAP 17, *Property, plant and equipment*. The depreciation was calculated using the incorrect useful lives. Consequently, depreciation and amortisation was understated by R13 727 130 and property, plant and equipment overstated by the same amount. My audit opinion on the financial statements for the period ended 30 June 2019 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 operating expenditure for the current period.

## Service charges

12. During 2019, I was unable to obtain sufficient appropriate audit evidence for revenue from service charges and to confirm the service charges by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to service charges, stated at R693 519 589 in note 22 to the financial statements. My audit opinion on the financial statements for the period ended 30 June 2019 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 operating expenditure for the current period.

## Property rates

13. During 2019, I was unable to obtain sufficient appropriate audit evidence for property rates and to confirm the property rates by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to property rates, stated at R143 648 432 in note 27 to the financial statements. My audit opinion on the financial statements for the period ended 30 June 2019 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 operating expenditure for the current period.

## Context for the opinion

14. 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.
15. 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.

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

### **Emphasis of matters**

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

### **Restatement of corresponding figures**

18. As disclosed in note 45 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 uncertainty relating to claims against the municipality**

19. With reference to note 42 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 provided for in the financial statements.

### **Material losses**

20. As disclosed in note 36 to the financial statements, material water distribution losses of R35 492 405 (2019: R28 093 100) and electricity distribution losses of R34 572 353 (2019: R15 278 740) were incurred by the municipality mainly due to leakages, burst water pipes, line losses, tampering and theft.

### **Material impairment**

21. As disclosed in notes 11 and 13 to the financial statements, receivables from non-exchange and consumer debtors were impaired by R1 698 988 453 (2019: R1 415 146 023).

### **Other matters**

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

### **Service delivery**

23. A project to construct the Refeng Kgotso sports complex was awarded in December 2019 with a planned project duration of 36 months and a budgeted cost of R7 545 383. The actual project expenditure at 30 June 2020 was R5 171 767 with additional payments of R1 863 927 being made up to May 2021. During a site visit conducted in February 2021, discrepancies were noted between the actual work that had been constructed and the work certified as completed, although the majority of the project costs were paid.

## Unaudited disclosure notes

24. 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.

## Unaudited supplementary schedules

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

## Responsibilities of the accounting officer for the financial statements

26. 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.
27. In preparing the financial statements, the accounting officer is responsible for assessing the Metsimaholo 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

28. 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.
29. 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

30. 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 selected key performance areas (KPAs)

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

31. 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
KPA 1 – basic service delivery and infrastructure investment	x – x

32. 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.
33. The material findings in respect of the usefulness and reliability of the selected KPA are as follows:

#### **KPA 1 – basic service delivery and infrastructure investment**

##### *Various indicators*

34. I was unable to obtain sufficient appropriate audit evidence for the achievement and the related measures taken to improve performance, as reported in the annual performance report, for the indicators listed below. Limitations were placed on the scope of my work, as the actual level of achievement for the year was not quantified. 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 achievements and the reported measures taken to improve performance.

Indicator descriptions	Planned targets	Reported achievements
% minimisation of water distribution losses	Water distribution losses minimised to 10%	Target not achieved – it was achieved only in the 2nd quarter (15,54%)
% compliance with the blue drop water quality accreditation system	> 99% compliance with the blue drop water quality accreditation system	Target not achieved
% compliance with the green drop quality accreditation system	> 99% compliance with the green drop water quality accreditation system	Target not achieved – the inflow exceeds the design capacity of the plant

### *Upgrade the waste water treatment works*

35. The achievement for the target upgrade the waste water treatment works reported in the annual performance report was 40%. However, the supporting evidence provided did not agree with the reported achievement and indicated an achievement of 53%.

### *Ensure that the municipality broadly delivers service according to the strategic orientation based on key sector plans*

36. The reported strategic objective did not agree with the planned objective stated in the approved service delivery and budget implementation plan (SDBIP). Additionally, the strategic objective in the approved SDBIP was changed without the necessary approval.

### **Other matter**

37. I draw attention to the matter below.

### **Achievement of planned targets**

38. 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 34 to 36 of this report.

## **Report on the audit of compliance with legislation**

### **Introduction and scope**

39. 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.

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

### **Annual financial statements**

41. 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 current assets, and disclosures identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

## Expenditure management

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 qualified opinion paragraphs.
43. Reasonable steps were not taken to prevent fruitless and wasteful expenditure of R7 197 491, as disclosed in note 52 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA.
44. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
45. Reasonable steps were not taken to ensure that the municipality implements and maintains an effective system of expenditure control, including procedures for the approval and payment of funds, as required by section 65(2)(a) of the MFMA.

## Procurement and contract management

46. Some goods and services with a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Similar non-compliance was also reported in the prior year.
47. Some invitations for competitive bidding were not advertised for a required minimum period of days, in contravention of SCM regulation 22(1) and 22(2). Similar non-compliance was also reported in the prior year.
48. Sufficient appropriate audit evidence could not be obtained that contracts were awarded only to bidders who submitted a declaration on whether they were employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c). Similar non-compliance was also reported in the prior year.
49. Sufficient appropriate audit evidence could not be obtained that contracts were only awarded to providers whose tax matters had been declared by the South African Revenue Service to be in order, as required by SCM regulation 43. Similar non-compliance was also reported in the prior year.
50. The preference point system was not applied to some 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 (PPPFA). Similar non-compliance was also reported in the prior year.
51. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded to bidders that scored the highest points in the evaluation process, as required by section 2(1)(f) of the PPPFA and the 2017 Preferential Procurement Regulations.
52. Sufficient appropriate audit evidence could not be obtained that all extensions or modifications to contracts were approved by a properly delegated official, as required by SCM regulation 5.



53. The performance of the contractors or providers was not monitored monthly, as required by section 116(2)(b) of the MFMA.
54. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e), the code of conduct for councillors issued in terms of the Municipal Systems Act 32 of 2000 and the code of conduct for staff members issued in terms of the Municipal Systems Act.

#### **Consequence management**

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

#### **Asset management**

58. 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**

59. A performance management system was not established, as required by section 38(a) of the Municipal Systems Act.

#### **Utilisation of conditional grant**

60. The municipal infrastructure grant was not spent for its intended purposes in accordance with the applicable grant framework, as required by section 17(1) of the Dora.

#### **Other information**

61. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report and the selected KPA presented in the annual performance report that have been specifically reported in this auditor's report.
62. 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.

63. 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.
64. 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

65. 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.
66. The municipal manager was on suspension for the financial year under review. All the manager positions that reported directly to the municipal manager were also vacant for the same period. This resulted in various officials acting in these vacant positions, contributing to the instability in the leadership of the municipality. At the time of finalising this report, none of these vacancies had been filled.
67. Although the municipality was placed under administration, the implementation of the corrective measures included in the audit action plan were inadequate and not effectively monitored to ensure that the weaknesses relating to the finance, performance and supply chain management were addressed.
68. A lack of commitment from key officials and the staff supporting them to implement and monitor internal controls over daily and monthly processing of transactions resulted in the material audit findings included in this report.
69. Inadequate oversight and accountability resulted in officials not being held accountable for transgressions with laws and regulations and an increase in the number of compliance findings raised during the year under review.
70. Management did not implement proper recordkeeping to ensure that complete, relevant and accurate information was accessible and available to support financial and performance reporting.
71. Management's inability to prioritise, develop and apply standard operating procedures to manage financial and performance reporting, including the safeguarding of information and effective monitoring and evaluation of reported financial and performance information, resulted in significant findings.

72. Management's lack of detailed review of the financial statements and the underlying records resulted in material misstatements that were not detected by the department's internal processes.

*Auditor-General*  
Bloemfontein

7 April 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 Metsimaholo 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.