

Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on Intsika Yethu Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Intsika Yethu 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 amounts for the year then ended, as well as notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the effects and possible 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 Intsika Yethu Local Municipality as at 30 June 2021, and its financial performance and cash flows for the year then ended in accordance with the with 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 4 of 2020 (Dora).

Basis for qualified opinion

Property, plant and equipment

3. The municipality did not recognise all its property, plant and equipment in accordance with GRAP 17, *Property plant and equipment*, due to the poor state of asset management controls in accounting for assets under construction in the prior and current years. The municipality paid for assets that were not received. I was unable to determine the full extent of adjustments necessary to property, plant and equipment – assets under construction, stated at R88,2 million (2020: R76,4 million) in note 9; capital grants revenue from non-exchange transfers and subsidies, stated at R71,7 million (2020: R46,7 million) in note 22; and unspent conditional grants and receipts, stated at R4,3 million (2020: R8,8 million) in note 15 to the financial statements, as it was impracticable to do so.
4. The municipality did not have adequate systems to maintain records of fixed assets. Certain fixed assets were recorded in the municipality's fixed assets register; however, these assets could not be located during physical verification of assets. The municipality's fixed assets register included assets that it did not own. Additionally, certain assets were derecognised from the asset register at year-end even though they were disposed of after year-end. Consequently, I was unable to determine the full extent of the misstatement in property, plant and equipment, stated at R558 million (2020: 530,2 million) in note 9 to the financial statements as it was impracticable to do so.

5. The municipality did not assess and recognise impairment on asset in accordance with GRAP 21, *Impairment of non-cash-generating assets*. Damaged assets were included in the infrastructure assets without being impaired. I could not confirm the impairment amount by alternative means. Consequently, I was unable to determine the full extent of the overstatement of property, plant and equipment, stated at R558 million (2020: 530,2 million) in note 9, and understatement of impairment loss, stated at Rnil (2020: R3,1 million) in note 31 to the financial statements as it was impracticable to do so.

Fruitless and wasteful expenditure

6. The municipality did not have adequate controls in place to correct the prior year misstatements of fruitless and wasteful expenditure incurred due to payments made for goods not yet received. As a result, I was unable to determine the full extent of the misstatement in the opening balance and the closing balance as it was impracticable to do so. Consequently, I was unable to determine whether any adjustment was necessary to fruitless and wasteful expenditure, stated at R16,7 million (2020: R16,7 million) in note 40.2 to the financial statements.

Irregular expenditure

7. The municipality did not have adequate controls in place to correct the prior year misstatements of irregular expenditure that were due to certain goods and services procured in contravention of supply chain management (SCM) legislation in the prior year. As a result, I was unable to determine the full extent of the misstatement in the opening and closing balance as it was impracticable to do so. Consequently, I was unable to determine whether any further adjustments were necessary to irregular expenditure, stated at R45,2 million (2020: R37,8 million) in note 40.3 to the financial statements.

Inventories

8. The municipality did not have adequate processes in place to ensure that all prior period errors in the financial statements were recorded in terms of GRAP 3, *Accounting policies, changes in accounting estimates and errors*. A restatement was processed to the prior year inventory balance; however, in processing the adjustment, the municipality derecognised assets that met the recognition requirements of GRAP 12, *Inventory*. Consequently, the opening balances for inventories and accumulated surplus were understated by R 2,7 million, resulting in the understatement of the closing balance for inventories and accumulated surplus.

Corresponding figures

Transfers and subsidies

9. I was unable to obtain sufficient appropriate audit evidence for the corresponding figure for transfers and subsidies, as the municipality did not maintain an accurate and complete register of the indigent households used to determine transfers and subsidies paid in the prior year. I could not confirm the amount by alternative means. Consequently I was unable to determine whether any adjustment was necessary to the corresponding figure for transfers and subsidies, stated at R5,3 million in note 34 to the financial statements.

Employee-related cost

10. I was unable to obtain sufficient appropriate audit evidence for the corresponding figure for employee-related cost, as the municipality could not provide adequate supporting documentation for journals processed in the accounting system. Consequently, I was unable to determine whether any adjustment was necessary to the corresponding figure for employee-related cost, stated at R117,9 million in note 28 to the financial statements.

Context for the opinion

11. 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.
12. 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.
13. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Emphasis of matters

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

Restatement of corresponding figures

15. As disclosed in note 38 to the financial statements, the corresponding figures for 30 June 2020 were restated as a result of errors in the financial statements of the municipality at, and for the year ended, 30 June 2021.

Material impairment

16. As disclosed in note 4 to the financial statements, a material loss of R 6,2 million (2020: R5,9 million) was incurred as a result of a provision of impairment of irrecoverable statutory receivables from non-exchange transactions.

Other matter

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

Unaudited disclosure notes

18. 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

19. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the 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.
20. 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

21. 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.
22. 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

23. 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 selected development priorities presented in the annual performance report. I performed procedures to identify material findings but not to gather evidence to express assurance.
24. 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.
25. 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 municipality's annual performance report for the year ended 30 June 2021:

Development priorities	Pages in the annual performance report
KPA 1– basic services and infrastructure development	x – x

26. 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.

27. The material findings on the usefulness and reliability of the performance information of the selected development priorities are as follows:

KPA 1– basic services and infrastructure development

Various indicators

28. 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. I was also unable to confirm the reported achievements by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements of the indicators listed below.

No	Indicator name on the annual performance report	Indicator target on annual performance report	Reported achievement on the annual performance report
1	No of km's of surfaced road constructed as per defined project list	2 km	2 km of surfaced road constructed in Cofimvaba
2	Number of dwellings provided with connections to the mains electricity supply by the municipality	274	88 dwellings provided with connections to the mains electricity supply by the municipality; 57 at Chamama Phindela ward 7; 31 at Ngcaca ward 21 connected by Eskom

Other matter

29. I draw attention to the matter below.

Achievement of planned targets

30. 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-/overachievement 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 28 of this report.

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 municipality's compliance 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 legislation are as follows:

Annual financial statements, performance 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. Material misstatements of receivables from exchange and non-exchange transactions, consumer deposits, and contingent liabilities identified by the auditors in the submitted financial statements were subsequently corrected, but the uncorrected material misstatements and/or supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

Strategic planning and performance management

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

Asset management

35. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Expenditure management

36. Reasonable steps were not taken to prevent irregular expenditure amounting to R7,4 million, as disclosed in note 40.3 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by contravention of SCM-related legislation.

37. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R28,9 million, as disclosed in note 40.1 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by overspending of the budget.

38. Reasonable steps were not taken to prevent fruitless and wasteful expenditure, as disclosed in note 40.2 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA.

Consequence management

39. The council certified some of the unauthorised expenditure as irrecoverable without having conducted an investigation to determine the recoverability of the expenditure, in contravention of section 32(2)(a)(ii) of the MFMA.

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

Procurement and contract management

42. 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).

Other information

43. 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.
44. 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.
45. 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.
46. 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

47. 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.
48. Leadership did not adequately implement the action plans to address prior year audit findings in respect of the annual financial statements, compliance with laws and regulations, and the annual performance report. Further adequate internal controls over the monthly financial and

performance reporting processes, including year-end reporting, were not implemented, as a number of misstatements were identified in the annual financial statements and annual performance report. This is further evidence that internal control deficiencies identified and reported in the previous year were not adequately addressed, resulting in repeat findings.

Material irregularities

49. 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 in progress

50. I identified a material irregularity during the audit and notified the accounting officer, as required by material irregularity regulation 3(2). By the date of this auditor's report, I had not yet completed the process of evaluating the response from the accounting officer. This material irregularity will be included in the next year's auditor's report.

Other reports

51. In addition to the investigations relating to material irregularities, 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.

52. The Directorate for Priority Crime Investigation (Hawks) is investigating allegations of fraudulent expenditure emanating from the awarding of the contract for upgrading of gravel roads to surfaced road in extension 1. This investigation was still in progress at the date of signing this report.

Auditor-General

East London

3 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

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 Intsika Yethu 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 provide the accounting officer with a statement that I have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on my independence and, where applicable, actions taken to eliminate threats or safeguards applied.