

Report of the Auditor-General to Gauteng Provincial Legislature for the audit of Merafong City Local Municipality

Report on the audit of the financial statements

Adverse of opinion

1. I have audited the financial statements of the Merafong City Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2021, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget information with actual information for the year then ended, as well as notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, because of the significance of the matters described in the basis for adverse opinion section of this auditor's report, the financial statements do not present fairly, in all material respects, the financial position of the Merafong city local municipality as at 30 June 2021, and financial performance and cash flows for the year then ended in accordance with the 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, 2020 (Act No. 4 of 2020) (Dora).

Basis for adverse of opinion

Property plant and equipment

3. Work-in-progress amounting to R209 034 079 included in note 4 to the financial statements was incorrectly classified as work-in-progress, while it was available for use in terms of GRAP 17, Property, plant and equipment. This resulted in the overstatement of work-in-progress and understatement of completed assets by R209 034 079. I was unable to quantify the misstatement of the depreciation amount as the municipality did not determine useful lives for these completed assets
4. The municipality did not calculate depreciation for all their property plant and equipment as disclosed in note 4 to the financial statements in accordance with their accounting policy and the requirements of GRAP 17 – *Property Plant and Equipment*. The asset register did not contain the total useful life nor the remaining useful life for these assets. As a result, I could not calculate the amount of the misstatement relating to depreciation
5. I was unable to obtain sufficient appropriate audit evidence for the impairment of property plant and equipment. The municipality did not provide information relating to their calculation and I was unable to confirm this amount by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to the impairment stated at R40 386 269 in note 38 to the financial statements.

Consumer debtors

6. I was unable to obtain sufficient appropriate audit evidence that consumer debtors for the current year was properly accounted for due to the status of accounting records. I was unable to confirm consumer debtors by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to consumer debtors stated at R240 168 765 in the financial statements. Since the consumer debtors balance is included in the determination of net cash flows from operating activities reported in the statement of cash flows, I was unable to determine whether any adjustments were necessary in the cash flows from operating activities stated at R1 066 756 742 in the financial statements

Receivables from non-exchange transactions

7. I was unable to obtain sufficient appropriate audit evidence that other receivables from non exchange transactions for the current year were properly accounted for, due to the status of accounting records. I was unable to confirm other receivables from non exchange transactions by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to other receivables from non exchange transactions stated at R9 140 953 in the financial statements. Since the other receivables from non exchange transactions balance is included in the determination of net cash flows from operating activities reported in the statement of cash flows, I was unable to determine whether any adjustments were necessary in the cash flows from operating activities stated at R1 066 756 742 in the financial statements.

Trade payables

8. The municipality did not recognise all outstanding amounts meeting the definition of a liability in accordance with GRAP 1, *Presentation of financial statements*. As the municipality did not maintain adequate records of outstanding payments for goods and services received but not yet paid at year-end, I was unable to determine the full extent of the understatement of trade payables as it was impracticable to do so.

Provisions

9. I was unable to obtain sufficient appropriate audit evidence that provisions for the current year had been properly accounted for, due to the status of accounting records. I was unable to confirm provisions by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to provisions stated at R72 022 865 in the financial statements.

Revenue from exchange transactions

10. I was unable to obtain sufficient appropriate audit evidence for revenue from exchange transactions due to the municipality not maintaining complete and accurate accounting records. The municipality did not have adequate systems of internal control for the recording of all transactions and events and could not reconcile the transactions and events to the financial statements. I could not confirm revenue from exchange transactions by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the revenue from exchange transactions stated at R921 951 297 in the financial statements.

Prior period error

11. I was unable to obtain sufficient appropriate audit evidence for the restatement of the corresponding figure for property, plant and equipment, accumulated depreciation, payables, sundry debtors and Vat input. As described in note 52 to the financial statements, the restatement was made to rectify a previous year misstatement, but the restatement could not be substantiated by supporting audit evidence. I was unable to confirm the restatement by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the property, plant and equipment, accumulated depreciation, payables, sundry debtors and Vat input corresponding figure stated in the financial statements.

Net cash flows from operating activities

12. The municipality did not correctly prepare and disclose the net cash flows from operating activities as required by GRAP 2 – *Cash flow statements*. This was due to multiple errors in determining cash flows from operating activities. I was not able to determine the full extent of the errors for the current and prior year in the net cash flows from operating activities as it was impracticable to do so.

Net cash flows from investing activities

13. The municipality did not correctly prepare and disclose the net cash flows from investing activities as required by GRAP 2 – *Cash flow statements*. This was due to multiple errors in determining cash flows from investing activities. I was not able to determine the full extent of the errors for the current and prior year in the net cash flows from investing activities as it was impracticable to do so.

Statement of comparison of budget and actual amounts

14. The municipality did not correctly prepare and disclose the statement of comparison of budget and actual amounts as required by GRAP 24 – *Presentation of budget information in financial statements*. The cash flow statement portion of the statement of comparison of budget and actual amounts and its accompanying note did not agree with the amounts in the cash flow statement. I was unable to determine the full extent of the errors in the statement of comparison of budget and actual amounts as it was impracticable to do so.

Context for the opinion

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

Emphasis of matters

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

Material uncertainty

19. With reference to note 49 to the financial statements, the municipality is the defendant in a number of lawsuits. The ultimate outcome of these matters could not be determined and no provision for any liability that may result was made in the financial statements.

Material impairments

20. As disclosed in note 13 to the financial statements, the consumer debtors balance has been significantly impaired. The allowance for impairment of consumer debtors amounts to R3 137 593 434 (2019-20: R2 246 311 044) which represents 92.9% (2019-20: 84.2%) of total consumer debtors.

Material losses – water

21. As disclosed in note 64 to the financial statements, material water losses amounting to R54 215 995 (2019-20 - R43 733 103) were incurred, which represents 23.97% (2019-20 - 25,68%) of the total water purchased.

Material losses - electricity

22. As disclosed in note 64 to the financial statements, material electricity losses amounting to R74 662 214.54 (2019-21 - R150,167,272) were incurred, which represents 33.00% (2019-20 - 51,36%) of total electricity purchased.

Other matter

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

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.

Responsibilities of the accounting officer for the financial statements

25. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the Standards of Generally Recognised Accounting Practice (GRAP) and the requirements of the Municipal Finance Management Act 56 of 2003 (MFMA) and the Division of Revenue Act 04 of 2020 (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.
26. 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

27. 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.
28. 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

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

30. My procedures address the usefulness and reliability of the reported performance information, which must be based on the Municipality's approved performance planning documents. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures do not examine whether the actions taken by the municipality enabled service delivery. My procedures do not extend to any disclosures or assertions relating to the extent of achievements in the current year or 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.
31. 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 goal 1 presented in the municipality's annual performance report for the year ended 30 June 2021:

Strategic goal	Pages in the annual performance report
Strategic goal 1 – Provision of Basic Services	x – x

32. I performed procedures to determine whether the reported performance information 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. I did not identify any material findings on the usefulness and reliability of the reported performance information for this goal:
- Strategic goal 1: To provide basic services

Other matters

34. I draw attention to the matters below.

Achievement of planned targets

35. Refer to the annual performance report on pages ... to ... for information on the achievement of planned targets for the year and management's explanations provided for the under/over achievement 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 paragraph 18 of this report.

Adjustment of material misstatements

36. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information of strategic goal 1. As management subsequently corrected the misstatements, I did not raise any material findings on the usefulness and reliability of the reported performance information.

Report on the audit of compliance with legislation

Introduction and scope

37. 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.

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

Annual financial statements

39. The annual financial statements were not submitted to the Auditor-General, for auditing, within two months after the end of the financial year, as required by section 126(1)(a) of the MFMA.
40. 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 investment property, property plant and equipment, payables from exchange transactions, depreciation and impairment loss and disclosure items identified by the auditors in the submitted financial statements were not corrected, resulting in the financial statements receiving a disclaimer audit opinion.

Procurement and contract management

41. 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
42. Some of the goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1).
43. Some of the bid documentation for procurement of commodities designated for local content and production, did not stipulated the minimum threshold for local production and content as required by the 2017 preferential procurement regulation 8(2).
44. 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. Similar non-compliance was also reported in the prior year.
45. 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. Similar non-compliance was also reported in the prior year.

Expenditure management

46. Reasonable steps were not taken to prevent irregular expenditure amounting to R33 893 638 as as disclosed in note 58 to the annual financial statements, as required by section 62(1)(d) of the MFMA. All of the irregular expenditure was caused by contravention of regulation 19(a), due to no competitive bidding processes for goods and services procured, non-compliance with regulation 32 and regulation 36(1) on procurement of goods and services under contracts secured by other organs of state and unjustified deviation from supply chain management regulations, respectively.

Asset management

47. The system of internal control for assets was not effective, as required by section 63(2)(c) of the MFMA.

Consequence management

48. Irregular expenditure incurred by the municipality were not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) 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, The other information does not include the financial statements, the auditor's report and those selected goal 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 goal presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
52. If based on the work I have performed, I conclude that there is a material misstatement in this other information, I are required to report that fact. I have nothing to report in this regards.

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 audit of predetermined objectives and the findings on compliance with legislation included in this report

Leadership

54. The accounting officer did not adequately perform oversight responsibility of financial and performance reporting as well as compliance with applicable legislation, resulting in material misstatements identified on the annual financial statements, as well as material findings on the audit of predetermined objectives and compliance with applicable legislation. Action plans that were developed were not monitored regularly to ensure that they have been adequately implemented taking into account the recommendations by internal audit and the audit committee.
55. The review processes of financial statements, compliance with legislation and performance reporting by senior management were inadequate in certain instances, resulting in material misstatements identified on the financial statements, findings in the performance report and non-compliance with applicable legislation

Financial and performance management

56. Senior management did not implement sufficient monitoring controls on compliance with legislation and to ensure that the financial statements were supported by credible information, which resulted in material misstatements identified in the annual financial statements and material non-compliance with key legislation.
57. Senior management did not have effective monitoring controls in place to ensure that the annual performance report was supported by valid, accurate and complete information.

Governance

58. The oversight structures did not prevent the misstatements on financial statements, performance information and non-compliance that were identified during the audit. Internal audit and audit committee should ensure that recommendations are implemented and that controls are designed that will assist in the improvement of the municipality's audit outcome.

Material irregularities

59. 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

Material irregularities in progress

60. I identified material irregularities during the audit and notified the accounting officer of these, as required by material irregularity regulation 3(2). By the date of this auditor's report, the responses of the accounting officer were not yet due. These material irregularities will be included in the next year's auditor's report.

Other reports

61. 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.

Investigations

62. There is an investigations in progress that is being conducted by an independent consultants. These investigations was initiated based on allegations of possible fraud and theft. These investigations was still in progress at the reporting date.

Yours sincerely

Velaphi Madzena

Senior Manager: Gauteng Business Unit

15 December 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 Goal 1 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 Merafong City 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.