

Report of the auditor-general to Eastern Cape Provincial Legislature and the Council on the Emalahleni Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Emalahleni 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 the 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 qualified opinion section of this auditor's report, the financial statements do not present fairly, in all material respects, the financial position of the Emalahleni Local Municipality as at 30 June 2021, and their 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 4 of 2020.

Basis for qualified opinion

Property plant and equipment

3. The municipality did not account for property, plant and equipment in accordance with GRAP 17 *Property, Plant and equipment*,
 - Land and Buildings that are rented out by the municipality are classified as property, plant and equipment instead of investment property.
 - the municipality has land in the asset register that is occupied by residents of the municipality without legal transfer of ownership to those residents.
 - The municipality did not impair infrastructure assets and community assets that had impairment indicators at year end in accordance with GRAP 21 *Impairment of non-cash-generating assets* and depreciation was incorrectly calculated.

Consequently, property plant and equipment has been overstated by R49,5 million, Investment property has been understated by R5 million and accumulated surplus by R44,5 million.

Investment property

4. The municipality did not accurately account for investment property in accordance with GRAP 16 *Investment property*, as they incorrectly included properties that are privately owned as investment property. Furthermore, the municipality incorrectly classified

community assets as investment property. Consequently, investment property is overstated by R3,4 million and net assets by the same amount

Receivables from exchange

5. The municipality did not account for the impairment in respect of receivables for exchange in accordance with Standard of GRAP 104 *Financial Instruments*, as the impairment provided was greater than the gross amount of receivable and the amount disclosed in the financial statement do not agree to the underlying records. In addition, I was unable to substantiate the restatement which were made to the opening with sufficient appropriate evidence. I was unable to confirm the receivables from exchange transactions by alternative means. Consequently, I was unable to determine whether any further adjustment to receivables from exchange transaction stated at R0,7 million (2020:R16,9million) in note 6 of the statement of financial position were necessary.

Employee cost

6. I was unable to obtain sufficient appropriate evidence for employee cost as the underlying records did not agree to the amount disclosed on the financial statements. I was unable to confirm employee cost by alternative means. Consequently, I was unable to determine whether any adjustment to employee cost of R88,7 million in the financial statements are necessary.

Irregular expenditure

7. The municipality did not account for all the irregular expenditure that meets the definition of irregular expenditure in the notes to the financial statements as required by section 25 (2) of Municipal Finance Management Act of South Africa, 2003 (Act No.56 of 2003). I was unable to obtain sufficient appropriate evidence regarding irregular expenditure as disclosed in note 41 to the financial statements, as the disclosure presented in the financial statement for auditing purposes was not complete. I was unable to determine whether any adjustments to irregular expenditure of R0,004 million were necessary.

Prior period error

8. I was unable to obtain sufficient appropriate evidence for the movements in the prior period error note. This was due to the municipality not being able to substantiate and provide adequate documentation for the errors as per prior period note. Consequently, I was unable to determine whether any adjustments were necessary to the prior period error note

Statement of comparison of budget vs actual

9. The municipality did not accurately disclose the budget and the actual amounts, as required by GRAP 24 *Presentation of Budget Information in Financial Statements*. Presentation of budget information in financial statements. The amounts disclosed did not agree to the approved budget and actual amounts incurred and this has resulted in misstatement in statement of financial performance and statement of financial position.

Cashflow

10. The municipality did not prepare the cash flow statements in accordance with the requirements of GRAP 2, *Cash Flow Statements*. The municipality incorrectly calculated the net cash flow from operating activities and this resulted in material overstatement of R8,1 million. In addition, the municipality incorrectly calculated the net cash flow from financing activities and this resulted in material overstatement of R5,3 million

Statement of changes in net assets

11. The municipality did not accurately disclose the statement of changes in net assets in accordance with GRAP 1, *Presentation of Financial Statements*, as there are errors in the statement of changes in net assets which could not trace to the prior period error note. Consequently, I was unable to obtain sufficient appropriate evidence with regards to the correction of error of R3,7 million in current year and R2,5 million in prior year.

Commitments

12. The municipality did not disclose the accounting policy for accounting for commitments as required by GRAP 1, *Presentation of Financial Statements*, as the WIP additions do not agree to amounts of expenditure disclosed in determining commitments. In addition, consequently, commitments disclosed in annual financial statement are overstated by R2,1 million.

Contingent liabilities

13. The municipality did not disclose all the contingent liabilities in accordance with GRAP 19, *Provision*, as not all the contingent liabilities as per external confirmation were included in the financial statements. Consequently, contingent liabilities disclosed are understated by R2,1 million.

Segment reporting

14. The municipality did not appropriately disclose segment information as required by the Generally Recognised Accounting Practice (GRAP) 18, *Segment Reporting*, as the items within the disclosure were incorrect. Consequently, segment information has not been appropriately disclosed.

Corresponding figures

Revenue from non-exchange transactions

15. The municipality did not correctly classify the revenue from non-exchange in accordance with GRAP 23, *Revenue from non exchange transactions*, as they reclassified actuarial gain in the comparative amount from revenue from non-exchange transaction to revenue for exchange transaction without the supporting evidence. I was unable to obtain sufficient appropriate evidence on the comparatives for revenue from non-exchange as the adjustment made could not be supported by sufficient appropriate evidence. Consequently, the comparative in revenue from non-exchange is understated by R2,3 million and revenue from exchange are overstated by the same amount.

Context for the opinion

16. 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.
17. I am independent of the Emalahleni Local 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.
18. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Emphasis of matters

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

Unauthorised Expenditure

20. As disclosed in note 41 to the financial statements, the municipality incurred unauthorised expenditure of R10,3 million (2020: R21,1 million) as a result of overspending in the approved budget.

Fruitless and wasteful expenditure

21. As disclosed in note 41 to the financial statements, the municipality incurred fruitless and wasteful expenditure of R6,1 million (2020: R15,1 million) as a result of various expenditure which was incurred in vain.

Electricity losses

22. As disclosed in 31 to the financial statements, the municipality incurred electricity losses totalling R4,1 million (2020: R2,2 million)

Responsibilities of the accounting officer for the financial statements

23. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with 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.
24. In preparing the financial statements, the accounting officer is responsible for assessing the Emalahleni 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

25. 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.
26. 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

27. 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 programmes presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
28. 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.
29. 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 programmes presented in the annual performance report of the municipality for the year ended 30 June 2021:

| Development priority | Pages in the annual performance report |
|---|---|
| Basic service delivery and infrastructure development | x – x |

30. 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,

31. The material findings on the usefulness and reliability of the performance information of the selected Programme 1 – Basic service delivery and infrastructure development are as follows:

Basic service delivery and infrastructure development

Number of households electrified (202 households electrified in ward 1, 5, 6,7,8,9 and 17 by 30 June 2021)

32. I was unable to obtain sufficient appropriate audit evidence for the achievement of 113 household electrified reported against target of 202 households to be electrified in the annual performance report, due to the lack of accurate and complete records. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement

Number of households receiving free basic service electricity (3900 households receiving free basic service (Electricity) by June 2021)

33. I was unable to obtain sufficient appropriate audit evidence to support the measures taken to improve performance against target 3900 as reported in the annual performance report. This was due to limitations placed on the scope of my work. I was unable to confirm the reported measures taken by alternative means. In addition, I was unable to obtain sufficient appropriate audit evidence for the achievement of 3765 households receiving free basic electricity reported against target 3900 household receiving electricity in the annual performance report, due to the lack of accurate and complete records. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported measures taken to improve performance and to determine whether any adjustments were required to the reported achievement

Other matter

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

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 explanations provided for the under achievement of a number of targets. This information should be considered in the context of the material findings on the usefulness of the reported performance information in paragraph 25 of this report.

Report on the audit of compliance with legislation

Introduction and scope

36. 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.

37. The material findings on compliance with specific matters in key legislations are as follows:

Strategic and performance management

38. The performance management system and related controls were inadequate as it did not ensure the performance review processes are conducted, organised and managed, as required by municipal planning and performance management regulation 7(1).

Annual financial statements, annual performance report and annual report

39. 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 identified by the auditors in the submitted financial statements were not adequately corrected which resulted in the financial statements receiving a qualified audit opinion.

Expenditure management

40. 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 qualification paragraph. The majority of the disclosed irregular expenditure was caused by non-compliance with SCM regulation.

41. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R6.1 million, as disclosed in note 41 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by court settlement

42. Reasonable steps were not taken to prevent unauthorised expenditure, as required by section 62(1)(d) of the MFMA. The expenditure disclosed does not reflect the full extent of the unauthorised expenditure incurred as indicated in the basis for qualification paragraph. The majority of the disclosed unauthorised expenditure was caused by exceeding the budget and weak budgetary controls.

Procurement and contract management

43. Awards were made to providers who were in the service of other state institutions, in contravention of MFMA 112(1)(j) and SCM Regulation 44. Similar awards were identified in the previous year and no effective steps were taken to prevent or combat the abuse of the SCM process, as required by SCM Regulation 38(1).

Other information

44. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes the audit committee's report. The other information does not include the financial statements, the auditor's report and those selected programmes presented in the annual performance report that have been specifically reported in this auditor's report.
45. 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.
46. 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 programmes presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
47. We did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, if we conclude that there is a material misstatement therein, we are 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, we may have to retract auditor's report and re-issue amended report as appropriate. However, if it is corrected this will not be necessary.

Internal control deficiencies

48. 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.
49. The controls were not operating effectively at the municipality, since the annual financial statements and annual performance report that were submitted for audit contained numerous material misstatements that were not identified by the municipality's system of internal controls.

AUDITOR-GENERAL

East London

01 February 2022



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

1. 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 Emalahleni Local Municipality 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 continuing 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 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

2. 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.

3. 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.

Explanatory information and examples

General