

Report of the auditor-general to the provincial legislature and the council on Makhado Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Makhado Local Municipality set out on pages xx to xx, which comprise statement of financial position as at 30 June 2019, the statement of financial performance, statement of changes in net assets, and cash flow statement and the statement of comparison of budget information with 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 of the matters described in the basis for qualified opinion section of this report, the financial statements present fairly, in all material respects, the financial position of the Makhado Local Municipality as at 30 June 2019, 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 (Act No. 01 of 2018) (Dora).

Basis for qualified opinion

Revenue from non-exchange transactions

3. The municipality did not recognise revenue from non-exchange transactions in accordance with GRAP 23, *Revenue from non-exchange transactions*. I identified properties from the municipality's valuation roll that were not correctly billed during the financial year, resulting in an overstatement of revenue from property rates. Consequently, revenue from property rates in note 22 to the annual financial statements stated at R73 345 242 was overstated by R10 218 627. There had a consequential impact on consumer debtors from non-exchange transactions in note 5 to the financial statements stated at R21 326 491 and the deficit for the period.

Context for the opinion

4. 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.
5. I am independent of the municipality in accordance with sections 290 and 291 of the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* and parts 1 and 3 of the International Ethics Standards Board for Accountants' *International code of ethics for professional accountants (including International Independence Standards)* (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.

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

Emphasis of matters

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

Material impairments

8. As disclosed in note 29 to the financial statements, material losses of R46 868 105 were incurred as a result of an impairment of irrecoverable debtors.

Material losses – electricity

9. As disclosed in note 40 to the financial statements, material electricity losses of R39 970 411 (2018: R20 661 114) were incurred, which represents 14,49% (2018: 9,4%) of the total electricity purchased.

Restatement of corresponding figures

10. As disclosed in note 37 to the financial statements, the corresponding figures for 30 June 2018 have been restated as a result of an error discovered in the financial statements of the municipality at, and for the year ended, 30 June 2019.

Other matters

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

Unaudited supplementary schedules

12. The supplementary information as 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.

Unaudited disclosure notes

13. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose the particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of financial statements and, accordingly, I do not express an opinion on it.

Responsibilities of the accounting officer for the financial statements

14. 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.

15. In preparing the financial statements, the accounting officer is responsible for assessing the Makhado 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

16. 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.

17. 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

18. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 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 development priorities presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.

19. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did 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.

20. 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 priorities presented in the annual performance report of the municipality for the year ended 30 June 2019:

Development priorities	Pages in the annual performance report
Development priority 2: Basic service delivery and infrastructure development	x – x
Development priority 4: Local economic development	x – x

21. 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.
22. The material findings in respect of the usefulness and reliability of the selected development priorities are as follows:

Development priority 2: Basic service delivery and infrastructure development

Performance indicators and targets not verifiable and not reliable

Number of households with access to refuse removal in rural areas by 30 June 2019

23. I was unable to obtain sufficient appropriate audit evidence to support the reported achievement of the target 6 889 households. This was due to a lack of proper performance management systems and processes and formal standard operating procedures or documented systems descriptions that predetermined how the achievement would be measured, monitored and reported. I was unable to confirm the reported achievement of the indicator by alternative means. Consequently, I was unable to determine whether any adjustments were required to the achievement of the reported achievements listed below as reported in the annual performance report.

No evidence was provided for the measures reported to improve performance

Number of Households earning less than R1100 per month with access to free electricity by 30 June 2019

24. I was unable to obtain sufficient appropriate audit evidence to support the measures taken to improve performance against target of 4 353 households as reported in the annual performance report. This was due to inappropriate measures disclosed in the annual performance report that could not be supported. 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.

Various indicators

25. The municipality did not have an adequate record keeping system to enable reliable reporting on achievement of the indicators listed below. As a result, I was unable to obtain sufficient appropriate audit evidence in some instances, while in other cases the supporting evidence provided did not agree to the reported achievements. Based on the supporting evidence that was provided, the achievement of these indicators was different to the reported achievement in the annual performance report. I was also unable to further confirm the reported achievements by alternative means. Consequently, I was unable to determine whether any further adjustments were required to the reported achievements of the indicators listed below.

Indicator description	Reported achievement	Audited value
Number of households electrified by 30 June 2019 at Songozwi Farm	42 Households electrified	48 Households electrified

Number of Mudimeli households electrified by 30 June 2019	210 Households electrified	225 Households electrified
Number of Households serviced with electricity postconnections by 30 June 2019	218 Households electrified	307 Households electrified
Number of Muananzhele/Mavhungeni households electrified by 30 June 2019	700 Households electrified	1050 Households electrified
Number of Mashau Tshilaphala households electrified by 30 June 2019	88 Households electrified	87 Households electrified

Reported indicator did not agree with the evidence provided

Number of households earning less than R1 100 per month with access to free electricity by 30 June 2019.

26. The achievement for 5 913 households earning less than R1 100 per month with access to free basic services in Makhado Local Municipality licensed areas reported in the annual performance report was 4 353. However, the supporting evidence provided did not agree to the reported achievement and indicated an achievement of 1 451.

Development priority 4: Local economic development

Various indicators

27. The reported achievement in the annual performance report did not agree to the supporting evidence provided for the indicators listed below. The supporting evidence provided indicated that the achievements of these indicators were as follows:

Indicator description	Reported achievement	Audited value
Number of LED projects supported by 30 June 2019	Six (06) projects supported by 30 June 2019	Two (02) projects supported by 30 June 2019

Other matters

28. I draw attention to the matters below.

Achievement of planned targets

29. Refer to the annual performance report on pages xx to xx for information on the achievement of planned targets for the year and explanations provided for the under/overachievement 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 23 to 26 of this report.

Adjustment of material misstatements

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

31. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.
32. The material findings on compliance with specific matters in key legislations are as follows:

Annual financial statements, annual performance report and annual report

33. 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.
34. Material misstatements of non-current assets, current assets, current liabilities and disclosure items identified by the auditors in the submitted financial statements were corrected and the supporting records were provided subsequently, but the uncorrected material misstatements resulted in the financial statements receiving a qualified audit opinion.

Strategic planning and performance management

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

Expenditure management

36. Reasonable steps were not taken to prevent irregular expenditure amounting to R14 204 502 as disclosed in note 41 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. Most of the irregular was caused by non-compliance with applicable legislation relating to bid and evaluation committees not being properly constituted.
37. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R84 406 344 as disclosed in note 42 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. Most of the unauthorised expenditure was caused by inappropriate budgeting of cash items during the financial year.

Procurement and contract management

38. Some quotations were accepted from bidders who had not submitted a declaration on whether they are employed by the state or connected to any person employed by the state, as required by supply chain management (SCM) regulation 13(c).

Consequences management

39. Appropriate action was not taken against officials of the municipality where investigations proved financial misconduct, as required by section 171(4)(b) of the MFMA and municipal regulation 6(6) relating to financial misconduct procedures and criminal proceedings.

Revenue management

40. An effective system of internal control for debtors/revenue was not in place as required by section 64(2)(f) of the MFMA.
41. Revenue due to the municipality was not calculated on a monthly basis as required by section 64(2)(b) of the MFMA.

Other information

42. 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 development priorities presented in the annual performance report that have been specifically reported in this auditor's report.
43. 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 thereon.
44. 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 priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
45. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information and 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

46. 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.

47. The internal policies and procedures of the municipality did not adequately address the processes pertaining to the planning, monitoring, managing and reporting of performance information at an overall performance management level or a development priority level.
48. Management did not implement the following daily and monthly controls designed for the municipality's business processes:
49. Monthly revenue/debtors reconciliations were not properly prepared and reviewed. This resulted in the billing errors in the financial system experienced by the municipality during the financial year.
50. The financial statements contained numerous misstatements, some of which were corrected. This was mainly due to staff not fully understanding the requirements of the financial reporting framework and insufficient reviews performed on the financial statements.
51. Non-compliance with legislation could have been prevented had compliance been properly reviewed and monitored. The municipality did not take reasonable steps to prevent irregular and unauthorised expenditure.

Auditor General

Polokwane

30 November 2019



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 development priorities and on the municipality’s compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the 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 related to events or conditions that may cast significant doubt on the Makhado Local Municipality’s ability 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 the 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 whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation
 - obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group to express an opinion on the consolidated financial statements. I am responsible for the direction, supervision and performance of the group audit. I remain solely responsible for my audit opinion.

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, related safeguards.