Consolidated general report
on the local government audit outcomes

MFMA 2019-20

AUDITOR-GENERAL
SOUTH AFRICA

MFMA 2019-20

CONSOLIDATED GENERAL REPORT ON THE LOCAL GOVERNMENT AUDIT OUTCOMES

The information and insights presented in this flagship publication of my office are aimed at empowering oversight structures and executive leaders to focus on those issues that will result in reliable financial statements, credible reporting on service delivery, and compliance with legislation.

This report is also meant to enable public accountability by empowering citizens with how their municipalities have spent their budgets and performed in the year under review.

This report further highlights the advances we have made in implementing our enhanced mandate brought about by amendments to the Public Audit Act. We report on the material irregularities identified and the progress made towards their resolution in accordance with relevant laws and regulations.

The findings and recommendations in this report serve as a good basis for the incoming administration to address the challenges faced by municipalities. The outcomes should aim to close the gap between the findings in the report and the lived realities of the citizens of our country.

The impact of the covid-19 outbreak has been felt by all. We faced these challenges head-on and found new ways of collaboratively working with our auditees. We remain committed to support government and local authorities in the drive towards clean administration, which will ultimately result in a better life for the people of South Africa.

I wish to thank the audit teams from my office and the audit firms that assisted with the auditing of local government for their diligent efforts towards fulfilling our constitutional mandate and the manner in which they continued to strengthen cooperation with the leadership of government. I also wish to thank the leadership of municipalities who worked with us during the audits.

Maluleke 30/06/2021

Tsakani Maluleke
Auditor-General

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MFMA 2019-20

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ANNEXURES

Annexures containing information on the following are available on www.agsa.co.za

Annexure 1: Auditees' audit outcomes; areas qualified; and findings on performance reports, compliance, specific risk areas and unauthorised, irregular as well as fruitless and wasteful expenditure

Annexure 2: Auditees' financial health indicators, supply chain management findings and root causes

Annexure 3: Auditees' audit opinions over the past five years

Annexure 4: Assessment of auditees' key controls at the time of the audit

Annexure 5: Consultant costs

MFMA 2019-20

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AUDITOR-GENERAL SOUTH AFRICA

Auditing to build public confidence

01

EXECUTIVE SUMMARY

EXECUTIVE SUMMARY

01

The covid-19 pandemic struck local government a few months before the end of the 2019-20 financial year. It resulted in the shutdown of offices, a shift towards a covid-19 response, and inevitable delays in attending to normal municipal business. In continuing with our commitment to President Ramaphosa, we performed a real-time audit of the local government covid-19 initiatives on which we report separately in our third special report on government's financial management of the funding made available for the covid-19 response.

Our normal audit processes and timelines were severely affected by the two-month concession granted by the finance minister to local government for the submission of their financial statements. Performing a real-time audit at the same time as the normal audits and the unavoidable challenges of auditing during a pandemic further contributed to our audits running into April 2021.

Looking back to our previous general report, we delivered a very direct message that local government finances were under severe pressure and were not being managed as they should. Accordingly, it was titled *Not much to go around, yet not the right hands at the till*. We warned that drastic changes were needed to ensure that the diminishing funds available to deliver on services to citizens were used in a prudent and effective manner - and that there was credible and transparent reporting of such use to enable accountability. We also emphasised that short-term solutions were not going to bring about the change needed and were often costly and ineffective, such as the continuing use of consultants for financial reporting.

We put forward the following solutions:

- Investing in preventative controls as it is more effective than having to deal with the impact of accountability failures, such as financial loss, fraud and corruption, the misuse of public resources, and service delivery failures.
- Significantly improving monitoring, review and oversight by senior officials, municipal leaders and councils.
- Using our reports, briefings and engagements to identify the key areas that needed attention and would benefit most from preventative controls, such as our status-of-record reviews that alert municipalities to risks during the year and act as an early warning signal.
- Effecting consequences for accountability failures. Over the past few years, we have emphasised the need to create an environment in which transgressions and poor performance are dealt with appropriately to set the standards for the public service and act as a deterrent to wrongdoing. In the first year of implementation of the material irregularity process, we highlighted the value and importance of supporting this process to strengthen the accountability mechanism.

We have seen little evidence of our messages being taken to heart. The progressive and sustainable improvements required to prevent accountability failures, or deal with them appropriately when they do occur, do not exist. We also do not see the fundamentals being strengthened to enable strong financial and performance management disciplines. The responsibility to turn local government around is entirely in the hands of its leadership. Hence, the theme of this general report is *Ethical and accountable leadership should drive the required change*.

Our conclusions and call to leadership for change are based on the overall state of financial and performance management, the material irregularities we identified, and our observations in the provinces, as outlined further on.

FINANCIAL AND PERFORMANCE MANAGEMENT

This report includes information, statistics, insights and stories on the state of financial and performance management in local government. Our key observations are as follows:

Local government finances continue to be under severe pressure as a result of non-payment by municipal debtors, poor budgeting practices, and ineffective financial management. The financial position of just over a quarter of municipalities is so dire that there is significant doubt that they will be able to continue operating as a going concern in the near future. This effectively means that such a municipality does not have enough revenue to cover its expenditure and owes more money than it has. Almost half of the other municipalities are exhibiting indicators of financial strain, including low debt recovery, an inability to pay creditors, and deficits.

The impact of municipal creditors not being paid is well-known – it severely affects Eskom and the water boards, but is even more devastating for smaller suppliers. Some municipalities do not even pay over taxes such as pay-as-you-earn and value-added tax to the South African Revenue Service or transfer contributions to the pension funds of their employees. Local government loses billions of rand annually because of interest and penalties. In 2019-20 alone, the resulting fruitless and wasteful expenditure totalled R3,47 billion.

Financial statements are not only an accountability mechanism but are also used by mayors, councils, the National Treasury, banks and lenders to inform important financial decisions. After all our years of reporting shortcomings and making recommendations, municipalities have still not mastered financial reporting – only 28% could provide us with quality financial statements to audit. This also does not bode well for the in-year financial reporting done to manage the budget and finances of a municipality – we observed good practices in this regard at municipalities that constitute only 12% of the expenditure budget.

Financial reporting carries a hefty price tag at just over R5 billion. This figure is based on only the salary cost of finance units and the cost of financial reporting consultants (which accounts for 18% of the total cost). Financial reporting consultants have become permanent features in the financial reporting processes of municipalities – 74% of municipalities that had used consultants in 2018-19 again used them in 2019-20. At only 2% of municipalities, consultants were used to bridge a vacancy gap; at the rest they were appointed to provide skills the finance unit did not have. What is concerning, however, is that the use of consultants was not necessarily effective. A total of 64% of the municipalities did not provide adequate records, appointed consultants too late or did not manage their work to benefit from their appointment – effectively outsourcing responsibilities. It is time to ask difficult questions about underperformance by finance units and the value derived from the money spent on financial reporting.

Disclaimed opinions are the worst audit opinion municipalities can get, as it means that they could not provide us with evidence for most amounts and disclosures in their financial statements. We could therefore not express an opinion on the credibility of these financial statements or determine what had been done with the funds they received for the year.

In spite of all our previous messages, actions taken by oversight, initiatives by national and provincial departments, and even placing some municipalities under administration, 22 municipalities had received disclaimed opinions by 4 June 2021. Another four that were previously disclaimed have not even submitted their financial statements for auditing yet. In this report, we look at 10 disclaimed municipalities to illustrate what went wrong, what it means, and its impact on residents. At most of these municipalities, we observed leadership instability (both at political and administrative level), poor oversight by councils, significant financial health problems, protests and strikes, a lack of consequences, and interventions that were not effective.

A lack of complete and proper records inevitably leads to unreliable financial reporting during the year and at year-end, or is likely to result in substantial harm to these disclaimed municipalities' ability to deliver on their service mandate. We therefore notified the relevant municipal managers that this constitutes a material irregularity in terms of the Public Audit Act. In their response, these municipal managers are required to clearly articulate what caused the material irregularity. They must also commit to actions that will prevent any further harm and ensure that there are consequences for those responsible for the dire state of their municipality. If they do not respond appropriately or do not implement the actions to which they have committed, we will use our expanded powers to take action to remedy the situation.

The **reporting by municipalities on their performance** was even worse than their financial reporting. It is not surprising that citizens experience poor service delivery from municipalities if not even a quarter of them could provide us with quality performance reports to audit. Even after addressing our findings, just under half of the municipalities still published performance information that was unreliable or had little relevance to what they had promised to do in their strategic planning documents.

We again observed widespread **non-compliance with legislation** and reported material non-compliance at 86% of municipalities. As in prior years, non-compliance with supply chain management legislation was prevalent, significantly contributing to the irregular expenditure of R26 billion. This amount is likely to be even higher, as just over a third of municipalities were qualified on the completeness of their disclosure or were still investigating the full extent of the irregular expenditure. We could also not audit contracts and quotations worth R1,43 billion as municipalities did not provide us with the required documentation and evidence in support of the procurement processes. Accurately disclosing irregular expenditure is only the first step in the accountability chain: councils need to investigate all instances and then either regularise the expenditure or take firm steps to quantify and recover losses and discipline those responsible. This is not happening, however: at year-end the cumulative amount of irregular expenditure not dealt with stood at R79,22 billion. Municipalities' disregard for effecting consequences is also clearly shown in their lack of investigations and actions in response to our findings on potential fraud and abuse of the supply chain management system.

The lapses in financial and performance management resulted in the uninspiring **overall audit outcomes** shown below (the picture includes 32 municipalities of which we finalised the audits after the cut-off date of this report up to 4 June 2021, while the rest of the report focuses on only the audits finalised up to 23 April 2021). Most municipalities are now in a worse position than at the beginning of this administration's term in 2016-17, with 46 improving their outcomes but 61 regressing over this period.

Audit outcomes at a glance

	Unqualified with no findings	Unqualified with findings	Qualified with findings	Adverse with findings	Disclaimed with findings	Outstanding audits
2019-20 257	27	96	80	7	22	25
2018-19 257	20	94	93	6	39	5
2016-17 257	33	114	72	6	32	0

The findings from the real-time audit we performed on the covid-19 initiatives show a striking resemblance to the poor outcomes and other findings we are reporting in this general report. The impact of compromised control environments and poor financial and performance management was even more pronounced in the midst of a pandemic when vulnerable citizens relied all the more on local government support.

MATERIAL IRREGULARITIES

The poor state of financial and performance management in local government, as evidenced by the audit outcomes, resulted in material financial losses at some municipalities and substantial harm to their ability to deliver on their mandate. The amendments to the Public Audit Act, which came into effect on 1 April 2019, provide us with the mandate to report on these matters as material irregularities and to take action if municipal managers do not deal with them appropriately.

In this, the second year of carrying out our expanded mandate in local government, we significantly expanded our work by implementing the process at more auditees and moving beyond just considering financial loss. By 11 June 2021, we had issued notifications for **96 material irregularities.**

A total of 75 of the material irregularities related to non-compliance with legislation that resulted in, or is likely to result in, a material financial loss, totalling an estimated R2,04 billion. These material irregularities emerged in four key areas: **procurement and payments, interest and penalties, revenue management, and investments and assets.** These are all matters that we have been reporting as areas of vulnerability for a number of years, including as part of this year's audit outcomes. They are not complex issues, but some of the basic disciplines and processes that should be in place at municipalities, such as procuring at the best price, paying only for what was received, making payments on time, recovering the revenue owed to the state, and safeguarding assets. Good preventative controls would have made all the difference in preventing or detecting these matters before they became so material.

As mentioned earlier, we identified material irregularities where municipalities received **disclaimed opinions.** By 11 June 2021, we had issued notifications on these material irregularities to the municipal managers of 21 municipalities. As the material irregularity process is continuous in nature and not bound by the audit cycle, we continue to assess the findings from our audits that could potentially be material irregularities. If confirmed and once the municipal managers have been notified, we will report on these matters in our 2020-21 reports.

Based on the responses to the notifications and the actions being taken to resolve the material irregularities reported in the previous year, we can conclude that we are starting to see signs of a behavioural change by most of the municipal managers towards responding in a decisive and timely manner to our findings. In order to resolve material irregularities, the support of mayors and councils is crucial, but this is an area where we have not yet observed any significant uptake or commitments.

We are fully committed to implementing the enhanced powers given to our office, without fear, favour or prejudice. The success of our amended powers will become evident when a culture of responsiveness, consequences, good governance and accountability becomes the norm rather than the ideal.

PROVINCIAL MESSAGES

Every province has a unique set of circumstances and diverse solutions to their problems, but the need for leadership – also at provincial level – to step up and turn the tide is transversal. We summarise our key provincial messages here and invite you to read our detailed insights in section 6.

EC

Improvement in outcomes, but this might not be sustainable due to poor control environments

Improve and focus on controls for sustainable outcomes

FS

Lack of accountability creates a perpetual disrespect for regulations, resulting in mismanagement of resources and lack of service delivery

Accountability can be realised through decisive leadership tone

GP

Despite pockets of improvements, inadequate monitoring of preventative controls resulted in stagnant outcomes and increasing levels of unauthorised, irregular and fruitless and wasteful expenditure

Improve monitoring of preventative controls

KZN

Stagnation in audit outcomes – effective accountability and consequences not consistently enforced

Upscale implementation of preventative controls and drive consistent consequences

LP

Improvement in audit outcomes, which is mainly consultant driven and not supported by equivalent improvement in sustainable key control environment

Active leadership supervision will lead to sustainable key control environment

MP

The state of internal controls, coupled with lack of consequences for transgressions and weakened oversight, is at the centre of the deteriorating accountability in our local government

A need for leadership to act on accountability to bring about the desired change

NC

The benefits derived from implementing preventative controls are evident, but there is still a lot to be done to address undesirable audit outcomes

Sustainable change starts with the leadership will to drive it

NW

Total neglect of internal control disciplines, resulting in financial and operational collapse, weakened governance and lack of accountability

To bring about accountability, leadership must be aligned and actively lead

WC

Good financial accounting controls but inadequate preventative controls on compliance

Improvement but concerns remain

A CALL TO LEADERSHIP

There have been many calls from all quarters of the country to turn around the decline in local government. Barely a day goes by without shocking revelations of fraud and corruption, wastage, infrastructure deterioration, and municipalities that have lost the trust of the communities they serve. The most jarring is the impact of service delivery failures on the most vulnerable of our citizens – the poor.

We have seen many initiatives, plans and strategies – even direct interventions by national and provincial government – but these have had little effect. Short-term solutions such as consultants, administration and additional monitoring, rules and capacitation are just not working. As an audit office, we have also done everything within our mandate and beyond to support municipalities; we have even taken on a more direct role in the accountability process through the material irregularity process.

We are convinced that if municipal leaders at both administrative and political level, supported by their provincial leadership, are fully committed to turn around local government towards the capable, efficient, ethical and development-oriented institutions envisaged by the Constitution, improvements are bound to follow. We have seen great results where leadership has moved beyond the politics and obstacles and taken definite strides towards a better future for the communities they serve.

Mayor and council

Municipal manager and senior managers

Provincial leadership

- Tone at the top – ethical and courageous leadership, service-orientation, good governance and accountability
- Capacitate and stabilise administration
- Enable and insist on strong control environment with practical, automated and routinely executed internal controls that prevent financial loss, wastage and transgressions; and significantly improve financial and performance management and reporting
- Consistent, appropriate and swift consequences for accountability failures

We remain committed to working tirelessly within our new mandate to strengthen financial and performance management in local government, emphasising the need for accountability and doing the basics right.

We encourage councils, Parliament, provincial legislatures as well as the political and administrative leadership to play their part effectively and without fear or favour to ensure accountability for government spending and improvement in the lives of the citizens of this country. Ethical and accountable leadership should drive the desired change.

02 INTRODUCTION

INTRODUCTION 02

This report reflects on the audit outcomes of local government for the financial year ended 30 June 2020.

As in all areas of our life, the covid-19 pandemic also had a significant impact on our audits:

- The finance minister gave municipalities subject to the Municipal Finance Management Act a **two-month extension for submission of financial statements** – from 31 August to 31 October 2020. For consolidated financial statements, it was moved to 30 November 2020.
- The **legislated audit completion date** for municipalities **moved** – from 31 October to 31 December 2020. For the audits of consolidated financial statements, it was moved to 31 January 2021.
- We **balanced the normal audit of the 2019-20 financial year with a real-time covid-19 audit**, which looked at the financial management of local government's covid-19 initiatives that commenced in May 2020 and continued beyond the financial year-end of June 2020. As part of this audit, we audited payments, procurement and delivery as they occurred until 31 December 2020. Thus, we effectively also performed an advanced audit of the 2020-21 financial year at selected municipalities. The results of this real-time audit will be reported separately in our third special report on government's financial management of funding made available for covid-19 initiatives.

Over the past four years we have consistently warned the current administration against the deterioration of accountability in local government and demonstrated through the audit results the impact of accountability failures, yet poor audit outcomes remain widespread and the state of financial health continues to be severely strained.

In the previous report, the theme centred on accountability failures in local government, especially in relation to financial management. Our focus therefore remains on the importance of accountability for government spending but we have expanded the central theme of this report to *Ethical and accountable leadership should drive the desired change*.

In section 3, we thus begin by reflecting on the **audit outcomes in local government,** covering key areas of financial and performance management and reporting, the state of financial health, and compliance with key legislation.

In section 4, we draw attention to those **municipalities that received disclaimed audit opinions** on their financial statements and look at what is needed to turn around the situation at these poor-performing municipalities. These municipalities were not adequately attended to during the term of this administration and in some cases are now in an even worse position than in the first year of administration.

In section 5, we report on the second year of implementation of our expanded mandate. We provide comprehensive insight on the **material irregularity process and include the outcomes of those material irregularities identified up to 11 June 2021.**

Section 6 provides an overview of the **results and reflections per province.**

To further supplement this report, the following can be found on our website (www.agsa.co.za):

- **Detailed annexures** that provide the key results per municipality
- **Educational information** on our audit process and the terminology we use

Please note the following important matters when reading this report:

- We are responsible for auditing 257 municipalities and 20 municipal entities. To simplify our reporting and ensure that our message is focused, this report covers only the municipalities. Unless otherwise indicated, the outcomes of the municipal entities are included in the annexures to this report (which are available on our website), but not in the analysis in this report.

- We set the cut-off date for inclusion of audit outcomes in this report as 23 April 2021, at which date 57 audits were still outstanding. The number of outstanding audits excludes two metropolitan municipalities (City of Tshwane and City of Johannesburg) that were finalised shortly after the cut-off date and are thus included in the analysis in this report.

- To determine the movements from the previous year, we compared the results of the completed audits for municipalities with their results in 2018-19. In some cases, we also compared the results of the completed audits to their results in 2016-17 (the first year of the current administration).

- When studying the figures, please note that the percentages are calculated based on all completed audits of 200 municipalities, unless indicated otherwise – such as in the following instances:

    - We applied a reduced audit approach at 10 municipalities, of which the audit of only three (Modimolle-Mookgophong – LP, Govan Mbeki – MP and Maquassi Hills – NW) had been finalised by the cut-off date of 23 April 2021. We follow this approach in response to the disclaimed opinions they receive year after year and the general limitations experienced in performing audits in these environments to build efficiencies into our audit process. The impact of applying the approach is that we did not perform some of the assessments and value-adding procedures at these auditees. Where we report on these matters (such as the assurance provided by internal audit units and audit committees), the percentages are calculated based on only 197 municipalities.
    - In section 4, we also include the outcomes of audits concluded since our initial cut-off date of 23 April 2021.

STATE OF LOCAL GOVERNMENT AUDIT OUTCOMES

03

STATE OF LOCAL GOVERNMENT AUDIT OUTCOMES

03

The 2019-20 financial year on which we reflect in this report, marked the fourth year of the current administration's term. Our message over this period and specifically in the previous general report was* Not much to go around, yet not the right hands at the till *- indicative that the finances of local government are under severe pressure and are not being managed as they should.

Our message to the provincial and municipal leadership included the following:

- Drastic changes are needed to ensure that the dwindling funds available to deliver services to citizens are used in a prudent and effective manner and that there is credible and transparent reporting of such use to enable accountability.
- Short-term solutions such as the continued use of consultants for financial reporting will not bring about the change needed and are often costly and ineffective.
- The required level of supervision and monitoring by senior officials, municipal leadership and oversight is not evident – resulting in poor financial and performance management, waste and opportunities for transgressions.
- It is more effective to invest in preventative controls and measures than to deal with the impact of accountability failures, such as financial loss, fraud and corruption; the misuse of public resources; and service delivery failures. We also invited leadership and oversight to use our reports, briefings and engagements on the status-of-records reviews to identify the key areas that needed attention and that could benefit the most from preventative controls.
- There must be consequences for accountability failures. Over the past few years, we emphasised the need to create an environment in which transgressions and poor performance are dealt with appropriately to set the standards for the public service and act as a deterrent to wrongdoing. We started implementing the material irregularity process in 2019 and we highlighted the value and importance of supporting this process to strengthen the accountability mechanism.

Despite our consistent warnings against the deterioration of accountability in local government, we see little evidence of our messages receiving the earnest attention they require. This is demonstrated through the audit outcomes that show an overall regression over the period of this administration. We continue to see a deterioration in the financial health of municipalities and a lack of consequences. The poor state of financial and performance management indicates that our recommendations remain unheeded and this is in direct contrast with the concepts of public interest and accountability entrenched in our country's Constitution and the legislation that governs local government.

The political leadership and municipal officials must achieve their municipalities' objectives while acting in the public interest at all times and consistently adhering to the requirements of legislation and government policies. **Accountability is critical** and means that municipal leaders are answerable to local communities and should take responsibility for their actions, decisions and policies. Municipalities should be able to demonstrate the appropriateness of all of their actions and should have mechanisms in place to encourage and enforce adherence to ethical values and respect for the rule of law.

When going through our observations on the 2019-20 local government audit outcomes in the rest of this section, the following become clear:

- Local government finances continue to be under pressure.
- Credible financial statements are crucial to enable accountability and transparency, but municipalities are failing in this area.
- Short-term and costly solutions such as consultants are not addressing the lack of financial management and reporting skills.
- Unreliable performance reporting is adding to the challenge of poor service delivery.
- The lapse in oversight and lack of controls relating to compliance are evident in a number of areas, including supply chain management.
- Audit outcomes remain poor and have regressed over the four-year period.
- The state of internal controls is still not improving.
- Information systems and automated controls are not supporting accountability by accurately recording and processing financial and performance information.
- All role players must fulfil their assurance responsibilities.
- The root causes of the poor state of local government continue to be a slow response to our call to strengthen internal controls, vacancies and instability that hamper progress, and a lack of consequences for accountability failures.
- All should play their role to assist local government in becoming capable, efficient, ethical and development-oriented.

POOR STATE OF FINANCIAL MANAGEMENT

LOCAL GOVERNMENT FINANCES CONTINUE TO WORSEN

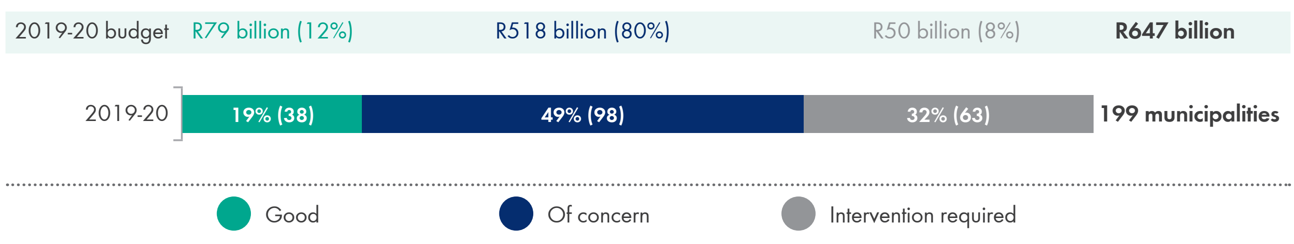
The financial statements of a municipality show how it spends its money, where its revenue comes from, its assets and the state of those assets, how much it owes creditors, how much is owed to the municipality, and whether it is expected that the money owed will be received.

The financial statements also provide crucial information on how the budget was adhered to; the unauthorised, irregular as well as fruitless and wasteful expenditure incurred; and the overall financial position of the municipality – whether its operations are financially sustainable.

The municipal managers of the 257 municipalities in the country managed an estimated expenditure budget of R719 billion in 2019-20.

We performed an analysis of the financial health of 199 municipalities based on their financial statements. The analysis shows **increasing indicators of a collapse in local government finances.** At 18 (9%) of the municipalities where the audits had been completed by the cut-off date of this report, the financial statements were not even reliable enough for analysis due to disclaimed (12 municipalities) or adverse opinions (six municipalities), while the financial statements of five were not submitted for auditing – more information on this later in the section. Section 4 of this report gives further details on municipalities with disclaimed audit opinions.

Financial health of municipalities in relation to their budget allocations



Our overall assessment of financial health was informed by the areas of **going concern, revenue, operating expenditure, capital expenditure,** and **expenditure management,** which we now look at in more detail.

Going concern

Based on their financial position, municipalities are required to disclose in their financial statements if there is significant doubt that they will not be able to continue with their operations in the near future as a going concern. Such disclosure effectively means that municipalities do not have enough revenue to cover their expenditure and that they owe more money than they have, which means that they are dependent on the equitable share provided by national government to continue operating.

In total, 53 municipalities (27%) responsible for 7% of the expenditure budget were in this dire financial position.

The map below shows the municipalities that disclosed significant doubt in their financial statements as to whether they will be able to continue operations in the near future.

NORTH WEST

- Dr Ruth S Mompati
- Mahikeng
- Maquassi
- Moses Kotane
- Tswaing

GAUTENG

- Rand West City
- Sedibeng District
- West Rand District

LIMPOPO

- Musina
- Thabazimbi
- Vhembe District

MPUMALANGA

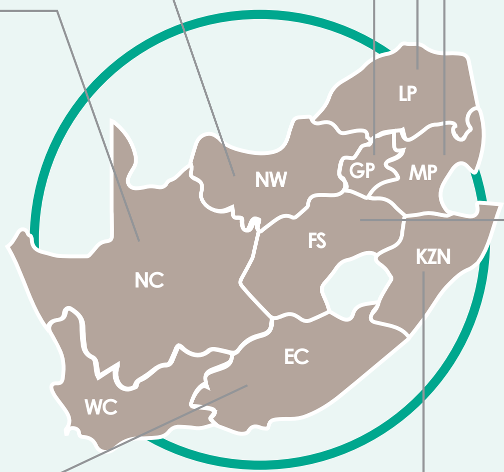
- Govan Mbeki
- Msukaligwa

NORTHERN CAPE

- Dikgatlong
- Emthanjeni
- Gamagara
- Ga-Segonyana
- Hantam
- Kai !Garib
- Kamiesberg
- Khai-Ma
- Nama Khoi
- Siyathemba
- Thembelihle

FREE STATE

- Dihlabeng
- Letsemeng
- Matjhabeng
- Mohokare
- Moqhaka
- Nala
- Ngwathe
- Phumelela
- Setsoto
- Tswelopele
- Xhariep District



EASTERN CAPE

- Amahlati
- Amathole District
- Dr Beyers Naudé
- Enoch Mgijima
- Inxuba Yethemba
- King Sabata Dalindyebo
- Kou Kamma
- Makana
- Raymond Mhlaba
- Walter Sisulu

KWAZULU-NATAL

- Mpofana
- Msunduzi
- Newcastle
- Ulundi
- uMkhanyakude District
- Umvoti
- uMzinyathi District
- uThukela District

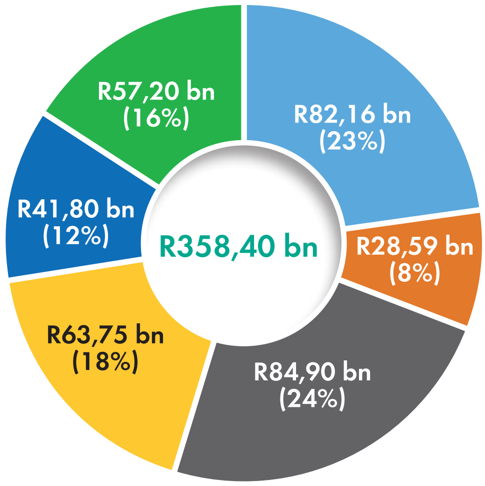
Revenue

Below we examine the revenue sources of municipalities and shortcomings in this regard.

Revenue sources

Total grant funding of
R99 billion

- Equitable share
- Total grants recognised as revenue (excluding equitable share)



Total own revenue of
R259,40 billion

- Property rates
- Service charges – electricity revenue
- Service charges – water revenue
- Other revenue (e.g. investment income, rentals, licences, traffic fines)

INDICATORS	
*Average irrecoverable debt	63%
*Average debt-collection days	203 days
Debt written off in year	R39,35 billion

→ We estimate that only **R103,76 billion (40%) of this revenue will be recoverable**

** Excludes18 municipalities whose financial statements were not reliable enough for financial analysis (i.e. those with adverse or disclaimed audit opinions)*

The main source of revenue for most municipalities is the rates and taxes paid by property owners and consumers of municipal services **(own revenue)**.

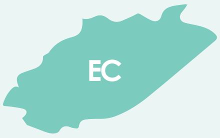
National government also provides **funding through grants:**

- The equitable share is a financial allocation that enables municipalities to provide basic services to poor households and to enable municipalities with limited own resources to afford basic administrative and governance capacity and perform core municipal functions.
- Conditional grants are provided to use for a specific purpose and in compliance with specified requirements.

The problem with own revenue is that municipal consumers are not paying what they owe – this has been a trend for many years and continues to worsen. Municipal debt recovery is expected to deteriorate further in 2020-21 because of the economic downturn in the wake of the covid-19 pandemic. This means that on paper the revenue of a municipality might look healthy but the money does not reach the bank – we estimate that only 40% (R103,76 billion) of own revenue is recoverable. Municipalities are therefore often dependent on the money they receive from national government to stay afloat.

But municipalities do not always play their part either – not all revenue owed is billed and poor debt-collection practices are common. In addition to raising these concerns through audit findings, we also issued material irregularity notifications where municipalities were suffering material financial losses as a result.

Examples illustrating revenue challenges of municipalities



Nelson Mandela Bay Metro did not charge interest on debtors with long-term debt arrangements, which means that revenue was being lost. The estimated revenue lost amounted to R11,16 million. An investigation revealed that the accounting system had been incorrectly set up. The system was re-programmed and, from February 2020, interest is now raised on a monthly basis.

Msunduzi continued to have challenges in collecting old debt as evidenced by the high debt-collection period of 154 days. This led to the municipality not being able to recover R2,56 billion (57%) of the outstanding debt of R4,5 billion. The provision for impairment also increased by 28% from the previous year, indicating that consumers are struggling to settle their outstanding debts.

Due to rising costs to provide municipal services in a financially sustainable manner, **Drakenstein** had to increase its tariffs. The increases and electricity disconnection where payments could not be made resulted in community dissatisfaction and demonstrations. The indigent policy also had to be updated. The full equitable share grant is used for indigent services as 50% of the municipality's population is now indigent.

Operating expenditure

With limited cash in the bank, municipalities prioritise the payment of salaries and councillor remuneration. They then pay municipal suppliers with what is left, including Eskom and the water boards that are essential for the supply of basic services. At some municipalities, returns and payments to the South African Revenue Service are also delayed and there are even municipalities that do not transfer contributions to the pension funds of their employees.

The impact of such late payments is as follows:

- It affects the cash flow of local government suppliers, which is in sharp contrast with the objectives of stimulating the economy and supporting especially smaller businesses. Suppliers and contractors stop delivering to municipalities, resulting in projects not being completed and performance objectives not being achieved. However, Eskom and the water boards are in the difficult situation of being required to continue delivering services despite non-payment.

- Interest and penalties charged on late payments result in material financial losses, which can be ill afforded. We issued material irregularity notifications on these material financial losses. The situation can be turned around through credible funding plans, debt arrangements with suppliers and careful expenditure management; and by not taking on projects and commitments without the required funds being available.
- Apart from increasing the liabilities in the municipalities, if pension fund contributions are not paid, there is a potentially detrimental impact on the employees when they retire as funds may not be available to pay their pension benefits. Failure to pay employees' pension fund contributions to their respective funds is a transgression of section 13A of the Pension Fund Act.

We further expand on the **expenditure challenges of municipalities** below.

SALARIES AND WAGES#	
Salaries and wages (including councillor remuneration) In total, 46% of the estimated recoverable revenue and equitable share allocation was used to pay salaries and wages as well as councillor remuneration	R74,40 billion

ESKOM ARREARS#	
Total arrears (including interest owed of R2,26 billion)	R12,41 billion
In arrears over 120 days	R9,84 billion
Interest paid to Eskom during the year	R4,43 billion
(Municipal managers were notified of 12 material irregularities in this regard)	

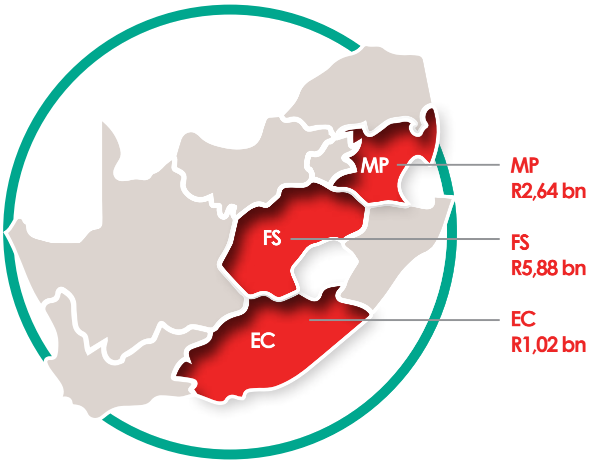
WATER BOARDS ARREARS#	
Total arrears (including interest owed of R0,07 billion)	R8,78 billion
In arrears over 120 days	R7,46 billion
Interest paid to water boards during the year	R0,01 billion
(Municipal managers were notified of 3 material irregularities in this regard)	

CREDITORS*	
Average creditor-payment period	209 days
Creditor-payment period > 30 days	158 (87%)

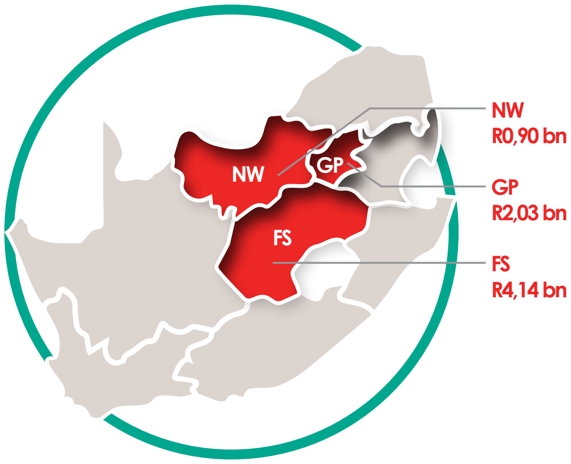
INFRASTRUCTURE ASSETS#	
Value of infrastructure assets that should be maintained and safeguarded	R366,33 billion
Expenditure on maintenance (only 2% of expenditure budget, as opposed to norm of 8%)	R13,61 billion

 # Excludes 57 outstanding audits
** Excludes 18 municipalities where the financial statements were not reliable enough for financial analysis (i.e. those with adverse or disclaimed audit opinions)*

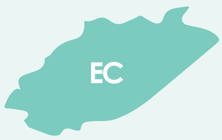
Highest contributors to Eskom arrears – R12,41 bn



Highest contributors to water boards arrears – R8,78 bn



Example reflecting expenditure challenges of municipalities



Amathole District was assessed by consultants appointed under the previous municipal manager to be a category 7 municipality from a category 6 municipality in 2017. This assessment was approved by the council, resulting in an additional 936 positions being available on the municipality's organogram as well as some staff being paid at a higher level. In 2019, the assessment of the municipality as category 7 was confirmed to be incorrect. The municipal manager and senior managers are now being paid outside the upper limits for remuneration packages set out in the Government Gazette because of this incorrect categorisation.

Capital expenditure

The majority of capital expenditure (the money government spends on buying, maintaining or improving fixed assets) is financed through conditional grants. Although there is a great need for these grants to finance infrastructure projects, they are often underspent, mostly because of poor project management. In some cases, the money is also not used for its intended purposes. The underspending on these grants means that valuable infrastructure assets meant for service delivery are not maintained, resulting in a deterioration in the quality of services to citizens, who continue to be frustrated with inadequate service delivery.

Management of infrastructure grants

AVAILABLE TO SPEND (PERCENTAGE OF FUNDS SPENT)	UNDERSPENDING BY MORE THAN 10%	USED FOR INTENDED PURPOSE
MUNICIPAL INFRASTRUCTURE GRANT - 168 MUNICIPALITIES		
R10,84 billion (88%)	63 municipalities (38%)	154 municipalities (92%)
PUBLIC TRANSPORT NETWORK GRANT - 10 MUNICIPALITIES		
R5,2 billion (78%)	5 municipalities (50%)	10 municipalities (100%)
URBAN SETTLEMENTS DEVELOPMENT GRANT - 7 METROS		
R11,61 billion (87%)	4 metros (57%)	7 metros (100%)
REGIONAL BULK INFRASTRUCTURE GRANT - 26 MUNICIPALITIES		
R1,74 billion (74%)	11 municipalities (42%)	23 municipalities (88%)
WATER SERVICES INFRASTRUCTURE GRANT - 62 MUNICIPALITIES		
R3,42 billion (80%)	31 municipalities (50%)	51 municipalities (82%)

Overall, 83% of municipalities materially complied with the Division of Revenue Act in the management of the infrastructure grants.

The municipalities that underspent grants by more than 60% are provided next. Except where otherwise indicated, the remaining funds were cash-backed (meaning that it was still in the bank at year-end).

MUNICIPAL INFRASTRUCTURE GRANT	
Eastern Cape	Amahlathi (69%) Enoch Mgijima (67%)
KwaZulu-Natal	Mandeni (60,1%)
North West	Ratlou (77%)
Western Cape	George (80%) Prince Albert (73%)

The only municipality that underspent the public transport network grant by more than 60% was Nelson Mandela Bay Metro, with underspending of 70%.

REGIONAL BULK INFRASTRUCTURE GRANT	
Free State	Mohokare (70%) (remaining funds not fully cash-backed)
Limpopo	Mogalakwena (71%) (remaining funds not fully cash-backed)
Mpumalanga	Msukaligwa (95%)
Western Cape	Witzenberg (99%)

WATER SERVICES INFRASTRUCTURE GRANT	
Free State	Setsoto (79%) (remaining funds not fully cash-backed) Metsimaholo (60,2%)
Gauteng	Merafong City (81%)
Mpumalanga	Bushbuckridge (65%)
Northern Cape	Nama Khoi (86%) Gamagara (66%) Kamiesberg (63%) (remaining funds not fully cash-backed)
Western Cape	Cederberg (86%) (remaining funds not fully cash-backed)

The planned completion dates for 74 of the 362 projects funded by the municipal infrastructure grant were not met and/or the project stage of completion was not assessed. We also identified supply chain management findings at 130 of these projects.

Example showing how poor project management has a negative effect on service delivery

The council of **OR Tambo District** suspended the municipal manager in June 2020 on allegations of financial misconduct, which included the approval of advance payments to an implementing agent and other service providers for goods or services not received relating to the delivery of water and sanitation infrastructure projects for the district. The projects amounting to R105 million were funded by the municipal infrastructure and regional bulk infrastructure grants. The municipality did not adequately monitor the performance of the contactors responsible for the construction of these projects. This resulted in some projects not being completed on time and other projects exceeding the contract values. The quality of the infrastructure projects is a further concern, as some of the projects were reported as being complete but no water services were supplied to the communities and some projects were not working as intended. At the Qokolweni water supply scheme project, no feasibility study was performed to identify that there was water in the area before the project commenced. The project was reported as complete but was non-functional, leaving the community without water.

Expenditure management

Although there are limited funds available, we still find municipalities not diligently and carefully managing funds (as is apparent from the material irregularities identified on payments for goods and services not received, as detailed in section 5 of this report). Many municipalities also do not follow the required procurement processes to ensure that the best price is paid for goods and services – the details of which are provided later on in this section.

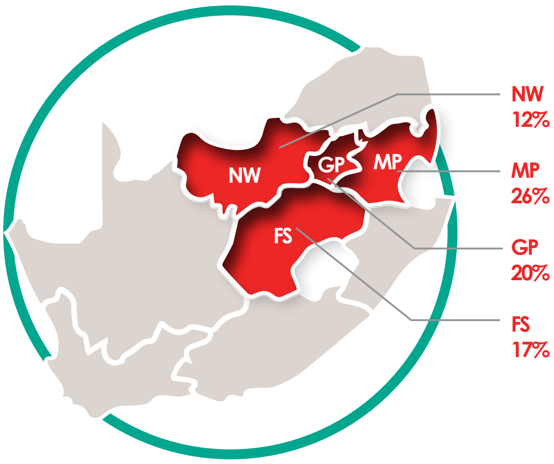
Another **indicator of the poor management of funds is the fruitless and wasteful expenditure incurred**, which has grown to R3,47 billion this year (including R1,50 billion of municipalities of which the audits had not been completed by the cut-off date of this report). The fruitless and wasteful expenditure incurred by the municipalities of which the audits had been completed by the cut-off date amounted to R1,97 billion, of which R1,83 billion represented 2019-20 expenditure. The expenditure incurred in 2019-20 constituted 0,3% of the total expenditure budget.

The fruitless and wasteful expenditure incurred by 174 municipalities of which the audits had been completed by the cut-off date of this report, was due to the following:

- Interest and penalties (69%) – R1,35 billion
- Litigation and claims (2%) – R0,04 billion
- Other (e.g. payments to suspended employees and write-off of assets that were never used) (29%) – R0,58 billion

The fruitless and wasteful expenditure could be higher because nine (5%) of the 200 municipalities where we had completed audits were qualified on the **incomplete disclosure** of fruitless and wasteful expenditure.

Highest contributors to fruitless and wasteful expenditure – R3,47 bn



TOP CONTRIBUTORS TO FRUITLESS AND WASTEFUL EXPENDITURE
Emalahleni (MP) – R0,33 billion *
City of Tshwane Metro (GP) – R0,30 billion
Matjhabeng (FS) – R0,28 billion
Emfuleni (GP) – R0,23 billion *
Govan Mbeki (MP) – R0,20 billion
Naledi (NW) – R0,17 billion *
Lekwa (MP) – R0,12 billion *
Nelson Mandela Bay Metro (EC) – R0,09 billion
Mopani District (LP) – R0,07 billion *
Msukaligwa (MP) – R0,07 billion
Matlosana (NW) – R0,07 billion *

** Audits still outstanding or finalised after cut-off date of report*

IMPACT OF POOR FINANCIAL MANAGEMENT

Stemming from the financial health woes experienced, there were many municipalities that owed creditors more money than what was available in the bank. As a result, these municipalities had to dig into the next year's budget to cover the current year's expenditure. The total deficit in local government was R7,44 billion, and expenditure exceeded revenue at year-end at 55 municipalities.

Below we look at a couple of the **specific effects of poor financial management** in local government.

CREDITORS GREATER THAN AVAILABLE CASH	
Creditors > available cash at year-end	89 (49%)
Total creditors at year-end	R60,93 billion
Cash available at year-end	R44,76 billion
Municipalities with highest percentages of creditors greater than available cash: • Phumelela (FS) – 322 985% (creditors = R278 823 227; cash available at year-end = R86 327) • Emthanjeni (NC) – 45 991% (creditors = R95 880 042; cash available at year-end = R208 475) • Victor Khanye (MP) – 36 282% (creditors = R511 391 499; cash available at year-end = R1 409 487)	

CURRENT LIABILITIES GREATER THAN 10% OF NEXT YEAR'S BUDGET*	
Current liabilities > 10% of next year's budget at year-end (next year's budget will therefore pay for expenditure of prior years)	176 (97%)
Current liabilities > 50% of next year's budget at year-end	52 (29%)

UNAUTHORISED EXPENDITURE	
Unauthorised expenditure (including R7,39 billion based on outstanding audits at cut-off date)	R22 billion
Unauthorised expenditure incurred by 104 municipalities relating to non-cash items#	R9,27 billion
Unauthorised expenditure could be higher as 14 (7%) of the 200 municipalities where we had completed audits were qualified on the incomplete disclosure of unauthorised expenditure	

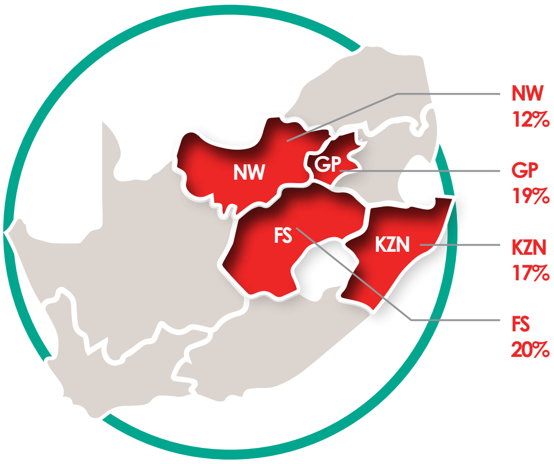
 # Excludes 57 outstanding audits

** Excludes 18 municipalities where the financial statements were not reliable enough for financial analysis (i.e. those with adverse or disclaimed audit opinions)*

Further exploring the unauthorised expenditure, we see that 175 municipalities incurred such expenditure (this includes 40 with outstanding audits based on unaudited financial statements as well as audits subsequently finalised). This means that municipalities incurred **expenditure without the council having made provision for it in the approved budget or the spending did not meet the conditions of a grant.**

As mentioned earlier, most of the expenditure related to non-cash items. Municipalities' budgets make provision for items that do not involve actual cash inflow or outflow. We term these 'non-cash items', which include accounting entries such as reducing the value at which assets are reflected in the financial statements (asset impairments) and providing for other types of potential financial losses. This is not actual expenditure but rather an accounting requirement that enables municipalities to assess the true value of their assets (such as equipment or debtors). It is important for municipalities to correctly budget for these non-cash items to show their true financial state.

Highest contributors to unauthorised expenditure – R22 bn

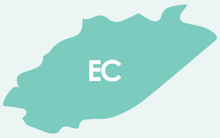


TOP CONTRIBUTORS TO UNAUTHORISED EXPENDITURE
City of Tshwane Metro (GP) – R2,25 billion
eThekwini Metro (KZN) – R1,78 billion
Emfuleni (GP) – R1,65 billion *
Matjhabeng (FS) – R1,50 billion
Mangaung Metro (FS) – R1,17 billion *
Vhembe District (LP) – R0,73 billion
Msunduzi (KZN) – R0,56 billion
Govan Mbeki (MP) – R0,55 billion
Enoch Mgijima (EC) – R0,48 billion
Matlosana (NW) – R0,48 billion *

** Audits still outstanding or finalised after cut-off date of report*

Municipalities should ensure that they can deliver services based on available resources; yet they continue to promise a level of service delivery and projects they cannot fund and to submit budgets to the council that balance but are effectively based on money that they will not be able to bring in. As a result, the spiral of non-delivery continues. The impact of this is felt directly by the communities and businesses the municipalities serve – particularly when it comes to inadequate access to basic services and the lack of economic development. This also places pressure on the country's finances overall – which in this economic climate, we can ill afford.

Examples illustrating impact of poor financial management



Amathole District had outstanding payables at year-end amounting to R563 million, which exceeded the cash available of R192 million. The outstanding creditors represented one-third of the next year's budget of R1,6 billion, which will now be used to pay those creditors instead of funding new service delivery priorities.

The unauthorised expenditure of **Msunduzi** increased by 232% (from R170 million to R565 million). The unauthorised expenditure was a result of poor budgeting, specifically relating to the increase in debt impairment due to the impact of the covid-19 pandemic. Currently the municipality would not be able to meet its existing obligations with the funds available.

Gamagara took an average of 172 days to collect money owed by customers, placing pressure on its ability to pay creditors. The municipality took 487 days to pay suppliers, ultimately affecting its ability to meet the service delivery needs of the community. The current creditors balance exceeded the current cash balance by 805,8%, indicating that the municipality will not be able to settle most of its short-term obligations.

SERIOUS WEAKNESSES IN FINANCIAL REPORTING

Financial statements are used by the municipal council to call the municipal manager to account and to make decisions on the financial management of the municipality. They are also used by creditors, banks and rating agencies to determine the level of risk in extending debt to a municipality and by the public to know how well the municipality is using the rates and taxes they pay to provide services.

Financial statements are credible, and thus reliable, when they are free of material misstatements (errors or omissions). However, 72% of municipalities submitted financial statements of a poor quality for auditing. These municipalities place reliance on the external audit process to identify misstatements. The poor quality of the financial statements received also reflects poorly on the credibility of in-year financial reporting and monitoring.

Notwithstanding the extended timelines granted for submitting financial statements in the current year, 11% of municipalities could not submit their financial statements on time. This is a slight increase from the 9% of municipalities that did not submit their financial statements on time at the beginning of the current administration's term. **The late submission of financial statements is one of the main reasons for the late finalisation of audits.**

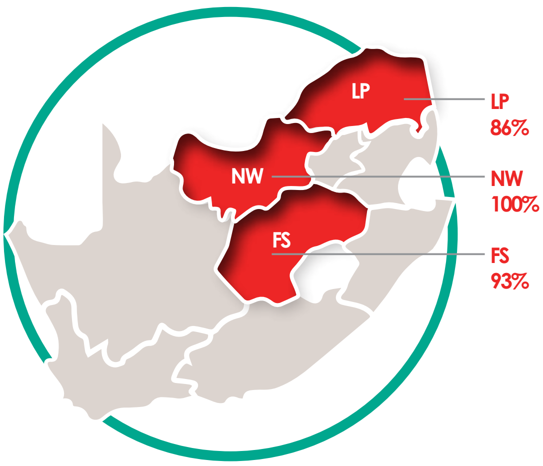
Twelve of the municipalities of which the audits had been completed by the cut-off date of this report, obtained disclaimed audit opinions. These municipalities could not provide us with evidence for most of the amounts and disclosures in their financial statements. We were therefore unable to conclude or express an opinion on the credibility of their financial statements. The financial statement stories of these municipalities remain untold or are unreliable, with their communities and creditors left in the dark with regards to their financial affairs. This is what makes a disclaimed opinion the worst audit opinion a municipality can get. In section 4 of this report, we focus on some municipalities with a history of disclaimed opinions.

TIMELY SUBMISSION AND QUALITY OF FINANCIAL STATEMENTS	
Submission of financial statements by legislated date (all auditees)	89%
Quality submission for auditing	28%

MATERIAL MISSTATEMENTS IN FINANCIAL STATEMENTS	
Irregular expenditure	28%
Property, infrastructure and equipment	25%
Receivables	25%
Expenditure	25%
Revenue from exchange transactions	24%

MUNICIPALITIES THAT HAD NOT SUBMITTED THEIR 2018-19 FINANCIAL STATEMENTS FOR AUDITING BY 23 APRIL 2021	
Free State	Maluti-A-Phofung, Masilonyana and Tokologo
Northern Cape	Phokwane and Renosterberg

Provinces that submitted poorest quality financial statements



THE HIGH COST OF POOR FINANCIAL MANAGEMENT AND REPORTING

Most municipalities appoint consultants for financial reporting as their own finance employees lack the skills required to prepare financial statements and schedules in support of those financial statements. The inability of these municipalities to master credible financial reporting means that they appoint consultants year after year, without ensuring that skills are transferred to municipal staff – and so the cycle never ends. This over-reliance on consultants leads to a high total cost of financial reporting.

Despite our warnings throughout the past four years, there is **little evidence suggesting that over-reliance on consultants will soon be a thing of the past.** In 2019-20, 156 municipalities (78%) appointed financial reporting consultants; an increase from 124 municipalities (62%) that used consultants at the beginning of the current administration's term. Consultants are also not rotated, as shown by the same consultants used in the previous year being re-appointed at 74% of the municipalities. In some cases, consultants continue to accept appointments although it is unlikely that they will add value to the municipalities; for example, where there is a lack of or inadequate records and documents or they are appointed too late. Consultants should therefore be cognisant of the circumstances at a municipality and evaluate whether their services will be effective before accepting any engagements.

Over R5 billion was spent on financial management and reporting for the year – this includes only the salary cost of finance units and the cost of consultants used for financial reporting services. In addition, the multiple interventions by national and provincial government, including placing municipalities under administration, are costly exercises. However, the return on investment is not yet apparent and we remain concerned about the high amount spent on consultants to support financial reporting – especially at municipalities where finance units are fully resourced.

Cost of financial reporting = R5 594 million

Salary cost of finance units **(R4 567 million)** + cost of consultants used by 172 municipalities for financial reporting services **(R1 027 million)**

Consultant cost constitutes 18% of total financial reporting cost

The table below reflects the financial reporting costs per province. In four provinces, consultant costs constituted more than 20% of the total financial reporting costs.

Province	Financial reporting consultant cost	Finance unit salary cost	Total financial reporting cost	Consultants as percentage of total financial reporting cost
Eastern Cape	R117,18 million	R601,80 million	R718,98 million	16%
Free State	R46,83 million	R280,28 million	R327,11 million	14%
Gauteng	R230,21 million *	R1 270,25 million	R1 500,46 million	15%
KwaZulu-Natal	R146,23 million	R717,02 million	R863,25 million	17%
Limpopo	R172,53 million	R511,05 million	R683,58 million	25%
Mpumalanga	R63,73 million	R189,65 million	R253,38 million	25%
Northern Cape	R97,16 million	R184,05 million	R281,21 million	35%
North West	R122,88 million	R168,24 million	R291,12 million	42%
Western Cape	R30,61 million	R644,76 million	R675,37 million	5%
Total	**R1 027,36 million**	**R4 567,10 million**	**R5 594,46 million**	**18%**

* *R198,43 million relates to City of Tshwane Metro*

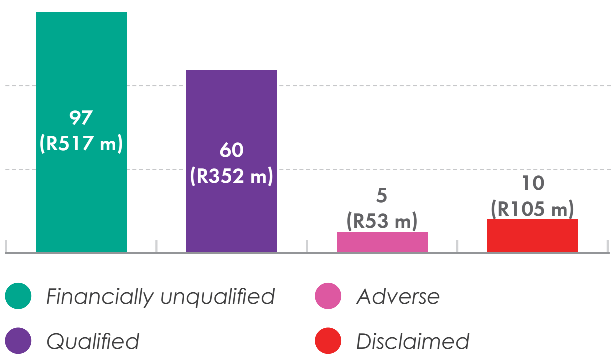
Most of the consultant costs were incurred on asset management services (R417,95 million by 96 municipalities), followed by the preparation or review of financial statements (R297,54 million by 127 municipalities) and tax services (R167,44 million by 51 municipalities).

Municipalities used consultants for the following reasons:

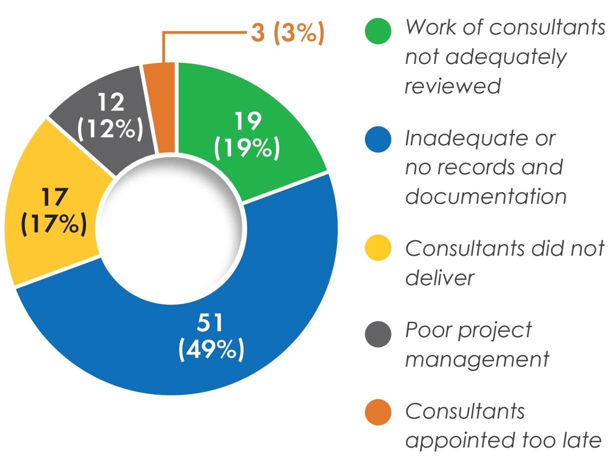
- Lack of skills at 117 municipalities (68%)
- Combination of lack of skills and vacancies at 52 municipalities (30%)
- Vacancies at 3 municipalities (2%)

As indicated earlier, the expected benefits from using consultants are not always apparent. We identified material misstatements in 59% of the submitted financial statements and/or supporting schedules that had been prepared by consultants. Below we detail the financial statement audit outcomes where consultants were used and look at why they were not effective.

Financial statement outcomes where consultants were used

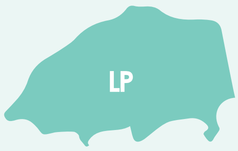


Reasons why consultants were ineffective



The over-reliance on consultants and the high total cost of financial reporting can be seen in the examples below.

Inkosi Langalibalele paid R13,9 million to consultants in the 2019-20 financial year, most of which was for the preparation and review of financial statements and the fixed asset register. The combined annual salary of finance staff employed for the same functions was R14,22 million. Consultants were mainly utilised due to a lack of skills within the municipality's finance unit. Repeat material misstatements were identified in the consultants' area of responsibility. This was because consultants did not deliver on the services for which they were engaged by the municipality. The use of consultants did therefore not have a positive impact on the audit outcome as the municipality regressed to a disclaimed audit opinion.



Sekhukhune paid R24,75 million to consultants in the 2019-20 financial year, most of which was for financial reporting services. This despite the finance staff of the municipality also being paid combined annual salaries of R70,84 million. There were enough officials to perform some of the duties performed by consultants, which would have reduced the consultant cost. However, officials lacked the appropriate skills, with no skills transfer taking place from consultants to staff, as consultants are appointed year after year. We assessed the municipality's finance unit as requiring intervention to prepare regular, accurate and complete financial and performance reports that were supported by reliable information, yet this was the main area of operation for the consultants. The involvement of consultants did therefore not improve the audit outcome as the municipality remained qualified.

However, some municipalities do effectively use consultants, as can be seen in the example below.

What works well at **Bergrivier** is the level of review performed by the chief financial officer and the accessibility of the consultant. Although consultants are responsible for the overall preparation of financial statements, any audit issues are addressed by the chief financial officer. The chief financial officer also does an overall review of all journals posted by the consultant and reviews the financial statements with the consultant. The templates used by the consultant are logical, easy to review, and included in an audit file.

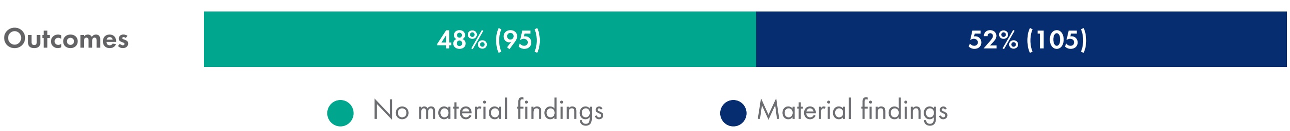
UNRELIABLE PERFORMANCE REPORTING – ADDING TO THE CHALLENGE OF POOR SERVICE DELIVERY

Municipalities are required to measure and report on their actual service delivery performance against the objectives and targets that have been predetermined in their integrated development plan and/or service delivery and budget implementation plan.

However, most municipalities had inadequate systems to collate and report on their performance information and officials did not understand or could not apply the performance management and reporting requirements. Four municipalities did not submit performance reports for auditing and only 24% of municipalities were able to submit performance reports without material misstatements or limitations.

Performance reports with material flaws are not credible enough for the council or the public to use in holding municipalities accountable for the service delivery promises they make in their strategic planning documents.

Status of performance reporting



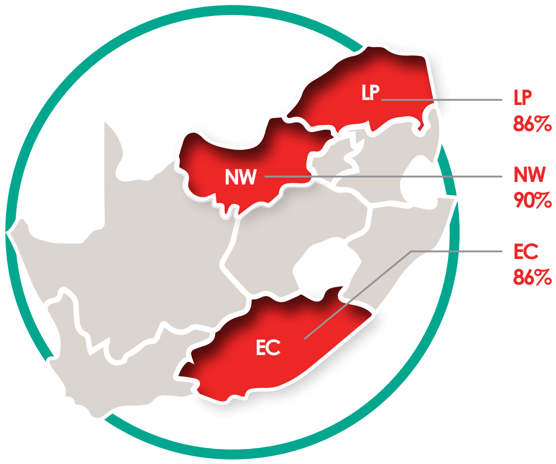
PREPARATION AND QUALITY OF PERFORMANCE REPORTS	
Preparation of performance reports	98%
Quality submission for auditing	24%

FINDINGS ON PERFORMANCE REPORTS	
Achievement reported not reliable	41%
Performance indicators and targets not useful	39%
No underlying records or planning documents	4%

MOST COMMON USEFULNESS FINDINGS

18%	17%	13%	10%
Indicators/targets not consistent	Indicators/targets not well-defined	Indicators/targets not verifiable	Measures taken to improve performance not corroborated

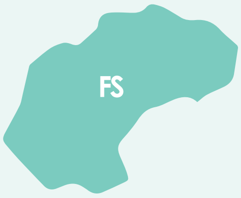
Provinces that submitted poorest quality performance reports



The following seven municipalities (4%) submitted performance reports without complete and accurate underlying records. As a result, we could not validate the services delivered as reported by these municipalities in their performance reports.

Eastern Cape	Sundays River Valley and Sakhisizwe
Mpumalanga	Thembisile Hani
Northern Cape	Nama Khoi, Khai-Ma, Kai !Garib and Karoo Hoogland

Examples showing link between unreliable performance planning and reporting and inadequate service delivery



At **Metsimaholo**, a project to construct the Refeng Kgotso sports complex was awarded in December 2019 with a planned project duration of 36 months and a budgeted cost of R7,54 million. The actual project expenditure at 30 June 2020 stood at R5,17 million; and additional payments of R1,86 million were made up to May 2021. During a site visit in February 2021, discrepancies were identified between the actual work done and the work certified as complete, although most of the project costs had been paid. For example, some invoices indicated that the fence around the complex and the tennis courts in the complex had been completed, but upon physical inspection these items were still in the early stages of construction.

At **Kai !Garib**, the reported achievements against planned service delivery objectives, indicators and targets as contained in the performance report could not be supported by underlying records. This includes an approved service delivery and budget implementation plan that was not submitted for auditing. As a result, we could not verify that what was reported as planned services was correct and we could not confirm that the reported achievements actually occurred. The lack of a proper performance planning and management system is one of the contributing factors to the current service delivery challenges experienced by the municipality. For example, the municipality has limited water pumps that are working due to poor maintenance and the community continues to struggle with water shortages.

WIDESPREAD NON-COMPLIANCE WITH LEGISLATION

Legislation serves to set parameters within which local government budget allocations may be utilised, with a view to stretch resources optimally, thereby enhancing service delivery to citizens. It sets out the dos and don'ts that every official entrusted with the financial affairs of local government ought to observe to ensure the realisation of service delivery promises.

Yet, **municipalities and their staff continue to disregard compliance with legislation.** We identified non-compliance with legislation at 172 municipalities (86%). The lapse in oversight and lack of controls relating to compliance were evident in a number of areas, including procurement and contract management; the quality of financial statements; and the prevention of unauthorised, irregular and fruitless and wasteful expenditure.

Municipalities therefore need to have mechanisms in place to identify applicable legislation as well as changes to legislation, assess the requirements of legislation, and implement processes to ensure and monitor compliance with legislation to enable sound financial management practices. Municipal managers ought to provide effective and ethical leadership, exercise oversight of compliance with legislation, and effect consequences against officials responsible for non-compliance.

Status of compliance with legislation

MOST COMMON AREAS OF NON-COMPLIANCE	
Procurement and contract management	74%
Quality of financial statements	73%
Prevention of irregular expenditure	72%
Prevention of unauthorised as well as fruitless and wasteful expenditure	60%
Effecting consequences	57%

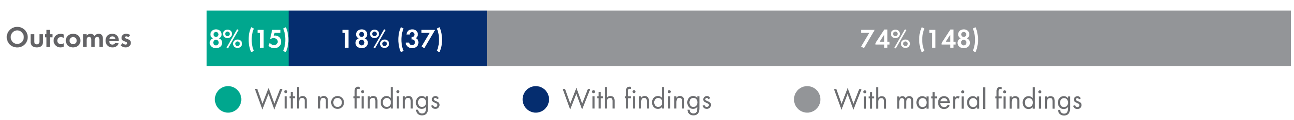
OTHER NOTABLE NON-COMPLIANCE AREAS	MOST COMMON FINDINGS	
Expenditure management at 49% of municipalities	Payments to creditors not settled within 30 days from receipt of an invoice	45% (90)
	No or inadequate management, accounting and information system for expenditure	9% (18)
Strategic planning and performance management at 40% of municipalities	Performance management system and related controls not maintained or inadequate	28% (55)
	No performance management system established	5% (10)
Asset management at 36% of municipalities	Ineffective system of internal control for assets	29% (57)
	No or inadequate management, accounting and information system for assets	11% (21)
Revenue management at 28% of municipalities	Ineffective system of internal control for revenue	22% (44)
	No or inadequate management, accounting and information system for revenue	10% (20)

We now look in more detail at three specific areas of non-compliance, namely **supply chain management, irregular expenditure,** and **effecting consequences.**

SUPPLY CHAIN MANAGEMENT

It is of great concern that material non-compliance with supply chain management legislation by municipalities is still very high.

Status of compliance with supply chain management legislation



Limitations

We were unable to audit procurement of R1 433 million due to missing or incomplete information at 29 municipalities (15%).

The impact of these limitations included the following:

- It is not known whether any part of the R1 433 million might represent irregular expenditure or material irregularities.
- There was no evidence that municipalities had followed a fair, transparent and competitive process for all awards. Should unsuccessful bidders request information on the process, also for possible litigation purposes, it would not be available.
- Poor record management created an environment in which it was easy to commit and conceal improper or illegal conduct.

The municipalities where we experienced the biggest limitations, accounting for 84% of the R1 433 million, were:

- Mogalakwena (LP) – R893 million: Contract management documents relating to 46 contracts were not provided for auditing due to a lack of adequate record keeping. The most significant contracts related to water services projects (R755 million), sports stadium projects (R71 million), and professional engineering services relating to supervision on water treatment and concrete work projects (R67 million).
- City of Tshwane Metro (GP) – R103 million: Inadequate record management as the contract with the service provider responsible for maintaining copies of all issued bids had expired and a new contract had not yet been concluded.
- Kagisano-Molopo (NW) – R73 million: Tender documents relating to six contracts and 25 quotations were not provided for auditing due to poor record management. The most significant of these contracts related to security services (R34,7 million), Municipal Standard Chart of Accounts implementation (R17,0 million), and the Vragas sports facility (R16,9 million).
- Dr Ruth Segomotsi Mompati District (NW) – R73 million: Bidding documents relating to five tenders or contracts were not provided for auditing due to a lack of an adequate record-keeping system. The most significant contracts related to the Mamusa drought-relief programme (R23,8 million), equipping of boreholes and tankering provision (R23,6 million), and professional engineering services for Taung (R11,3 million).
- Siyathemba (NC) – R64 million: Tender documents pertaining to three contracts could not be provided as a result of poor record keeping by management.

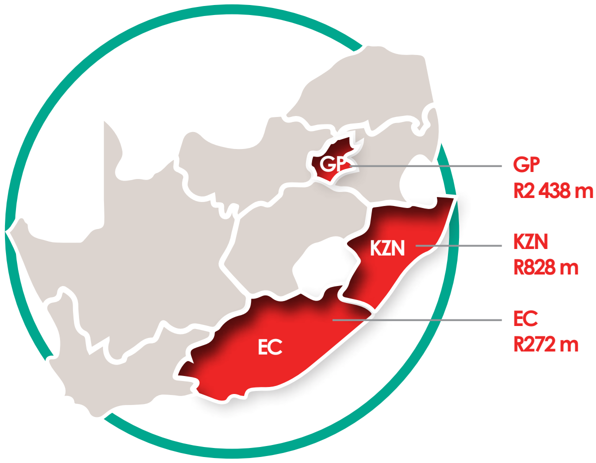
Awards to employees, councillors, close family members and other state officials

The Municipal Supply Chain Management Regulations prohibits the awarding of contracts to, and acceptance of quotations from, employees, councillors or other state officials, or entities owned or managed by them, if they are in the service of the municipality or any other state institution.

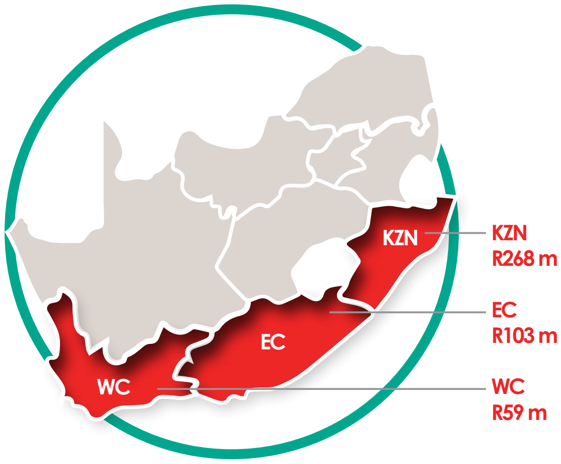
Awards to close family members of persons in the service of the state, whether at the municipality or another state institution, are not prohibited. However, such awards of more than R2 000 must be disclosed in the financial statements of the auditee for the sake of transparency and as required by supply chain management regulation 45. Furthermore, such awards might create conflicts of interest for employees or councillors.

AWARDS/FINDINGS	Number of municipalities with awards	Amount
Prohibited awards to other state officials	52% (104)	R3 619 million
Prohibited awards to employees and councillors	15% (29)	R19 million
At five municipalities (3%), awards were made to councillors		
Awards to close family members of employees	36% (71)	R527 million
At 16 municipalities (8%), awards to close family members were not disclosed in the financial statements as required		

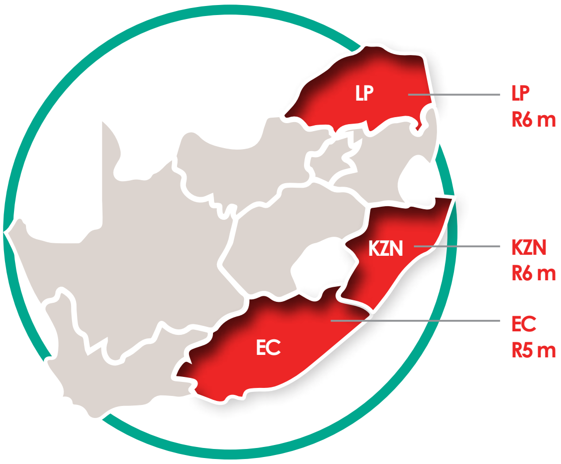
Highest contributors to prohibited awards to other state officials – R3 619 m



Highest contributors to awards to close family members – R527 m



Highest contributors to prohibited award to employees and political office-bearers – R19 m



False declarations by suppliers and non-disclosure by employees

Despite raising concerns year after year about contracts being awarded to employees and their families, we still find that awards are made without the necessary declarations of interest.

FINDINGS	Number of municipalities	Number of suppliers/ employees	Amount
Suppliers owned or managed by employees of another state institution made false declarations	23% (45)	350	R882 million
Suppliers owned or managed by close family members of employees of municipality made false declarations	16% (32)	225	R249 million
Suppliers owned or managed by employees and councillors of municipality made false declarations	5% (9)	24	R4 million
Employees of municipality failed to declare family member's interest	17% (34)	169	R79 million
Employees of municipality failed to declare own interest either as part of procurement processes or through annual declarations	7% (13)	41	R5 million

Examples of how municipalities are dealing with awards made without necessary declarations of interest

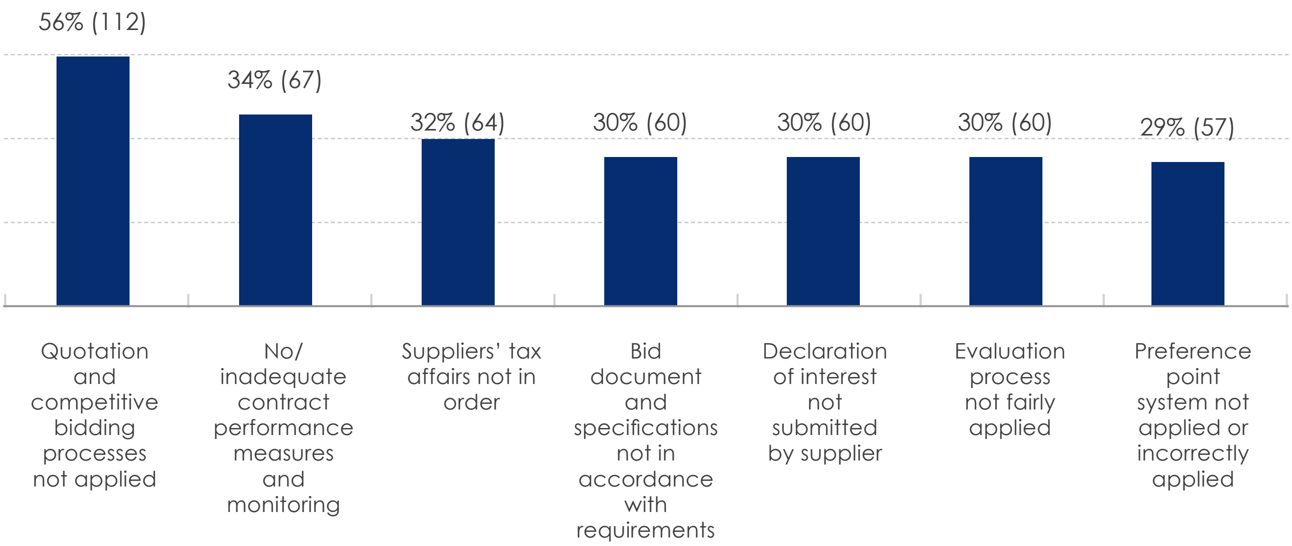
As there were weaknesses in the preventative controls of the **City of Ekurhuleni Metro**, the municipality depended on our computer-assisted audit techniques to identify conflicts of interest. Municipal employees flagged in this way subsequently resigned from being directors of companies doing business with the state. As the municipality did not have access to a database of companies for which family members of employees worked, it was not possible to identify conflicts of interest relating to family members.

Umhlatuze relied on the submission of declarations and supply chain database reports for all procurement to identify any interests and act in accordance with its policy. Where we flagged suppliers to management for investigation of false declarations through our computer-assisted audit techniques, management issued a letter to the supplier regarding the interest and gave them 30 days to respond; failing which, the municipality did not make awards to them in future.

Uncompetitive and unfair procurement processes and inadequate contract management

Uncompetitive and unfair procurement processes and inadequate contract management were still common. Often findings on non-compliance with supply chain management legislation are viewed and commented on as procedural issues or possible fraud. However, the potential for losses to government due to the correct processes not being followed is often overlooked. Less competition often leads to higher prices being paid for goods and services while non-compliance relating to contract management can open up the state to losses when contracts are not in place or performance is not monitored.

We reported findings (of which 70% was material) on uncompetitive and unfair procurement processes at 84% of municipalities, and contract management findings (of which 35% was material) at 44% of municipalities.



The aim of the Preferential Procurement Regulations is to support socio-economic transformation. The public sector should lead by example to achieve this goal, but we again found that some municipalities are failing in this area. At 57 municipalities (29%), the **preference point system was not applied or was incorrectly applied.**

The Preferential Procurement Regulations also requires municipalities to procure certain commodities from local producers. Municipalities failed in this regard as well, as 69 of the 136 municipalities (51%) where we audited local content **did not comply with the regulation on promotion of local producers** on awards amounting to R603 million.

In addition, 54 municipalities (27%) were awarded **contracts without properly constituted bid adjudication committees,** resulting in irregular expenditure of R3 310 million. At eight municipalities (4%), goods and services were procured through **contracts secured by other organs of state without complying with the prescribed requirements.**

Example illustrating effect of contract management shortcomings

Kagisano-Molopo did not have adequate controls in place to monitor the work done by contractors to ensure that it was in line with the contract. For example, the municipality contracted a supplier to construct a 1,8 km road to the value of R9,2 million in Tseoge Village. The contractor constructed only 1,63 km of the road but was paid for 1,8 km, resulting in the municipality overpaying the contractor.

PREVENTION OF IRREGULAR EXPENDITURE

Irregular expenditure is **expenditure that was not incurred in the manner prescribed by legislation.**

Such expenditure does not necessarily mean that money had been wasted or that fraud had been committed. It is an indicator of non-compliance in the process that needs to be investigated by management to determine whether it was an unintended error, negligence, or done with the intention to work against the requirements of legislation (which, for example, require that procurement should be fair, equitable, transparent, competitive and cost-effective).

Through such investigation, it is also determined who is responsible and what the impact of the non-compliance is. Based on the investigation, the next steps are determined. One of the steps can be condonement if the non-compliance had no impact and negligence was not proven. Alternatively, if negligence was proven, the steps can be disciplinary action, the recovery of any losses from the implicated officials, or even cancelling a contract or reporting it to the police or an investigating authority. This responsibility rests with the council, who should be supported by the municipal public accounts committee in this regard.

Irregular expenditure remained high at R26 billion and municipalities still did not deal with it speedily. Of the R19,31 billion in irregular expenditure incurred by municipalities of which the audits had been finalised by the cut-off date of this report, R14,5 billion was incurred in 2019-20 and represented 2% of the total expenditure budget.

*Annual irregular expenditure

R26 billion incurred by **246 municipalities** (consisting of R6,43 billion and R19,31 billion incurred by municipalities with outstanding audits and completed audits, respectively)

#But irregular expenditure is not complete

73 municipalities (37%) were qualified on completeness of their disclosure and/or did not know total amount and were still investigating to determine this

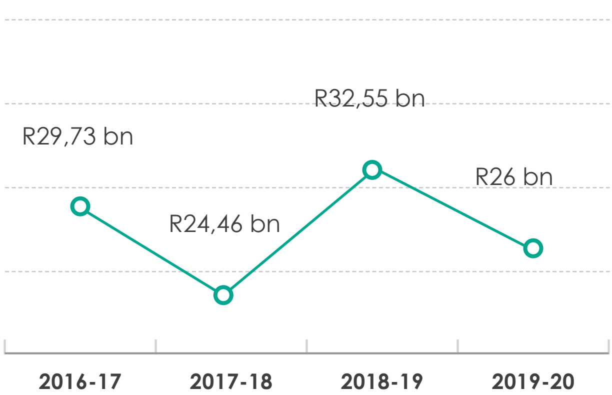
We could not audit procurement processes for selected contracts valued at **R1,43 billion**

#When did transgressions take place?

Current year = R8,73 billion (45%)
Prior year = R4,81 billion (25%) (only uncovered and disclosed now)
Multi-year contracts = R5,77 billion (30%)

**Includes 57 outstanding audits*
#Excludes 57 outstanding audits

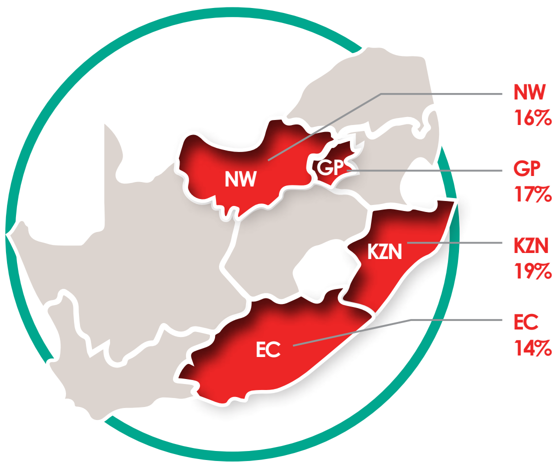
*Movement over 4 years



Non-compliance with supply chain management legislation remained the main cause of irregular expenditure, with R18,70 billion (97%) of the irregular expenditure incurred by municipalities of which we had completed the audits, relating to non-compliance with supply chain management legislation as follows:

- Non-compliance with other procurement process requirements (such as preference points not being applied or procurement from suppliers who had not submitted valid tax clearance certificates) – R10,78 billion (58%)
- Procurement without following a competitive bidding or quotation process – R4,77 billion (25%)
- Inadequate contract management – R3,15 billion (17%)

Highest contributors to irregular expenditure – R26 bn

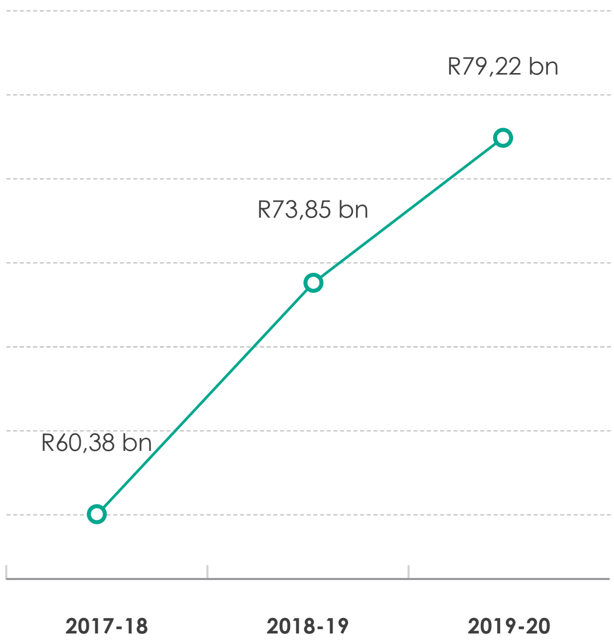


TOP CONTRIBUTORS TO IRREGULAR EXPENDITURE
City of Tshwane Metro (GP) – R2,53 billion
Mangaung Metro (FS) – R1,60 billion *
Nelson Mandela Bay Metro (EC) – R1,37 billion
eThekwini Metro (KZN) – R1,07 billion
City of Johannesburg Metro (GP) – R1,05 billion
Ngaka Modiri Molema District (NW) – R0,87 billion *
OR Tambo District (EC) – R0,70 billion
City of Cape Town Metro (WC) – R0,67 billion
Moses Kotane (NW) – R0,62 billion
Rustenburg (NW) – R0,57 billion *

** Audits still outstanding or finalised after cut-off date of report*

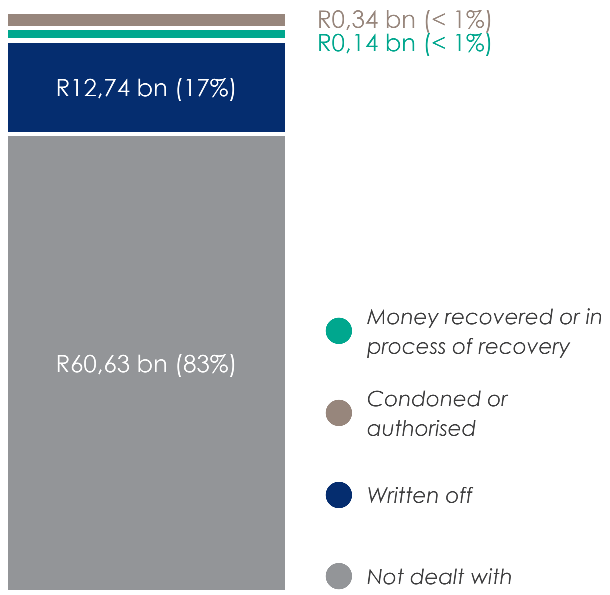
By looking at what municipalities have done with the 2018-19 irregular expenditure, it becomes clear that the pace at which this type of expenditure is being dealt with, remains very slow.

Closing balance of irregular expenditure continues to increase

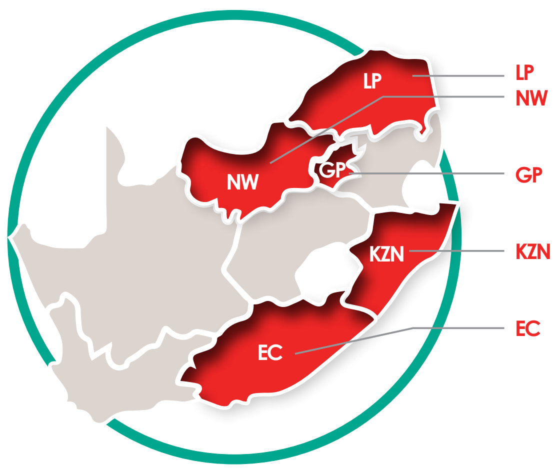


Yet municipalities are slow in dealing with it

(Figures are expressed as percentage of previous year's closing balance of R73,85 bn)



Top contributors to irregular expenditure – R37,93 bn



TOP CONTRIBUTORS (R37,93 BILLION) TO IRREGULAR EXPENDITURE NOT DEALT WITH – CONSTITUTES 63% OF R60,63 BILLION
Nelson Mandela Bay Metro (EC) – R16,54 billion
City of Tshwane Metro (GP) – R3,97 billion
City of Johannesburg Metro (GP) – R3,48 billion
eThekwini Metro (KZN) – R2,44 billion
uMkhanyakude District (KZN) – R2,33 billion
JB Marks (NW) – R2,17 billion
Buffalo City Metro (EC) – R2,08 billion
Mogalakwena (LP) – R1,86 billion
City of Ekurhuleni Metro (GP) – R1,71 billion
OR Tambo District (EC) – R1,35 billion

Examples illustrating challenges municipalities face in adequately investigating irregular expenditure

The **City of Tshwane Metro** had a backlog of investigations into allegations of possible fraud, corruption as well as unauthorised, irregular and fruitless and wasteful expenditure. This was due to internal capacity constraints and funding challenges caused by budget cuts that hindered the municipality from contracting external consultants to assist with investigations.

At **JB Marks**, the municipal public accounts committee was not adequately resourced to enable them to properly investigate irregular expenditure to determine if the municipality had suffered any losses and if any person was liable for such losses. As a result, the council mandated the audit committee to investigate the irregular expenditure, but this committee could also not implement the requirements prescribed by section 32 of the Municipal Finance Management Act, mainly due to a lack of adequate procurement documentation. In addition, the supply chain management unit was not adequately capacitated. The audit committee was terminated on 10 March 2020 and new members were only appointed on 28 September 2020, which further hampered the investigation of irregular expenditure. The council had also not been able to adopt the oversight report for the previous financial year, contributing to a lack of monitoring of recommendations made with regard to irregular expenditure.

EFFECTING CONSEQUENCES

It is of great concern that more than 60% of municipalities did not materially comply with legislation relating to effecting consequences.

Status of compliance with legislation on effecting consequences

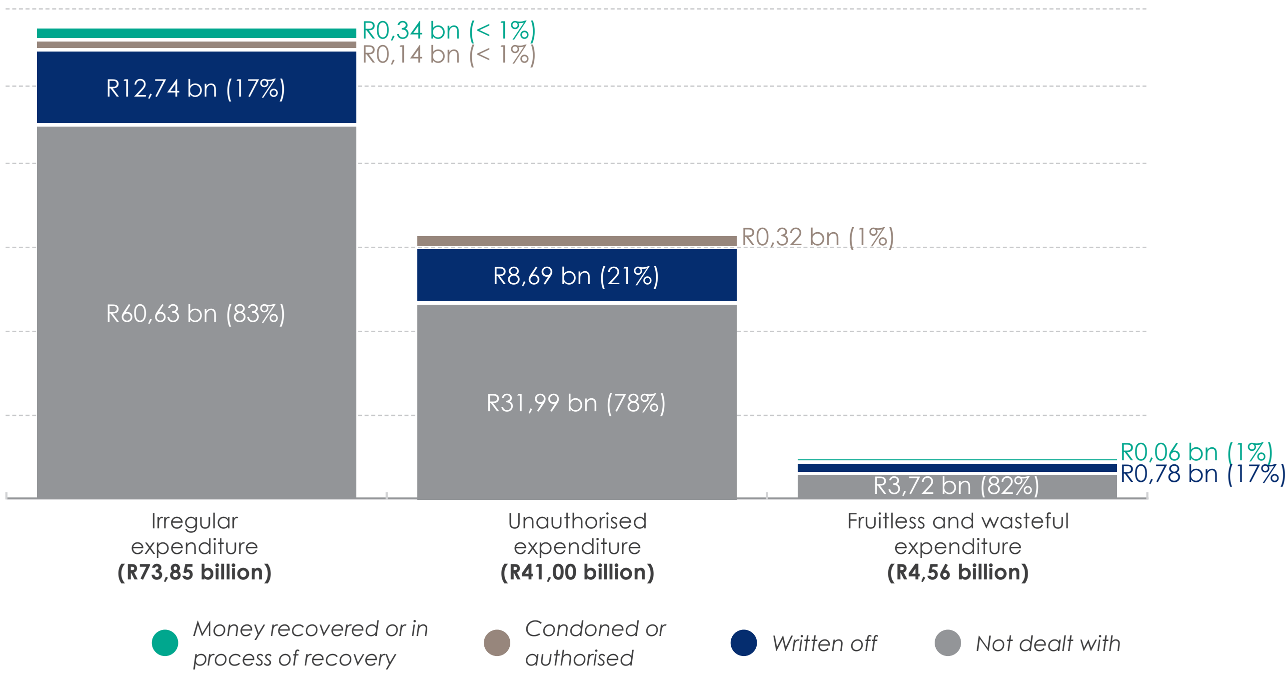
The most common findings involved the lack of investigation of unauthorised, irregular as well as fruitless and wasteful expenditure. This means that sufficient steps were not taken to recover, write off, approve or condone such expenditure. In total, 96 municipalities (48%) did not investigate the previous year's irregular expenditure, 88 (44%) did not do so for fruitless and wasteful expenditure, and 80 (40%) failed to investigate the previous year's unauthorised expenditure.

As a result, **the year-end balances of these types of unwanted expenditure continue to grow.** The year-end balance of irregular expenditure that had accumulated over many years (inclusive of outstanding audits) and had not been dealt with totalled R108,24 billion, while that of unauthorised expenditure stood at R71,76 billion, and the fruitless and wasteful expenditure added up to R9,28 billion.

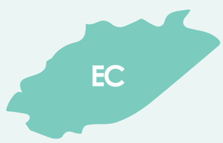
Investigations into these types of expenditure should be done in an objective and diligent manner. Councils should not write off or condone such expenditure without making sure that losses had not been suffered or that any such losses cannot be recovered.

How did the council deal with all prior year unauthorised, irregular and fruitless and wasteful expenditure to date?

Figures are expressed as percentage of previous year's closing balance



Example showing effect of municipalities' failure to investigate prior year irregular expenditure



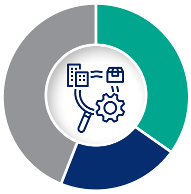
OR Tambo District did not effectively investigate all instances of irregular expenditure as required by legislation, which had accumulated to R1,98 billion at year-end. Furthermore, controls were lacking to prevent or detect errors in financial and performance information as well as non-compliance with legislation, resulting in the municipality's stagnation on a qualified audit opinion.

We further tested whether **allegations of financial and supply chain management misconduct and fraud** had been adequately followed up at 70 municipalities. We found the following:

- Investigations took longer than three months to complete at 25 municipalities (36%)
- Allegations were not investigated at 19 municipalities (27%)
- Allegations were not properly investigated at five municipalities (7%)

We also report indicators of possible fraud or improper conduct in the supply chain management processes, and recommend that management further investigate these matters. In 2018-19, we reported such indicators at 121 municipalities for follow-up. There is a definite need to increase the momentum in finalising these investigations.

Status of investigations into indicators of possible fraud or improper supply chain management conduct

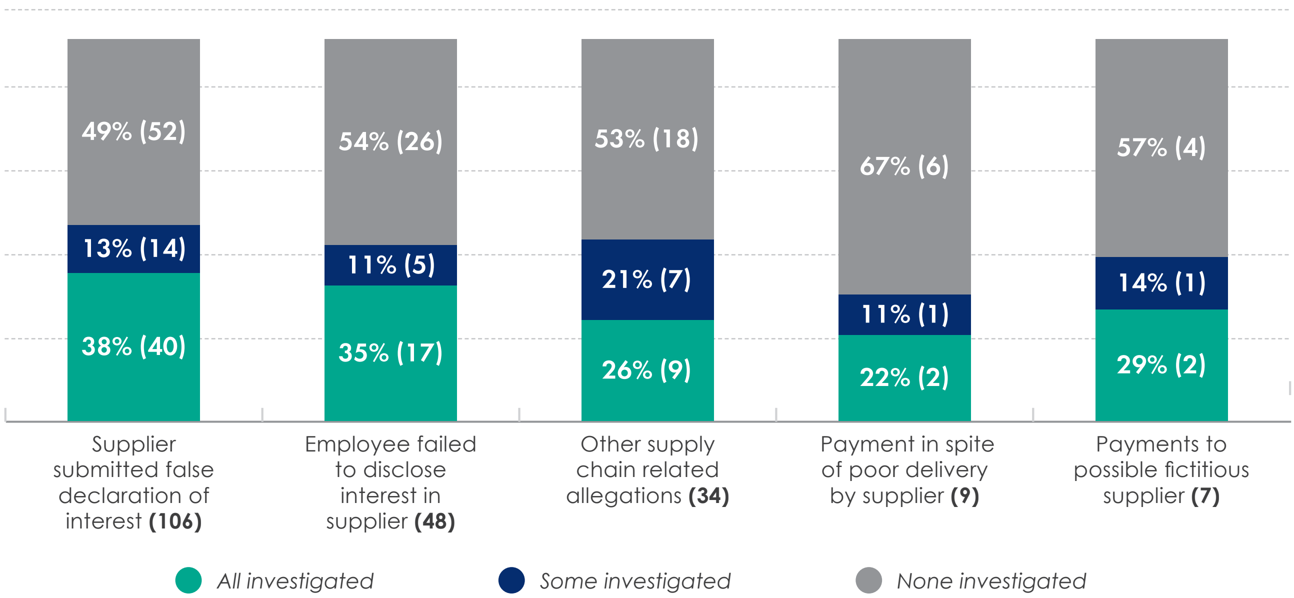


35% (42) municipalities investigated all the findings we reported

21% (26) municipalities investigated some of the findings we reported

44% (53) municipalities investigated none of the findings we reported

43 (63%) of the 68 municipalities that investigated all or some findings, satisfactorily resolved these investigations, but the remaining 37% did not (for example, the investigation recommended that contracts in which employees failed to declare their interest be cancelled, but the municipality did not do so)



POOR AUDIT OUTCOMES REMAIN THE NORM

The financial statements and the performance report of a municipality tell the story of how well a municipality is managed. It can be a good story of disciplined spending that achieves value for money and commitments to creditors being honoured.

However, the tale that is unfolding is of many municipalities being crippled by debt and being unable to pay for water and electricity; expenditure that is unauthorised, irregular, fruitless and wasteful; and a high dependence on grants and assistance from national government. Most concerning are those municipalities that cannot even prepare credible financial statements, even after paying millions to consultants for assistance and receiving sizeable support from national and provincial government.

The lapses in financial and performance management are apparent from the overall audit outcomes.

Although there was an overall improvement in the audit outcomes from the previous year, most municipalities are now in a worse position than at the beginning of the current administration, with 41 improving and 51 regressing over this period as at 23 April 2021. It is essential that focused and urgent attention is given to municipalities with a history of disclaimed audit opinions. We provide further detail on these struggling municipalities in section 4 of this report.

Audit outcomes

	Unqualified with no findings	Unqualified with findings	Qualified with findings	Adverse with findings	Disclaimed with findings	Outstanding audits
	11%	34%	26%	2%	5%	22%
2019-20 257	27	89	66	6	12	57
2018-19 257	20	94	93	6	39	5

First year of administration

	Unqualified with no findings	Unqualified with findings	Qualified with findings	Adverse with findings	Disclaimed with findings	Outstanding audits
2016-17 257	33	114	72	6	32	0

Movement from previous year

43 auditees (10% of budget) Improved

13 auditees (1% of budget) Regressed

Movement from 2016-17

41 auditees

51 auditees

Unqualified with no findings · Unqualified with findings · Qualified with findings · Adverse with findings · Disclaimed with findings · Outstanding audits

The provinces with the most regressions over the four-year period of the current administration are the Eastern Cape (12), Free State (seven), KwaZulu-Natal (15) and Northern Cape (five).

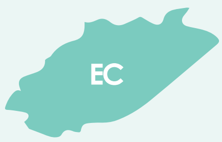
We urge the provincial leadership of these provinces in section 6 to reverse this negative trajectory as follows:

Eastern Cape	Improve and focus on controls for sustainable outcomes
Free State	Accountability can be realised through decisive leadership tone
KwaZulu-Natal	Upscale implementation of preventative controls and drive consistent consequences
Northern Cape	Sustainable change starts with the leadership will to drive it

On a positive note, some municipalities were able to maintain their clean audit status over the four-year period.

MUNICIPALITIES WHO SUSTAINED THEIR CLEAN AUDIT STATUS OVER FOUR YEARS	
Eastern Cape	Senqu
Gauteng	Midvaal
KwaZulu-Natal	Okhahlamba
Western Cape	Witzenberg, Cape Agulhas, Cape Winelands District and Overstrand

Below we share some of the best practices at these municipalities – struggling municipalities should emulate them in pursuit of improved audit outcomes.



Senqu established a structure within the municipality to segregate responsibilities to ensure that officials could be held responsible. The timeous filling of vacancies resulted in review processes being executed effectively and errors and concerns being identified and corrected early on. The municipality had a functioning internal audit unit that implemented standardised controls in the procurement processes and other areas were compliance plays a significant role, thereby preventing compliance findings. Even though the municipality did not draft interim financial statements, it concluded a clear preparation plan mid-year and followed the plan through up until the preparation of financial statements, ensuring that the correct processes were followed. The municipality had an experienced leadership team with both the municipal manager and chief financial officer having 15 years' experience in local government. The fully functional municipal public accounts committee probed municipal affairs and solicited relevant answers from management. The municipality also had an efficient disciplinary board, including members of the provincial treasury and legal services, which held officials to account for their actions and responsibilities.

Midvaal had institutionalised the daily disciplines of financial performance and compliance controls. These controls were embedded in the control environment and the effect of the covid-19 pandemic thus did not prevent the municipality from sustaining its clean audit outcome for the past seven years. The finance unit is adequately capacitated with competent staff who produce quality financial statements. There is good synergy between those responsible for service delivery on the ground and those responsible for monitoring the key performance indicators, resulting in performance information that is valid, accurate and complete. Compliance with laws and regulations is strictly enforced and monitored, which allows for early detection, correction and prevention of possible breaches of compliance. The internal audit function plays a vital role of ensuring that the design and implementation of key controls are working effectively and that key recommendations and action plans are appropriately implemented. Those charged with governance provide the necessary level of assurance and oversight and hold the administrative leadership accountable. The municipality is well supported by the provincial treasury and provincial cooperative governance department in the areas of finance and compliance. The municipality also leads the province by sharing best practices with other local municipalities in terms of the operation clean audit project. The political and the administrative leadership work well together and have a culture of high performance.

The institutionalisation and monitoring of key controls, commitment to accountability, and reliance on the contributions of an adequately resourced internal audit unit and audit committee – by the municipal manager and senior management – were key in **Okhahlamba** retaining its clean audit for the past six years. The municipal manager also fostered a strong control environment and tone that promoted clean administration. Furthermore, systems of internal control relating to record management, review and reporting processes as well as continuous monitoring of compliance with legislation and policies were embedded in the day-to-day activities by an adequately resourced finance team who understood what needed to be done. Additionally, quarterly financial statements were prepared and reviewed by the internal audit unit and audit committee.

Witzenberg is an example of a municipality with a strong leadership tone at the top and active involvement by the municipal manager in all areas of the municipality, including the audit process, which enabled a strong control environment and contributed to a culture of accountability. The municipality had its own well-capacitated internal audit unit – the importance of which was evidenced by management's responsiveness to the internal and external audit findings. The audit committee had the appropriate skills and the municipality ensured that committee members had the required experience in financial, legal and information technology areas as a minimum. The municipality also had an adequately functioning municipal public accounts committee and an effective council. Processes and procedures had been institutionalised to ensure clean administration. These included policies and procedures that were regularly updated, job descriptions that were well defined, and staff members who were aware of their individual roles and had good institutional knowledge of the municipality. Consequences were timeously effected as adequate disciplinary action was taken against transgressors.

The main reasons for the sustained clean audit outcome at **Cape Agulhas** for so many years, were that the municipality took all audit findings seriously and timeously put the necessary processes in place to resolve audit findings and address the internal control deficiencies that gave rise to the findings. The municipal manager and the chief financial officer were fully engaged and provided extensive support to the audit process, which motivated staff to do the same. The management team and staff have remained stable for a number of years, which ensured continuity and high-level institutional knowledge. This was also evident by the fact that the change in municipal manager during the 2019-20 financial year had no impact on the municipality's operations, activities and ability to maintain a clean administration. Management and staff did not consider the audit outcome as a threat, but as a 'management tool' to improve themselves.

Cape Winelands District sustained its clean audit outcome through the close monitoring of the control environment by management and those charged with governance to ensure the effective implementation of policies and procedures. This was further strengthened by the active involvement of those charged with governance throughout the audit process and the willingness of management together with leadership to address audit findings, which were monitored through management's action plans. Those charged with governance actively engaged management on the progress of the action plans on a quarterly basis in order to strengthen the control environment. As a result of the proactive attitude of senior management and those charged with governance, the municipality was able to avoid repeat findings within the control environment.

The continued clean audit outcome at **Overstrand** was made possible by the assurance provided by management and those charged with governance through the implementation of sound and effective policies and procedures. The necessary internal financial controls had also been institutionalised, which inherently created an environment of effective leadership over financial governance, performance and compliance with legislation. The use of governance structures assisted the municipality to adequately respond to key risk areas and proactively address identified deficiencies, which were effectively monitored through management's action plans.

The audit outcomes of seven provinces improved from the previous year, Gauteng's outcomes remained the same, and KwaZulu-Natal showed a slight improvement as at the cut-off date of this report. Section 6 of this report shows the overall audit outcomes per province and then deals with the outcomes of the individual provinces in more detail.

Overall movement from previous year in audit outcomes as well as per audit opinion

AUDIT OUTCOME	MOVEMENT			
	43 Improved	144 Unchanged	13 Regressed	57 Outstanding audits
Unqualified with no findings = 27	12	15		3
Unqualified with findings = 89	19	68	2	8
Qualified with findings = 66	1 10	48	7	22
Adverse with findings = 6	1	3	2	2
Disclaimed with findings = 12		10	1 1	22

Twelve municipalities improved their audit outcome to financially unqualified with no findings, bringing the total number of clean audits to 27 in 2019-20. Fifteen municipalities were able to retain their clean audit status from the previous year, but two municipalities could not do so.

We set the cut-off date for inclusion of the audit outcomes in this report as 23 April 2021. By this date, 57 audits were still outstanding, of which 32 were subsequently finalised. For five of the nine outstanding audits for which the financial statements were submitted late (two each in the Free State and North West, and one in the Northern Cape), the main reason for the late submission of financial statements is the backlog of audits as the 2018-19 financial statements were also submitted late.

We list the outcomes of the subsequently finalised 32 municipalities in section 6 of this report.

Status of audits not finalised by cut-off date of report

23 April 2021 — audits of **57** auditees outstanding

4 June 2021

→ **32** of these finalised

→ **25** not yet finalised

RESULTS OF 32 AUDITS SUBSEQUENTLY FINALISED

7 | 14 | 1 | 10

MAIN REASONS FOR DELAY

- Financial statements submitted late – 9
- Financial statements outstanding – 5
- Delays by auditee – 10
- Delays in audits – 1

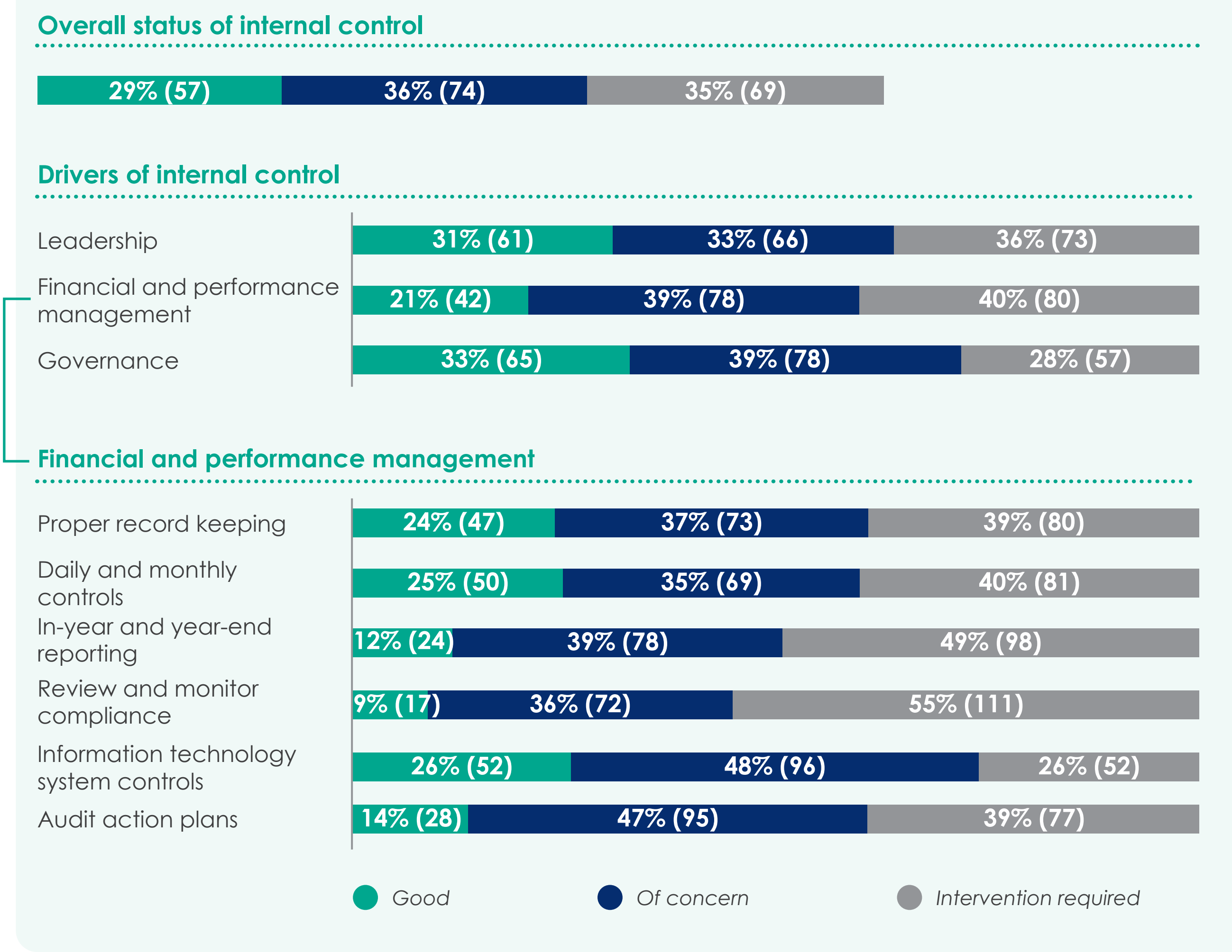
Unqualified with no findings · Unqualified with findings · Qualified with findings · Adverse with findings · Disclaimed with findings · Outstanding audits

STATE OF INTERNAL CONTROLS STILL NOT IMPROVING

Our message has been consistent throughout this administration and before: municipalities must have a strong control environment with practical, automated and routinely executed internal controls.

Internal controls support the achievement of municipal objectives by mitigating the risks of human error, incorrect decisions, fraud, abuse and loss. Such controls also prevent financial losses, wastage and transgressions, and significantly improve financial and performance management and reporting.

Investing in and progressively building a disciplined control culture is the sustainable solution that local government requires to do more with the limited funds at its disposal. However, the status of local government controls shows that this solution is not receiving the necessary attention.



Over the four years of the current administration, 34 municipalities improved their overall internal controls, but 37 are now in a worse state. The status of the financial and performance management controls answers the question of what is wrong at municipalities:

- Many still struggle with basic and routine daily transactional disciplines and monthly controls such as reconciliations. These disciplines and controls are also not supported consistently and effectively by information technology system controls, as elaborated on further below.
- We rarely find municipalities with good, built-in processes to monitor and review that all transactions, procurement, payments and decision-making comply with legislation, practices and policies.
- The lack of proper record keeping of financial and performance information is the key reason why we struggle to audit at some municipalities. It also weakens the potential for credible in-year reporting to enable municipal leaders to monitor performance and make well-informed decisions. At year-end, financial statements and performance reports are then consequently full of misstatements.
- Even our consistent call for audit action plans to address the root causes of audit findings is not getting the required attention, with plans being developed but then not executed.

Where sound systems of internal control are lacking, it could lead to a regression in audit outcomes. The provinces with the most unfavourable controls are also the provinces with the most regressions in audit outcomes over the four-year period.

Provinces with the most unfavourable controls

Example illustrating the effect of inadequate controls

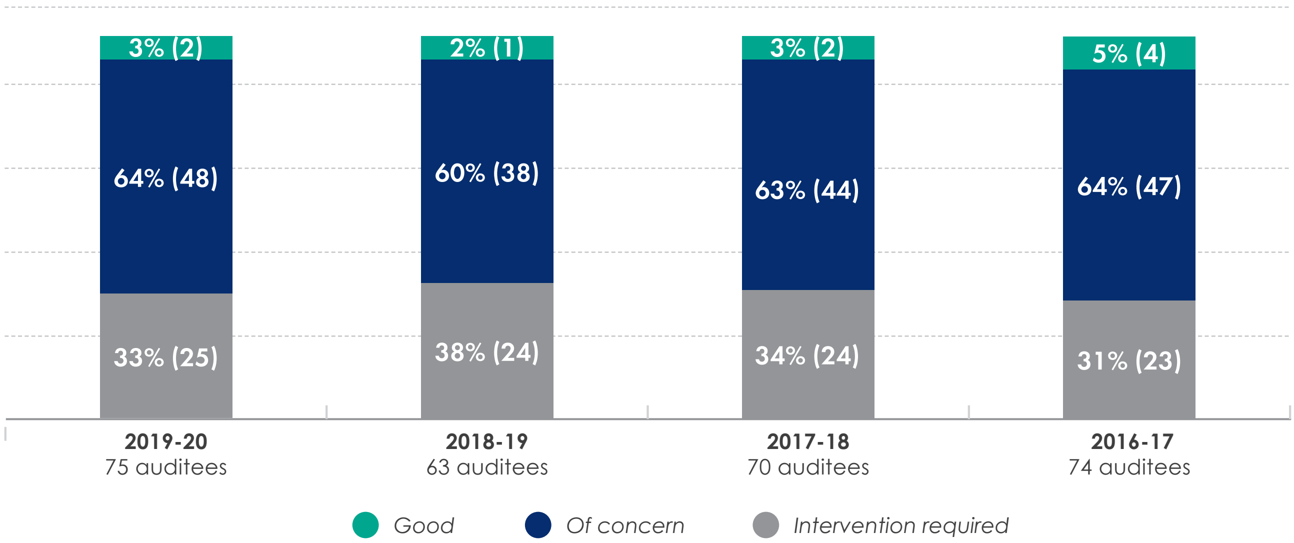
The lack of adequate controls is not only linked to non-adherence to legislation but some municipalities also struggled with controls around their expenditure. **Msukaligwa** could not fully account for its general expenditure and also recorded some of the general expenditure relating to the previous year in the current year. **Emakhazeni** did not have an adequate document management system and as a result could not provide us with evidence in relation to expenditure transactions. All of these accounting challenges are an indication that the building blocks of a good control system are not in place. There is a lack of skills to accurately apply the relevant accounting standards and there is no commitment to daily and monthly controls such as document management, proper independent review of work performed, reconciliations, asset verifications or periodic reporting in order to ensure credible financial reporting.

INFORMATION TECHNOLOGY CONTROLS

Information technology (commonly known as IT) refers to the information systems and automated controls municipalities use for recording, processing and reporting financial and non-financial transactions. Despite a slight improvement in the status of IT controls, the confidentiality, integrity and availability of municipal and metro information still cannot be ensured and effective service delivery is not enabled.

INFORMATION SYSTEMS AND AUTOMATED CONTROLS

Status of automated controls at 67 municipalities and 8 metros



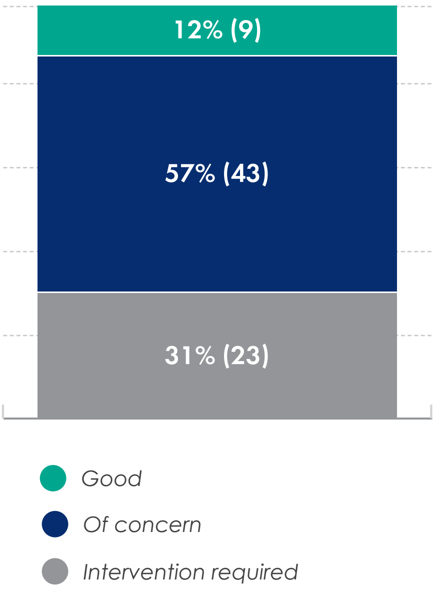
We assessed the IT controls supporting key financial systems, including supply chain, at 75 municipalities with more complex IT environments. The IT controls of 65 of these municipalities and eight metros had failed.

Although we had reported weak IT controls for the last four years, only 10 municipalities showed some improvement from the previous year. All metros remained stagnant. With little or no improvement in the general controls environment, minimum reliance can thus be placed on the application systems processing financial information. As a result, there is an increased risk that unauthorised transactions and changes can be processed on such application systems.

The eight metros operated modern enterprise resource planning systems such as SAP, Solar and JDEdwards. Although these systems had the functionality to be fully automated, it was not enabled, which increased the risk of data manipulation, fraud and errors.

IT GOVERNANCE

Status of IT governance at 67 municipalities and 8 metros – overall IT governance assessment



We assessed IT governance processes and controls at 75 municipalities (including eight metros). IT governance controls had failed at 59 of the municipalities and seven of the metros, demonstrating a lack of accountability in relation to the economical, efficient and effective use of IT resources. Governance processes were not effective in preventing and detecting the abuse or misuse of IT resources, resulting in the following:

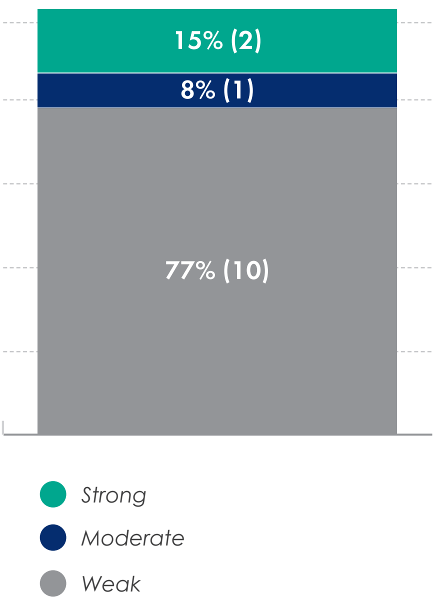
- Many of the municipalities did not derive value from their IT expenditure and, in some cases, this led to possible fruitless and wasteful expenditure.
- Management had not taken corrective action over a number of years, in spite of an increase in expenditure on IT programmes. Overall, 88% of municipalities and metros had weak IT governance practices compared to 86% in the previous year.

We identified weaknesses in the following key areas of IT governance:

- 31 municipalities (41%) and three metros (4%) had IT strategic plans that were inadequate and/or they did not manage funds and resources effectively; 59% were repeat findings.
- 24 municipalities (32%) and four metros (5%) had IT steering committees that were not operating effectively and as a result action plans were not monitored and implemented; 67% were repeat findings.
- Only 17 (23%) of the 75 municipalities (which included four metros) performed IT audits through their internal audit function.

CYBERSECURITY VULNERABILITIES AND THREATS

Status of cybersecurity posture at 5 municipalities and 8 metros – IT security controls



We performed IT security reviews at 13 large municipalities (including the eight metros) and found that 85% of them failed their IT security controls. As a result, data processed by their systems and the integrity of their information have a high risk of being compromised.

It is of concern that the status of 77% of these municipalities had stagnated or regressed compared to the previous year.

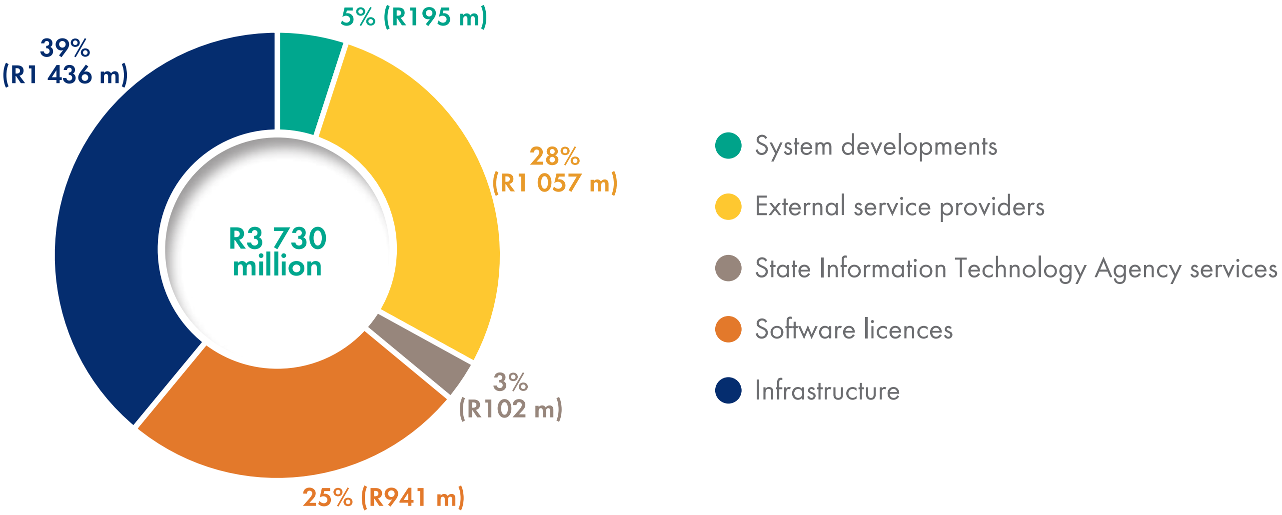
A lack of improvement in the area of IT security management at two metros led to cybersecurity breaches of their networks during the period of review, which resulted in the disruption of services.

The main contributing factors leading to failed IT security controls were the following:

- Long-standing shortage of IT security skills.
- Ageing/legacy IT infrastructure and lack of adequate investment in cyberdefence mechanisms.
- Lack of network monitoring controls to detect issues in time.

IT EXPENDITURE

Status of IT expenditure at 67 municipalities and 8 metros



Countrywide, 75 municipalities (with a total IT spend of R3 730 million), including the eight metros where R2 754 million was spent on IT, had more complex environments that were highly dependent on information systems to process financial transactions and support core business operations.

We tested software licences at these 75 municipalities and found that the City of Johannesburg Metro paid R95 million and the City of Ekurhuleni Metro paid R3 million for licences. However, licences worth R75 million at Johannesburg and R3 million at Ekurhuleni, were not used.

We selected six projects valued at R1 053 million for auditing at two municipalities and four metros, and identified the following concerns:

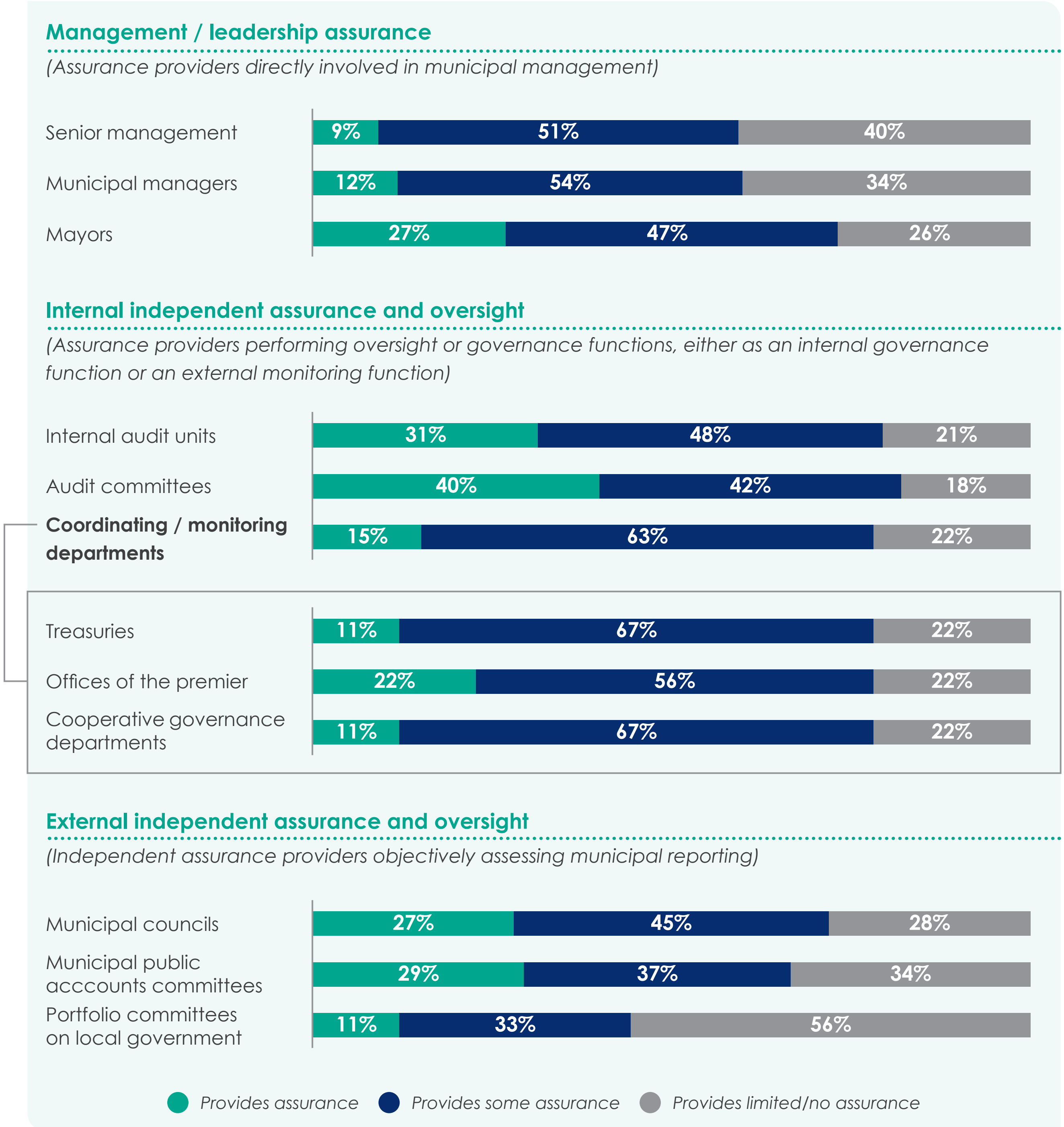
- R600 million was spent by the City of Johannesburg Metro on a SAP upgrade. The project scope and budget were not well managed, which led to this project absorbing more money than the value it created.
- R1 906 million was spent by the City of Ekurhuleni Metro on a Solar upgrade. As a consequence of not having well-defined criteria for deliverables, the metro spent R1 906 million from an original budget of R842 million.

Although a lot of money is spent on IT, the necessary controls surrounding IT investment and IT governance are not always implemented to ensure the effective and efficient functioning of IT systems in local government.

ALL ROLE PLAYERS MUST FULFIL THEIR ASSURANCE RESPONSIBILITIES

Our reporting and the oversight processes reflect on history, as they take place after the financial year. Many other role players contribute throughout the year to the credibility of financial and performance information and compliance with legislation by ensuring that adequate internal controls are implemented.

We assess the level of assurance provided by role players in local government based on the status of municipalities' internal controls and the impact of the different role players on these controls. In the current environment, which is characterised by inadequate internal controls, corrected and uncorrected material misstatements in financial and performance information, and widespread non-compliance with legislation, all role players must fulfil their assurance responsibilities. As shown below, however, this is unfortunately not the case.



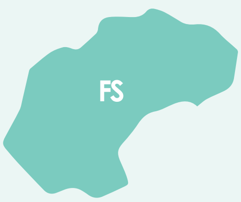
A key element of internal control is monitoring by the different assurance providers to ensure that internal controls are adhered to, risks are managed, and outcomes are achieved. Low levels of assurance show that there is a breakdown in a crucial element of the accountability chain. The provinces below fared the poorest in this regard.

Management/leadership assurance

Internal independent assurance and oversight

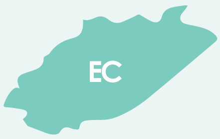
External independent assurance and oversight

Where the required level of assurance is not provided, it could negatively affect the audit outcome of a municipality, as illustrated below.



At **Fezile Dabi,** management did not implement controls to ensure the timeous capturing and maintenance of employees' leave transactions or the maintenance of commitment and asset registers. Although there were employees to do this work, consultants performed these functions at year-end as part of the financial statement preparation processes. The internal audit unit also did not help with the implementation of internal controls, as they did not monitor the implementation of the municipality's action plan. In fact, they defended management and their wrongdoing when we raised findings.

The following example illustrates the opposite: where the required level of assurance and assistance is provided by role players, the situation at municipalities can be turned around.



Elundini improved to an unqualified opinion with no findings from the previous year's unqualified opinion with findings. This was due to the municipal manager and senior management effectively implementing and monitoring action plans. They also demonstrated a strong commitment towards a clean administration and effected consequences for prior year transgressions. This resulted in the municipality instituting processes to recover some of the irregular as well as fruitless and wasteful expenditure previously incurred. The audit committee, through the internal audit function, provided independent assurance of municipal controls. The municipality ensured that key positions were filled with competent personnel, with stability in the finance unit positively contributing to the improved audit outcome.

ROOT CAUSES OF POOR STATE OF LOCAL GOVERNMENT

Below we look at two of the root causes of the poor state of local government, namely a **slow response** to our call to municipal leadership to strengthen internal controls, as well as **vacancies and instability** that slow down – or even reverse – any gains. We have already discussed a third root cause, namely the continuing culture of a **lack of consequences**, under *Widespread non-compliance with legislation* earlier on.

A SLOW RESPONSE TO OUR MESSAGES ON OVERALL INTERNAL CONTROLS

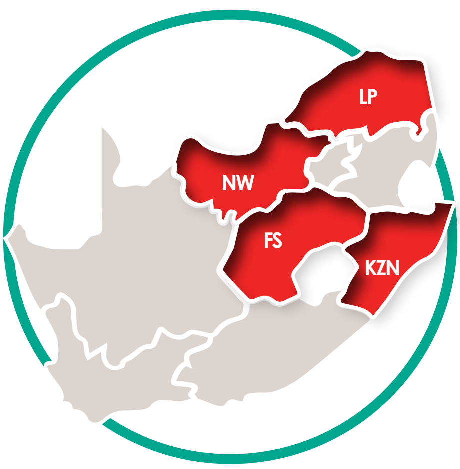
The most common reason for municipalities not achieving clean audits is that they are slow in responding to our recommendations, or do not even respond to our recommendations at all.

2019-20 91% (157)

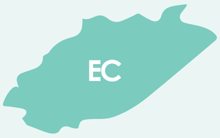
2018-19 90% (183)

	Slow response	No response
Slow response by managment	123	29
Slow response by political leadership	40	14
Slow response by oversight	18	9

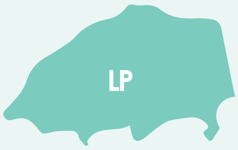
Provinces where no response is most common



The following examples illustrate how weak internal controls compromised the internal control environment, resulting in poor audit outcomes.

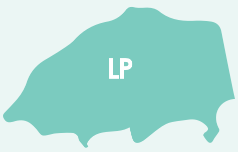


Nelson Mandela Bay Metro stagnated on a qualified opinion due to the slow response by management to address all prior year findings, combined with leadership instability. The senior management vacancy rate was high at 38% and the municipality continued to operate without a municipal manager for the third successive year. A chief financial officer was appointed late in the year, with the result that not all prior year findings could be resolved in time. The vacancies compromised the internal control environment over a prolonged period and resulted in a lack of effective consequences. The municipality continued to operate without fully integrated information technology systems, which put further pressure on its control environment.



Mogalakwena had an extremely weak internal control environment when it came to all three drivers of internal control, namely leadership, financial and performance management, and governance. This was evident in poor service delivery due to the mismanagement of resources and the poor state of records, for which municipal officials were not held accountable. The municipality failed to resolve prior year audit findings, resulting in many repeat findings in 2019-20. The municipality even lacked the basic controls of ensuring that the financial statements were supported by accurate and underlying records, due to the poor record-keeping controls.

On the flipside, good controls result in favourable audit outcomes, as illustrated below.



Municipalities such as **Capricorn District, Greater Giyani, Molemole and Thulamela** had good internal controls in place. These municipalities had improved their controls over record keeping, processing and/or reconciling and reporting. All these municipalities received unqualified audit opinions, with Capricorn District in the spotlight for maintaining its clean audit opinion. The good control environment enabled Greater Giyani to improve its audit opinion from qualified in 2018-19 to unqualified in 2019-20. These municipalities had put in place controls around financial, performance and compliance areas to enable strong reporting systems that produced credible information. The attitude of their management and oversight structures towards creating an environment characterised by good internal controls further contributed to the good audit outcomes in the current financial year.

VACANCIES AND INSTABILITY CONTRIBUTE TO POOR AUDIT OUTCOMES

Vacancies and instability in key positions significantly contributed to municipalities achieving poor audit outcomes. For example, at 63 municipalities (36%), instability and vacancies in key positions was a root cause that hindered them from improving and sustaining their audit opinion. In contrast, stability in key positions such as those of municipal manager and chief financial officer has enabled municipalities to obtain better audit outcomes.

Overall, the average vacancy rate at municipalities was 21%, while that of both senior management and finance units was 18%. We assessed the resourcing of 92 finance units (46%) as either concerning or requiring intervention. In addition, there was instability at council level at 13 municipalities (7%).

Vacancies and stability in key positions

POSITIONS	VACANCIES			AVERAGE NUMBER OF MONTHS IN POSITION
	Vacant for less than 6 months	Vacant for 6 months or more	Total vacancies	
Municipal manager	5% (9)	9% (17)	13% (26)	42 months
Chief financial officer	3% (6)	13% (26)	16% (32)	42 months

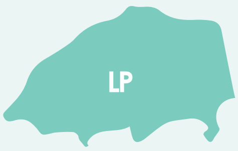
Stability* in key positions produces better audit outcomes

*AVERAGE MONTHS IN POSITION	CLEAN AUDIT	UNQUALIFIED WITH FINDINGS	QUALIFIED WITH FINDINGS	ADVERSE/ DISCLAIMED WITH FINDINGS
Municipal manager	71	36	41	22
Chief financial officer	60	45	37	21

Provinces where instability or vacancies in key positions are most prominent

The following examples show how vacancies and instability contribute to municipalities struggling to improve their audit outcomes – or even regressing.

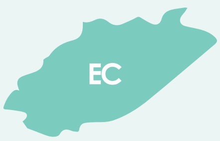
Instability in the chief financial officer position had a negative impact on **Rand West City**'s audit outcome. The municipality had three different chief financial officers from the start of the financial year up to the date of the audit report, which contributed to the regression from an unqualified audit opinion with findings to a qualified audit opinion.



Mogalakwena again received an adverse opinion. The chief financial officer position was vacant throughout the financial year. Although the municipality appointed consultants to prepare financial statements, they were not effective as evidenced by underlying records that substantially differed from what was disclosed in the financial statements. The instability at council level compromised the effectiveness of the council's oversight of municipal matters. This resulted in the audit opinion not improving.

Moretele again received a qualified audit opinion with findings. The chief financial officer and municipal manager positions were vacant throughout the year and neither an audit committee nor an internal audit unit had been established. This compromised the preparation and review of the financial statements and resulted in the audit opinion not improving. Although the municipality appointed consultants to prepare financial statements, they were not effective as evidenced by underlying records that could not be made available for auditing.

Conversely, stability in key positions enables municipalities to obtain better audit outcomes.



Mnquma received an unqualified opinion with findings, consistently improving over the years from a disclaimed opinion in 2016-17, an adverse opinion in 2017-18, and a qualified opinion in 2018-19. The municipality ensured that vacancies were filled and that the finance unit was adequately capacitated with competent staff. The municipal manager and senior managers took ownership of the financial and performance management of the municipality by taking appropriate action to respond to prior year recommendations. This led to an improvement in record keeping and the strengthening of daily and monthly reconciliation and processing controls.

Gauteng remains a destination of choice for professionals seeking employment in the country, with municipalities that have both attracted and retained staff with the right skills benefiting from this continuity. This has had a positive impact on financial management and – in turn – audit outcomes. One such example is the **City of Ekurhuleni Metro**. The municipality is adequately capacitated with experienced staff who have the right skills, contributing to improved financial and performance reporting and compliance over recent years.

SHORT-TERM SOLUTIONS ARE NOT HAVING THE DESIRED IMPACT

Local government cannot be turned around through short-term solutions. A case in point is the **continued use of financial reporting consultants** as discussed earlier – what was meant to temporarily bridge the skills gap, has now become a permanent and expensive solution.

At some municipalities, there has been a total collapse of internal control, severe financial health problems, and a complete lack of accountability. Where municipalities have become so dysfunctional, some provinces stepped in to place those **municipalities under administration** in an effort to restore good governance and sound financial management. This essentially means that the administrator manages and oversees the day-to-day running of the municipality.

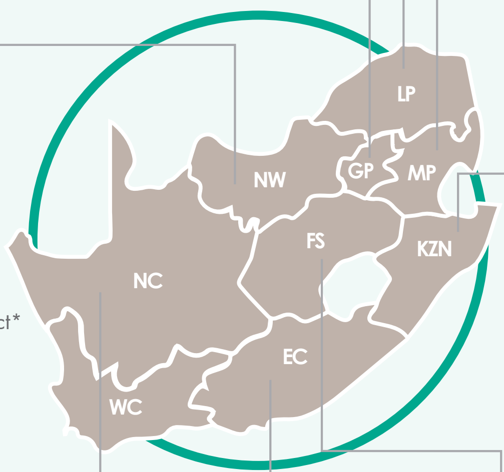
Below we show which municipalities are under administration – some of which for as long as four years.

GAUTENG
- City of Tshwane Metro*
- Emfuleni$
- West Rand District$

LIMPOPO
- Mogalakwenai*

MPUMALANGA
- Dr JS Moroka*
- eMalahleni*
- Govan Mbeki×
- Msukaligwa*
- Thaba Chweu*

NORTH WEST
- Bojanala District*
- Ditsobotla$
- JB Marks*
- Lekwa Teemane*
- Madibeng$
- Mahikeng*
- Maquassi Hills*
- Naledi*
- Ngaka Modiri Molema District*
- Ratlou$
- Tswaing*



KWAZULU-NATAL
- Abaqulusi$
- eMmadlangeni*
- Inkosi Langalibalele¥
- Mpofana¥
- Msunduzi$
- Mtubatuba×
- Richmond*
- Umkhanyakude District×
- Umzinyathi District§
- uThukela District$

NORTHERN CAPE
- Phokwane¥
- Renosterberg*

EASTERN CAPE
- Enoch Mgijima$
- Makana*

FREE STATE
- Mafube§
- Maluti-A-Phofung¥
- Mangaung Metro*
- Metsimaholo*

** Under administration for 1 year*
$ Under administration for 2 years
¥ Under administration for 3 years
§ Under administration for 4 years
× Under administration after 2019-20 financial year

Unqualified with findings | Qualified with findings | Adverse with findings | Disclaimed with findings | Outstanding audits

Unfortunately, there is little evidence yet that these supposedly short-term solutions are leading to wholesale improvements in the status of these municipalities.

As the following example illustrates, however, this need not be the case as the unfavourable situation can be turned around with the necessary assistance of various role players.

Although **Msunduzi** received a qualified audit opinion, the number of qualification areas decreased to only one, namely expenditure. The improvement is partly attributable to the assistance received from the provincial cooperative governance department and the National Treasury in the period of administration over the past two years. The National Treasury also made resources available in an effort to improve the audit outcome of the municipality.

Additional examples of municipalities under administration are included in section 4 of this report as part of our discussion on disclaimed municipalities.

MOVING TOWARDS AN IMPROVED LOCAL GOVERNMENT

Finding and implementing sustainable solutions for the crisis in the municipal landscape should be a common goal for all in local government. The relevant role players should work together to strengthen the capacity, processes and controls of municipalities, which will enable credible financial and performance reporting, compliance with key legislation, sound financial management, and improved service delivery.

We are committed to continue playing our part in improving local government audit outcomes.

OUR ROLE – AUDITING AND REPORTING FOR ACCOUNTABILITY

Our primary responsibility is to audit and report to the council and its committees on the credibility of the financial statements and performance reports and on whether the municipality complied with key legislation. It is the role of these oversight structures to use our audit report to determine whether they can rely on the financial statements and performance reports for oversight and decision-making purposes and to call the administration to account for matters we report in the audit report.

But as public sector auditors with a keen interest in seeing local government succeed, we have always done **more than just report.**

Through our management, audit and general reports, we **report the weaknesses in internal control and the risks that need attention**.

In our reports, we **provide root causes** for audit findings and **recommendations** to address these root causes. As part of our expanded mandate, we also report on **material irregularities** (section 5 of this report details our work in this regard).

In addition, we began a **real-time audit** in May 2020 of the key covid-19 initiatives introduced by government and of the management of the relief funding made available to respond to the pandemic.

We ensure that our messages are heard through **impactful engagements** with senior officials, municipal managers, mayors, municipal public accounts committees, and councils. Our engagements have been extended over the past two years to also include a **status-of-records review** that comprises an assessment of records, risks and progress made by the municipality to address prior year issues early in the financial year. This provides an early warning system whereby municipal managers can be alerted to matters that can potentially lead to undesirable audit outcomes.

We further aim to capacitate municipal leadership and oversight through our reports and engagements. We have provided **preventative control guidance and awareness** on good financial and performance management practices and also participate in specific **capacitation initiatives** such as induction sessions for councillors.

All of these measures are aimed at assisting the municipal leadership and the council to prevent accountability failures. However, in most cases there is a failure to act on our warning signals and as a result we continue to find the vast majority of municipalities in need of intensive care.

THE ROLE OF LEADERSHIP – STEERING MUNICIPALITIES TO SUCCESS

The **leadership sets the tone** at the top of any municipality. If a municipality's leaders are unethical; have a disregard for governance, compliance and control; and are not committed to transparency and accountability, it will filter through to the lower levels of the municipality. Inevitably, a culture of poor discipline, impunity and non-delivery will develop.

The leaders in local government should therefore take responsibility for the deteriorating accountability in municipalities – it is their duty to turn the situation around. **Ethical and accountable leadership should drive the desired change.**

Local government leadership includes the municipal manager and his/her senior managers who are responsible for the administration and service delivery of the municipality; the political leadership (mayor and council members) that oversees the functioning of the municipality and takes key decisions; and the provincial leadership (premier, members of the executive council, and heads of provincial departments that support local government). The provincial legislature also has a role to play as part of its oversight function.

Below we set out the responsibilities that leadership should pay attention to.

Municipal leadership

Municipal managers and their senior managers need to focus on the financial and performance management of the municipality.

Senior managers should significantly improve the processes and controls to ensure that municipal objectives are achieved through good planning, people management, project management, monitoring, and effecting consequences. They should also prioritise basic control disciplines to prevent, detect and correct errors, transgressions, non-compliance and poor performance.

Municipal managers should create an environment in which accountability, high performance and ethical behaviour can flourish. They can do so by setting an example and ensuring that enough competent and committed people are employed and perform their work within a set of rules defined in policies and procedures.

Political leadership

The political leadership in the local government sphere has a direct relationship with, and impact on, the municipal administration. This model provides for a more participative government whereby community members can oversee and direct their municipality through their elected council members.

Unfortunately, political infighting at council level at some municipalities directly affected the administration of these municipalities, with councils delaying decision-making and neglecting their oversight duties in pursuit of a political agenda. We also observed political inference in the administration of some municipalities.

The focus of mayors and council members should be on capacitating, stabilising, supporting and overseeing municipal administration to the benefit of the community that elected them. But – in turn – they then need to be respected and empowered with information that allows them to effectively monitor and oversee the activities of the municipality. This is why they must insist on credible financial and performance information – not just in the annual report, but throughout the year to determine if the municipality is achieving its objectives within the budget and within the requirements of legislation. The mayor, council and municipal public accounts committee are entitled in terms of legislation to report on matters such as supply chain management deviations, non-compliance, financial misconduct, losses and shortfalls throughout the year.

As representatives of the people that elected them, the mayor and council members should consistently display ethical and courageous leadership and champion transparency and accountability.

Provincial leadership

The need for provincial leadership to pay close attention to municipalities in the manner required by legislation is becoming crucial – often action is only taken after a municipality has deteriorated to a point of collapse.

The levels of provincial leadership support to municipalities differed across the provinces. The most successful provinces (in terms of audit outcomes) have in common a premier that provides leadership and direction on local government matters in a consistent manner and follows through on commitments in this regard. We also see strong provincial treasuries and cooperative governance departments working together to support and guide municipalities.

In turn, municipalities need to respond to the provincial and national support and interventions in a positive and timeous manner.

The leadership at all three levels should focus on the following key matters:

- Tone at the top – ethical leadership, service-orientation, good governance and accountability
- Capacitate and stabilise administration – free from political interference/changes
- Enable and insist on strong control environment with practical, automated and routinely executed internal controls that prevent financial loss, wastage and transgressions; and significantly improve financial and performance management and reporting
- Consistent, appropriate and swift consequences for accountability failures

Only a capable, efficient, ethical and development-oriented state can deliver on the commitment to improve the lives of the people of this country.

- President Cyril Ramaphosa

MUNICIPALITIES WITH A HISTORY OF DISCLAIMED AUDIT OPINIONS

04

MUNICIPALITIES WITH A HISTORY OF DISCLAIMED AUDIT OPINIONS

04

In this section, we highlight some of the worst-performing municipalities in local government and flag the urgent need for intervention.

Over the years, we have called on the provincial leadership and oversight to direct their efforts towards municipalities that continue to receive disclaimed opinions. However, the inability of some municipalities to reverse the trend of negative audit outcomes points to a culture that is not responsive in dealing with control weaknesses flagged in prior years.

A disclaimed opinion means that a municipality could not provide us with evidence for most amounts and disclosures in their financial statements and we therefore could not express an opinion on the credibility of these financial statements. Municipalities with disclaimed opinions are also typically unable to provide supporting documentation for the achievements they report in their performance reports and do not comply with key legislation.

In 2019-20, 22 municipalities received disclaimed opinions. This includes 12 municipalities of which we had completed the audits by 23 April 2021 (the cut-off date of this report), and another 10 municipalities of which the audits were subsequently finalised up to 4 June 2021. Four municipalities (Tokologo, Maluti-A-Phofung and Masilonyana in the Free State as well as Renosterberg in the Northern Cape) that received disclaimed opinions in the past have not yet submitted their financial statements. This means that the number of disclaimed municipalities for 2019-20 could still increase.

The map below lists the 22 disclaimed municipalities as well as the four previously disclaimed municipalities that have not yet submitted their financial statements for 2019-20.

NORTH WEST

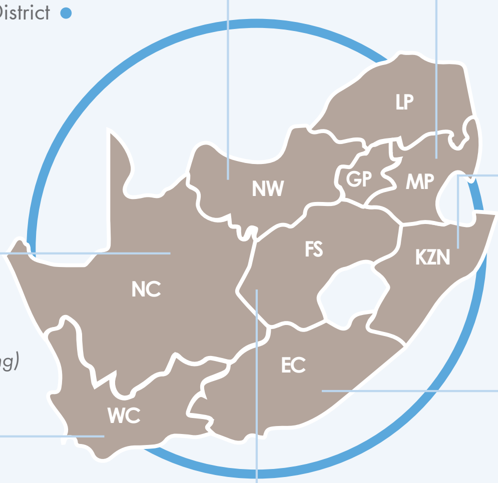
- Dr Ruth Segomotsi Mompati District ●
- Lekwa Teemane * ●
- Mamusa ●
- Madibeng $ ●
- Maquassi Hills * ●
- Ratlou $
- Ramotshere Moiloa ●

NORTHERN CAPE

- !Kheis ●
- Kai !Garib ●
- Renosterberg * *(audit outstanding)*

WESTERN CAPE

- Beaufort West



MPUMALANGA

- Dipaleseng ●
- Dr Pixley Ka Isaka Seme
- Govan Mbeki ˣ ●
- Lekwa ●

KWAZULU-NATAL

- Amajuba District
- Inkosi Langalibalele ¥
- Nquthu
- uMzinyathi District § ●

EASTERN CAPE

- Chris Hani District
- Ingquza Hill ●
- Makana * ●
- Sundays River Valley ●

FREE STATE

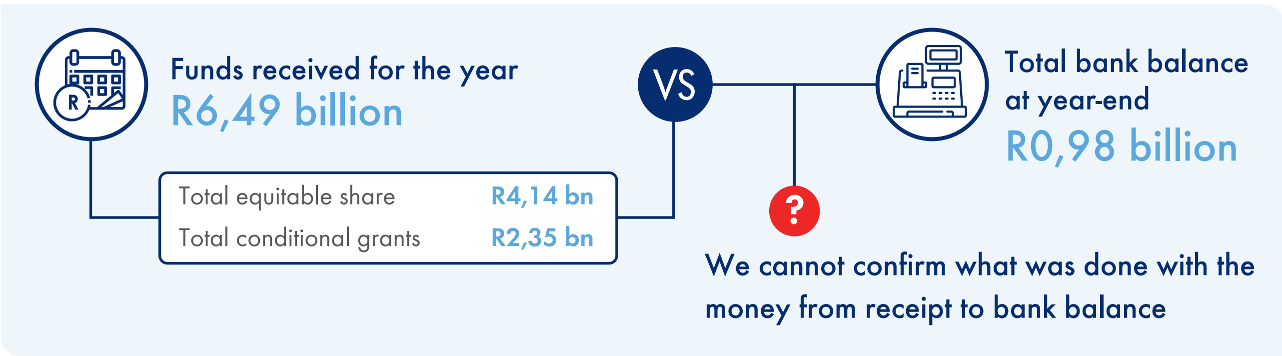
- Tokologo *(audit outstanding)* ●
- Maluti-A-Phofung ¥ *(audit outstanding)* ●
- Masilonyana *(audit outstanding)* ●

* *Under administration for 1 year*
$ *Under administration for 2 years*
¥ *Under administration for 3 years*
§ *Under administration for 4 years*
ˣ *Under administration after 2019-20 year-end*
● *Notification of material irregularity issued by 11 June 2021*

At least five of the disclaimed municipalities have been under administration for two years or more, yet we see a prolonged state of poor performance and therefore remain concerned about the effectiveness of the administration process. A further concern is that just over 77% of the disclaimed municipalities have shown a regression in their audit outcomes since 2016-17.

The high number of municipalities that received disclaimed opinions compelled us to consider the impact of full and proper records not being kept and the lack of credible financial reporting. We concluded that these lapses in accountability caused substantial harm to the majority of these municipalities, as their financial position was so poor that they disclosed in their financial statements a material uncertainty as to whether they can continue operations. Some of the municipalities were not able to deliver services as required and the Department of Cooperative Governance determined them to be dysfunctional. In addition to the municipalities already highlighted, notifications on material irregularities were issued to three municipalities (Mafube in the Free State, and Ditsobotla and Kgetlengrivier in North West) where the audits were still outstanding at the date of this report. Further details on the notification of material irregularities identified are included in section 5 of this report.

The municipalities received funding during the year in the form of an equitable share of revenue raised nationally and grants to enable them to operate and deliver essential services to the communities they serve. However, we cannot confirm what was done with the money from receipt to what was left in the bank at year-end. We show these figures for the 22 municipalities where the audits had been completed below.



At most of these municipalities, we see instability at both political and administrative leadership level, weak oversight by councils, poor financial health, protests and strikes that disrupt and result in poor performance, a lack of consequences as well as interventions not being effective, all of which contribute to the poor audit outcomes.

In the rest of this section, we share some examples of the worst performing of these municipalities across four provinces, namely the Free State, Mpumalanga, Northern Cape and North West.

We provide insights on the following:

- Location of municipalities and communities they serve
- Municipalities' audit outcome history, insights on why they are disclaimed as well as interventions undertaken and why these are not bearing fruit
- Impact of poor financial and performance reporting and management on service delivery
- What must be done to turn around the poor audit outcomes of these municipalities

MALUTI-A-PHOFUNG

Funds received for the year

Total equitable share	R600 m
Total conditional grants	R278 m

VS

Total bank balance at year-end

R42 m

Audit outcomes

2019-20	Outstanding audit
2018-19	Outstanding audit
2017-18	Disclaimed
2016-17	Disclaimed

Previously under administration

FEBRUARY 2018 TO JULY 2020 (27 MONTHS)

Use of financial reporting consultants

(2016-17)

R20 m

Total salary cost of finance unit

Audit outstanding

Maluti-a-Phofung is located in Phuthaditjhaba in the Thabo Mofutsanyana district and has a population of 353 452 people. The municipality, which borders the picturesque Golden Gate National Park, was named after the Drakensberg mountains (known as 'Maluti' in Sesotho) and the Sentinel peak in Qwaqwa (known as 'Phofung' in Sesotho).

The municipality received a disclaimed opinion in 14 of the last 15 years. It was only able to avoid a disclaimed opinion in 2015-16 by delaying the submission of its financial statements to address prior year audit matters and appointing two consultants for the whole year. However, the next year it again received a disclaimed opinion as this short-term solution was not sustainable and it did not improve the internal control environment. After the local government elections in 2016, the newly elected political leadership inherited a dysfunctional municipality. This status has unfortunately continued, as the new leadership has not been able to address the municipality's prevailing shortcomings.

Significant political instability led to some councillors being expelled and the mayor being removed. This resulted in the council no longer having a quorum for council meetings and being unable to make key decisions and provide the leadership and oversight required to deliver municipal services to the local community. The municipality received R600 million in equitable share funding and R278 million in conditional grants in 2019-20. However, it was not able to use these funds effectively to ensure that water and electricity were consistently supplied to its residents, which led to a number of service delivery protests. Residents had to rely on water tanks for their daily use. In addition, only R42 million remained in the municipality's bank account and it was not able to account for the spending of the grants it had received. These grants were also used to fund the operations of its municipal entity, Maluti-a-Phofung Water, which has equally poor financial management, making it impossible to determine whether the funds received were used for their intended purpose.

Due to its dire financial situation, the municipality failed to pay its creditors. In January 2019, the municipality's movable assets were attached by some creditors, which intensified the challenges it faced. For example, since the assets attached by the creditors included laptops and computers, the municipality was not able to bill its consumers, resulting in a loss of revenue. At the same time, it was still obliged to pay for bulk purchases of electricity and provide free water through tankering services. This had a negative impact on revenue and cash flow, as consumers would not pay bills they had not received.

The municipality has consistently failed to submit its financial statements by the legislated deadline. It only submitted its 2018-19 financial statements on 11 December 2020 after a new municipal manager and chief financial officer were appointed. The 2019-20 financial statements will only be compiled once the 2018-19 audit has been finalised. The closing balance of irregular expenditure disclosed in the 2017-18 financial statements was R465,24 million. However, we could not determine the full extent of this irregular expenditure as municipal officials did not provide supporting documents for the contracts that were awarded. Therefore, we could not confirm that the municipality had complied with procurement prescripts and that contracts had been properly awarded.

In February 2018, the municipality was placed under administration in terms of section 139(1)(b) of the Constitution. Two different administration teams were appointed and neither team completed a year at the municipality. This, together with instability in both political and administrative leadership at the municipality, made it difficult for administrators to hold municipal officials accountable for poor, or a lack of, performance. There were also no consequences when municipal officials did not make information available to support transactions that had been processed. This created a culture in which it was normal for supporting documentation not to be maintained and retained. While the municipal manager and chief financial officer positions have subsequently been filled, there has not been any significant improvement in municipal operations. Administrators did not develop and implement sustainable systems and preventative controls, and this lack of proper guidance resulted in them not being able to work effectively with municipal officials.

To improve the situation at the municipality, the incoming council should set a strong and ethical leadership tone to ensure that leadership and officials are held accountable for their day-to-day responsibilities. The focus should be on cleansing the municipality of the culture of non-performance and lack of consequences.

MASILONYANA

FS

Funds received for the year

Total equitable share	R119 m
Total conditional grants	R109 m

VS

Total bank balance at year-end

R2 m

?

Audit outcomes

2019-20	Outstanding audit
2018-19	Outstanding audit
2017-18	Outstanding audit
2016-17	Disclaimed

Previously under administration

MAY 2017 TO NOVEMBER 2019 (31 MONTHS)

Use of financial reporting consultants

(2016-17)

R5 m

Total salary cost of finance unit

Audit outstanding

Masilonyana is located in Theunissen, a small town in the Free State with a population of approximately 62 770 people. The municipality is surrounded by small farms and is predominantly a mining community for diamonds and gold.

In 2015-16, the municipality regressed from a history of qualified opinions to a disclaimed opinion after a prolonged period of instability in its municipal manager and chief financial officer positions. **Despite the municipality having been placed under administration for 31 months, its financial and performance reporting had not improved, which is reflected in the poor service delivery in the area.** The administrator had not developed and implemented sustainable systems and preventative controls. Due to financial statements not being submitted for a number of years, we are currently busy with the 2017-18 audit, as those financial statements were only submitted on 7 December 2020.

The municipal manager position was vacant due to the council's decision to remove the incumbent, while the chief financial officer had been acting in the position for a number of years. In addition, there was instability in the finance unit, which resulted in several transactions, balances and disclosures captured in the 2017-18 financial statements that could not be supported by appropriate evidence. For example, accurate monthly bank reconciliations were not performed and reviewed, which resulted in numerous reconciling items that could not be supported. This included payments that were confirmed on the bank statements but could not be traced to the general ledger because they were receipts from the daily cash-ups, but were recognised as outstanding payments on the bank reconciliation. Some transactions were also recorded as payable without any supporting documentation.

The provincial cooperative governance department appointed consultants to prepare the 2016-17 financial statements at a cost of R2,3 million. However, the consultants did not cooperate with the municipal staff and thus had a limited impact on the audit outcome. When the consultants were appointed, four of the five senior manager positions at the municipality were vacant. Since the consultants were appointed by the department, they felt that they were stepping into the senior management roles and did not have to report to the lower-level municipal staff. The consultants were also not available to discuss and address errors identified during the audit, as they reported back to the department and not to the municipal manager.

The municipality incurred a net loss of R136,22 million for the year ended 30 June 2017, with its current liabilities exceeding its current assets by R131,96 million at that year-end. Despite receiving R228 million in equitable share funding and conditional grants, the municipality has nothing to show for it, with only R2 million remaining in its bank account at 30 June 2020. In addition, the municipality continues to owe Eskom huge amounts that are long overdue. Our analysis in 2016-17, which is the last financial year we audited, showed that deductions from employees for pension and medical aid contributions could not be traced as having been paid over to third parties. We were also unable to vouch for several disclosures in the financial statements as supporting documentation was not available. This was because proper controls were not maintained when the finance unit moved from one building to another, to make sure that all documentation was accounted for. Therefore, when we requested documentation, no one knew where to start looking for it. We were also unable to audit the usefulness and reliability of the selected key performance area, as the performance report was presented without accurate and complete underlying performance records. This hampers any decisions the council needs to make as it does not have a current set of reliable financial and performance information on which to base its decisions.

The municipality has a history of being unable to support all awards made and demonstrating that procurement prescripts had been followed. It has not implemented consequences, as evident from the lack of investigations into irregular expenditure and allegations of financial misconduct. The municipal public accounts committee and audit committee were not functional and did not meet. Due to management instability, the working environment has prevented the municipality from recovering from the financial challenges of the last few years. This has been worsened by the council's failure to prioritise and fill the vacancies in leadership positions that could help the municipality recover.

Despite our continued efforts to influence positive improvement through our audit recommendations and engagements with provincial leadership, there has been no visible impact. This could be attributed to long-term vacancies in key senior management positions. The instability in political and administrative leadership has left employees with a sense that they are not accountable because there is no corrective action for poor performance and transgressions.

The lack of service delivery has resulted in protest actions over several issues, including the appointment of the municipal manager and mayor, who were subsequently removed from their positions in May 2021.

Financial and performance management at the municipality has been in a dire state for a number of years. Although the current council inherited an already dysfunctional municipality, it is leaving the municipality in a state that is just as bad, if not worse. To improve the situation at the municipality, the incoming council should prioritise filling key vacant leadership positions, especially those of the municipal manager and senior managers. These incumbents, with support from the council, should prioritise rebuilding the municipality, instilling in municipal staff the culture and will to perform their daily duties, and implementing consequences for poor performance.

TOKOLOGO

Funds received for the year

Total equitable share	R55 m
Total conditional grants	R222 m

VS

Total bank balance at year-end

R8 m

?

Audit outcomes

2019-20	Outstanding audit
2018-19	Disclaimed
2017-18	Disclaimed
2016-17	Disclaimed

Currently/previously under administration

Use of financial reporting consultants

(2016-17, 2017-18 & 2018-19)

R19 m

Total salary cost of finance unit

Audit outstanding

Tokologo is one of five municipalities in the Lejweleputswa district in the western Free State, accounting for almost a third of its geographical area. The municipality, which includes the towns of Boshof, Dealesville and Hertzogville, services a population of approximately 29 149 people. It is bordered by the Northern Cape and North West provinces and the Xhariep district.

In 2016-17, the municipality regressed to a disclaimed opinion after its financial system was breached by a virus that destroyed most of its information. Since adequate backups were not available, the municipality was unable to restore reliable data and it continued to operate using unreliable information. This is reflected in its audit outcomes on all financial statements submitted for auditing.

In 2017-18, the municipality again received a disclaimed opinion as, except for the municipal manager, there were no permanently appointed senior managers to assist in rebuilding the municipality's financial system after the breach.

In 2018-19, the municipality received a disclaimed opinion for the third consecutive year, as it could not submit supporting evidence for most of the material line items in the financial statements. In addition, the documentation for infrastructure assets and work in progress was removed from the municipality's archives in 2017-18, which placed a significant limitation on the audit. These missing documents are alleged to have been stolen from the municipality by the previous technical manager, and the municipal manager has opened a criminal case in this regard. There was also a complete disregard for supply chain management prescripts.

After the local government elections in 2016, the newly elected political leadership inherited a dysfunctional municipality. However, unlike the previous council, the leadership did not ensure that financial statements were submitted by the legislated deadlines and is thus leaving the municipality in an even worse state. In addition, the leadership did not fill the vacancies of the chief financial officer and other senior managers.

The municipality operates in crisis mode. A water pipeline between the municipality's three towns, which includes their reservoirs, had not been completed over several years, despite contractors having been paid approximately R17,48 million (59% of the total contract value of R29,59 million). As a result, the municipality had to source water from its own boreholes as well as those belonging to residents to provide communities with water. Because the municipality did not generate revenue from services, such as providing water and removing refuse, it did not have the funds to maintain the cemetery, parks, roads and storm-water drainage. Municipal infrastructure at landfill sites had broken down due to projects not being completed. Landfill sites were neither maintained nor rehabilitated and had no fencing around them, creating a safety hazard and health risk to the community. The municipality received equitable share funding of R55 million and conditional grants of R222 million even though it could not account for what the money was spent on, and on 30 June 2020 it had only R8 million in its bank account.

The municipality is characterised by a lack of commitment from management to resolve prior year findings, numerous vacancies, and inadequate knowledge in the technical unit. Financial and performance reporting was not continuously monitored, and record keeping and filing were not done. In essence, there was no evidence that anyone in the municipality does what they are supposed to do, due to a lack of will and a lack of consequences for any wrongdoing. Support from the provincial treasury and the provincial cooperative governance department was limited to deploying officials to attend the audit steering committee meetings. However, this has not yielded positive results as the municipality requires help to create an environment focused on implementing controls that will detect and prevent errors before they occur.

To improve the situation at the municipality, the political and administrative leadership should set the right tone from the top by implementing and adhering to good governance practices, and enforcing a culture of ethical behaviour. They should also prioritise filling vacancies with competent and dedicated staff as well as implementing consequences for poor performance, especially non-compliance with supply chain management prescripts.

GOVAN MBEKI

Funds received for the year

Total equitable share	R284,50 m (2018-19: R257,24 m)
Total conditional grants	R143,71 m (2018-19: R126,2 m)

VS

Total bank balance at year-end

R202,4 m
(2018-19: R113,3 m)

?

Audit outcomes

2019-20	Disclaimed
2018-19	Disclaimed
2017-18	Disclaimed
2016-17	Unqualified with findings

Currently under provincial administration

NOVEMBER 2018 TO DATE

Use of financial reporting consultants R1,5 m*

(2018-19 & 2019-20)

Total salary cost of finance unit R50,02 m (2018-19: R47,52 m)

** 2019-20: Consultants were used for TAX SERVICES ONLY*

Govan Mbeki is the smallest of seven municipalities in the Gert Sibande district, covering an area of 2 955 square kilometres. The municipality services a community of approximately 340 091 people in 108 894 households. It is mainly agricultural, with three urban areas, namely Leandra, Greater Secunda and Bethal / eMzinoni.

The municipality has been on a downward trajectory for the past few years, having regressed from a financially unqualified audit opinion in 2016-17 to consecutive disclaimed opinions for the past three financial years. In 2019-20, the municipality received R428,21 million in equitable share funding and conditional grants, but only R202,4 million remained in its bank account at year-end. We could not confirm how the funds were used, as the municipality was unable to provide us with the supporting documentation or explanations we needed to formulate any conclusion. Bank and cash was one of the items for which the municipality could not provide sufficient records or explanations. The municipality struggled to prepare proper periodic reconciliations to ensure that the bank balances on the accounting system matched up with the balances held by the bank, which resulted in reconciliation items that management could not explain or support at year-end.

The Municipal Standard Chart of Accounts was first implemented during 2017-18, and the municipality never fully resolved some of the significant challenges it experienced with migrating to the new system. This resulted in material misstatements that have still not been fixed, especially for bank and cash as well as revenue. The billing system is also plagued with weaknesses relating to the credibility of the revenue masterfile. For example, some consumer debtors had never been billed but were using the services provided by the municipality. These challenges undermined the credibility of the financial statements. The assistance from consultants appointed during the 2018-19 financial year to correct the previous year's errors and prepare the municipality's financial statements did not bear fruit. The municipality then used its in-house finance staff to prepare the 2019-20 financial statements, which did not improve the audit outcomes, as we continued to experience unreliable and insufficient information to support the restated opening balances and current year transactions. This was because the municipality did not engage the developers of Munsoft early enough to interrogate the system and adequately address the shortcomings.

There were material inconsistencies between the indicators and targets in the planning documents and those reported in the performance report. The municipality was also unable to support some of the reported targets and achievements, making it impossible for us to conclude on the credibility of the reported performance. This brings into question the municipality's decisions during the year as neither the financial nor performance information was credible. Furthermore, the municipality did not effectively manage its infrastructure projects. For example, the construction of a new wastewater treatment works in Charl Cilliers, valued at R15,85 million, commenced on 17 October 2019 with a planned completion date of 30 June 2020, which was extended to 30 November 2020. However, a progress report dated 30 October 2020 indicated that only 35% of the work amounting to R6,41 million had been done. During a site visit in December 2020, we observed that the project had still not been completed. This meant that the residents of Charl Cilliers had still not received much-needed sanitation services.

All the issues raised above show that management and those charged with governance were unable to effectively run the municipality, which had a dire impact on service delivery. As a result, service delivery protests continued in the 2019-20 financial year, highlighting the dissatisfaction of the communities this municipality serves. Some of the service delivery protests during the year were because of the lack of electricity provided to Bethal, eMzinoni and eMbalenhle.

During the 2019-20 financial year, the municipality reported irregular expenditure of R222,1 million, compared to R251,2 million in 2018-19, due to non-compliance with procurement process requirements. This accumulated into a closing balance of R880,05 million at year-end. The poor status of the municipality's record keeping resulted in limitations in our audit of procurement and contract management, as we could not audit awards to the value of R37,5 million and R12,6 million for 2019-20 and the previous two years, respectively, because the requested contracts and quotations were not provided for auditing. We were therefore not able to conclude on whether the municipality had complied with all applicable laws and regulations. The municipal council did not provide effective oversight throughout its term, especially in this regard, as it failed to investigate the irregular expenditure of prior years. The council therefore created a culture of high tolerance for non-compliance without any consequences.

These deficiencies were mainly due to the following vacancies and instability in key management positions, which led to a complete breakdown in internal controls:

- Instability in the municipal manager position over the past three years. The municipal manager was suspended after the 2019-20 financial year-end on allegations of maladministration and poor performance.
- The chief financial officer was in the position for the last three years, but was suspended after the 2019-20 financial year-end on allegations of supply chain management fraud.
- The executive mayor resigned after the 2019-20 financial year-end.
- The finance unit had a vacancy rate of 36% in 2019-20, compared to 32% in 2018-19, which affected its ability to perform daily and monthly preventative internal controls.

While the municipality did attempt to fill these key positions with acting personnel, they did not have the skills required to fulfil the roles as intended. The district municipality also assisted by seconding officials to fill the municipal manager and chief financial officer positions; however, this did not translate into improved audit outcomes because of the unstable control environment.

The municipality's governance structures (municipal public accounts committee, internal audit unit and audit committee) did not provide the required level of assurance to significantly improve governance and the control environment. The internal audit unit was inadequately staffed and the recommendations from the audit committee were not fully implemented. The mayor and municipal council were slow to respond to these challenges.

The municipality has been under mandatory provincial intervention in terms of section 139(1)(a) of the Municipal Finance Management Act since November 2018. The provincial cooperative governance department assisted the municipality with developing a financial recovery plan and the provincial treasury helped the municipality to implement the plan, but this did not yield any improvements, mainly due to weaknesses in the billing and collection processes. The provincial cooperative governance department also established a cash-flow committee to rotate payments to suppliers so as to alleviate excessive interest on late payments. Unfortunately, this committee was rendered ineffective by limited cash resources due to challenges around billing and debt recovery.

In the 2018-19 financial year, the municipality was also placed under section 106(1)(b) of the Municipal Systems Act, which relates to non-performance and maladministration. The investigation report was finalised after year-end (October 2020) and the outcome of the investigation led to the mayor resigning days after the report was issued. The council is in the process of implementing the report's recommendations.

The municipality's financial health remained vulnerable during the financial year under review. The council approved an unfunded budget (the budgeted operating expenditure of R2,4 billion exceeded the operating revenue of R2 billion), which already meant that it would not realise its planned indicators and targets. The municipality struggled to maximise its revenue from the services rendered and failed to maximise its debt collection. This negatively affected the payment of suppliers, especially Eskom and Rand Water. The municipality does not have any payment agreements in place with bulk suppliers, resulting in R199,5 million of the total fruitless and wasteful expenditure of R202 million relating to interest on late payments to these two suppliers. This is one of the very few amounts disclosed in the financial statements that we were able to audit. Such leakages in the public purse could have been used for much-needed service delivery.

We continue to urge the leadership of the province and the municipality to work together to achieve the following:

- Fill vacancies in key positions in order to stabilise the municipality.
- Ensure that the appointed municipal manager and team implement a solid system of internal control, including monitoring controls, to ensure that the internal controls are implemented and function as intended.
- Ensure that policies and procedures on individual performance management are implemented so that appointed individuals step up and take accountability for the municipality's results.
- Engage the system developers of Munsoft earlier so that they can interrogate the system and adequately address the shortcomings – this must be done in collaboration with someone skilled in accounting to ensure that the challenges with the accounting system are addressed in line with the accounting principles.

When these recommendations have been implemented, accountability will improve, which will have a positive effect on both service delivery and the credibility of the municipality's financial and performance information.

!KHEIS

NC

Funds received for the year

Total equitable share	R22,7 m (2018-19: R23,1 m)
Total conditional grants	R15,3 m (2018-19: R23,2 m)

VS

?

Total bank balance at year-end

R0,77 m
(2018-19: R1,94 m)

Audit outcomes

2019-20	Disclaimed
2018-19	Disclaimed
2017-18	Disclaimed
2016-17	Qualified

Currently/previously under administration — ✗

Use of financial reporting consultants (OVER 4 YEARS) — R3,6 m

Total salary cost of finance unit — R6,3 m (2018-19: R4,7 m)

!Kheis is one of five municipalities in the ZF Mgcawu district, accounting for 11% of its geographical area. It services around 4 307 households in the towns of Groblershoop, Boegoeberg, Opwag, Topline and Wegdraai, and the surrounding farming communities. The Orange River runs from the southeast of the area through to the northwest, contributing to the cultivation of table grapes, which are marketed and exported.

The municipality's audit outcome regressed to a disclaimed opinion during the current administration's term. Apart from the accounting officer, who joined the municipality during the previous financial year, key staff members were employed over the four-year period. Despite this, there were still inadequate competence and capability, which ultimately resulted in the deterioration of the internal control environment as basic internal control processes were not implemented. Such controls included monthly reconciliations, proper record keeping for invoices, and frequent updating of the registers for contracts, commitments as well as unauthorised, irregular and fruitless and wasteful expenditure. The municipality also failed to show an understanding of specific financial framework requirements by recording certain transactions on a cash basis rather than via the accrual basis of accounting. These poor practices being the norm, raises the question of how management and the council can make strategic decisions that best serve the community using such incomplete and inaccurate information.

There were also deficiencies in how internal controls were designed and implemented to ensure that there was evidence available to support the targets of some of the performance indicators reported in the performance report. As a result, we could not conclude on the reliability of the reported achievement of these performance indicators. In prior years, we repeatedly reported the lack of adequate systems to ensure the safekeeping of documentation in support of the financial statements and the performance report. However, leadership failed to implement an audit action plan to address these internal control weaknesses, resulting in repeat findings and widespread material misstatements.

The municipality's financial health is in a dismal state due to issues such as the information required for a proper analysis being incomplete. As a result of cash-flow challenges, the municipality could not meet all of its financial obligations and could not settle supplier accounts within 30 days of receiving invoices. On average, the municipality took 643 days to pay creditors and 648 days to collect revenue. Its current liabilities exceeded its current assets, and the R0,7 million cash it had available in the bank at year-end was not enough to pay the R30 million owed to municipal creditors. This means that the following year's budget is being used to pay for prior year expenses. Municipal suppliers bore the brunt of late payments, which negatively affected their businesses.

The municipality failed to implement both sound financial reporting consistent with the financial reporting framework and accountability for the conditional grants it received. As a result, its equitable share allocation was reduced and it was not permitted to roll over unspent conditional grants that were not cash-backed, further compromising its ability to meet service delivery expectations. This has caught the attention of the Public Protector, who is currently investigating the municipality's management of conditional grants. A large portion of the municipality's expenses are made up of salaries and councillor remuneration, which are paid first from the little available cash. Salaries and wages paid to employees amounted to 70% of cash receipts from operations, leaving only 30% to fund operational expenses and deliver services. The lack of controls around billing revenue and recording receivables, combined with the poor revenue collection for services rendered, adds to the municipality's dismal financial situation.

We also remain extremely concerned about the status of the municipality's compliance with legislation. As reported in prior years, the municipality has been unable to support all awards made and we cannot confirm the full extent of irregular expenditure. The Municipal Finance Management Act requires municipalities to recover irregular expenditure from the person liable for the expenditure, unless – after investigation by a council committee – the council certifies the expenditure as irrecoverable and writes it off. The municipality wrote off irregular expenditure without investigating why it was incurred or determining whether disciplinary steps needed to be taken against liable officials, which resulted in staff not being held accountable for transgressions. This should be of great concern to the council as well as the oversight departments in the province.

Despite our continued efforts to influence positive improvement through our audit recommendations and engagements with provincial leadership, there has been no visible impact. This could be attributed to the tone set by leadership and management, which created a culture of employees not caring about their responsibilities. There is no accountability and no corrective action is taken against poor performers and transgressors. For example, every year, most of the prior period adjustments to the financial statements cannot be explained or accounted for. We could not derive any assurance from the municipality's established assurance providers, which led to the current dire state of governance and accountability at the municipality and points to the failure of the combined assurance model. This was not helped by the slow response from the provincial cooperative governance department and the provincial treasury to support the municipality, as interventions did not commence in time to have a positive impact on the compilation of the 2019-20 financial statements. The audit committee experienced the same slow response, which also affected its ability to provide assurance.

The situation can be remedied by leadership, as a starting point, instilling in municipal staff the culture and will to perform their daily duties. Leadership should also use training interventions to ensure that staff understand the basic disciplines. The council should intensify the level of support offered to the municipal leadership so that a proper tone is set from the top. A lot of work needs to be done to cleanse the municipality of the culture of non-performance and lack of consequences.

RENOSTERBERG

NC

Funds received for the year

Total equitable share	R24,7 m
Total conditional grants	R16,9 m

VS

Total bank balance at year-end

R0,7 m

(AS PER UNAUDITED ANNUAL FINANCIAL STATEMENTS NOTE)

?

Audit outcomes

Year	Outcome	Year	Outcome
2019-20	Outstanding audit	2017-18	Disclaimed
2018-19	Outstanding audit	2016-17	Qualified

Currently under administration

7 SEPTEMBER 2020 TO DATE

Use of financial reporting consultants

(2016-17 & 2017-18)

R5,5 m

Total salary cost of finance unit

Audit outstanding

Renosterberg is the smallest of eight municipalities in the Pixley ka Seme district, accounting for only 5% of its geographical area. The municipality services a population of fewer than 12 000 people in the towns of Philipstown, Petrusville and Vanderkloof. Philipstown and Petrusville are known for their unique Karoo architecture, with many homes still in their original state, while Vanderkloof has the second-largest dam (by volume) in the country.

We are currently auditing the municipality's financial statements for the past two years, which were not submitted on time, and the audit outcomes are thus still outstanding. **The late submission of financial statements shows a lack of leadership accountability and a blatant disregard for legislative timelines and oversight processes.** Without an audit, it is difficult for oversight structures to adequately hold leadership accountable for the municipality's performance.

During the municipality's last audit (for the 2017-18 financial year), the state of its financial records and internal control processes had weakened to such an extent that its audit outcome regressed. This was mainly due to vacancies in key management positions, poor record keeping, and a lack of accountability and consequences.

In certain instances, the municipality did not timeously implement basic internal control practices, including monthly bank reconciliations; proper record keeping for invoices; and regular updating of registers for contracts, commitments as well as unauthorised, irregular and fruitless and wasteful expenditure. As a result, management could not adequately report on the municipality's financial affairs and service delivery performance. The municipality also had inadequate processes in place to account for funds received and payments made, which ultimately affected its decision-making ability.

There was widespread non-compliance by the municipality, most notably in the areas of procurement and contract management, revenue management, and strategic planning and performance management. We experienced continuous limitations during our audit of procurement and contract management, as management could not provide information relating to the procurement processes followed. The extent of the municipality's non-compliance with Municipal Supply Chain Management Regulations and officials' inability to apply the principles of fairness, competitiveness, equality and transparency as enshrined in the Constitution, warrant great scrutiny and should concern the council as well as other oversight departments in the province. Management could not quantify the municipality's irregular expenditure and no consequences were instituted against officials found to have been negligent in their duties.

There were inadequate processes in place to ensure that creditors were accounted for when goods and services were received, that suppliers were paid within 30 days of invoices being received, that receivables were recognised when services had been rendered to the community, and that strategies were developed to enhance debt collection. Amounts deducted from employees on behalf of third parties for pension contributions and pay-as-you-earn were not paid over within seven days, as required.

As mentioned earlier, we are still performing the audit for the 2018-19 period, and it is concerning that the municipality incurred a deficit for the year of R35,4 million (an increase of R13,8 million from the previous year) and reflected a net current liability position. This indicates that the municipality is unable to meet its short-term obligations, showing its dire financial situation.

The municipality has been plagued by political and administrative challenges. The significant number of vacancies in key management positions also hindered its ability to exercise accountability due to the continuous vacancies and rotation of staff acting in these positions. The positions of municipal manager and chief financial officer have been vacant for a number of years, contributing to the municipality's instability and lack of accountability. An acting municipal manager and chief financial officer were in place during the 2017-18 period. However, the detrimental effect of having a vacant chief financial officer position during 2017-18, along with other key senior management positions, resulted in the municipality being heavily dependent on consultants to prepare the financial statements. This situation was made even worse as the money spent on consultants did not yield any return on investment.

The municipality also had no audit committee, internal audit unit or municipal public accounts committee. Furthermore, the council failed to exercise its duties and enforce accountability within the municipality. This created an environment where staff continued to transgress without any consequence due to inefficient and ineffective oversight structures.

The provincial member of the executive council for cooperative governance dissolved the municipality due to its continued dysfunction and lack of clear leadership, and it has been under administration since 7 September 2020. The provincial cooperative governance department, provincial treasury, Pixley ka Seme District and respective members of the executive council intervened to monitor and support the municipality, but these interventions were unfortunately not very successful. The municipal council failed to implement and support the National Treasury's discretionary financial recovery plan that ran from 2018 until November 2019. The municipality also refused to cooperate with, accept, support or subject itself to monitoring by two other arms of government, namely the National Treasury and the provincial legislature.

The municipality requires strong and stable leadership to instil a culture of discipline, consequences and effective preventative controls. We also urge the municipality to embark on a systematic process to ensure that its financial statements are submitted for auditing on time, and oversight structures to hold the municipal leadership accountable for its performance.

We are encouraged that steps have been taken to bring stability to the municipality, as the provincial cooperative governance department seconded an acting municipal manager and the provincial treasury an acting chief financial officer for a one-year period effective March 2021 and April 2021, respectively. Filling these key positions will, in the short term, help the municipality to achieve stability, provide the necessary leadership and enable consequence management. We do, however, encourage the municipality to embark on a recruitment process to permanently fill these positions as soon as possible, to ensure that the short-term stability benefits will be maintained after these secondment periods end.

LEKWA TEEMANE

NW

Funds received for the year

Total equitable share	R46,4 m (2018-19: R44,9 m)
Total conditional grants	R34,7 m (2018-19: R22,8 m)

VS

?

Total bank balance at year-end

R6,1 m
(2018-19: R1,7 m)

Audit outcomes

2019-20	Disclaimed	2017-18	Disclaimed
2018-19	Disclaimed	2016-17	Disclaimed

Previously under administration

1 JULY 2019 – 30 JUNE 2020 (12 MONTHS)

Use of financial reporting consultants

R11,9 m
(2018-19: R5,5 m)

Total salary cost of finance unit

R11,1 m
(2018-19: R12,9 m)

Lekwa Teemane is located in the Dr Ruth Segomotsi Mompati district, accounting for approximately 7,75% of its geographical area. The municipality, which services 14 930 households, is situated in Christiana – an agricultural town on the banks of the Vaal River – and also includes the town of Bloemhof. The area is known for the discovery of diamonds in the river banks, but today the main economic activity is agriculture.

The municipality obtained a disclaimed opinion for 13 of the past 14 years (92%). In the past four years, the municipality faced serious challenges, including the accounting officer being suspended due to allegations of irregularities and the chief financial officer position being vacant. This resulted in a significant breakdown of basic financial disciplines as well as poor record keeping. As we reported in prior years, the financial statements that were submitted did not agree to the general ledger and sub-ledgers. During 2019-20, management was able to submit financial statements that agreed to the general ledger, but was still unable to provide evidence for the recorded transactions.

One of the reasons for the continued disclaimers is the numerous changes to consultants. Although the chief financial officer position was filled in March 2019, the municipality does not have adequate technical proficiency and there is a lack of basic understanding of the financial reporting framework. Basic key controls, such as monthly and asset reconciliations, meter readings and transaction reviews, are not done throughout the year. The municipality then relies heavily on consultants to source these records, compile registers and perform reconciliations, which only happens after year-end. However, because consultants are appointed late and enter an environment with weak or no financial controls, a lack of supporting evidence and a shortage of technical proficiency, neither improvements nor skill transfers are realised. It is extremely concerning that even though the vacancy rate in the finance unit was only 3% and the chief financial officer position was filled, the municipality was unable to implement basic key financial controls and instead relied on consultants to do so.

Due to the disclaimed opinion, we could not confirm that the entire total expenditure budget of R318 million, made up of R290 million operational and R28 million capital expenditure, had been appropriately spent on service delivery. The municipality is in serious financial distress with high uncertainty about whether it will be able to adequately fund its operations in future. This is evident in the municipality implementing an unfunded budget and overspending by R172 million, of which R41 million was on cash items.

The municipality is characterised by poor cash-flow management, increasing outstanding debt and payments to creditors, and excessive supplier-payment periods. The municipality relies heavily on the equitable share and is not able to pay key suppliers such as Eskom and the Department of Water Affairs and Sanitation. In addition, the department took the municipality to court, claiming R173 million for extracting water from the Vaal River. The matter was referred to the North West High Court on 9 December 2019 and is still ongoing. Due to these financial challenges, the municipality is unable to replace ageing and dilapidated infrastructure, resulting in high water and electricity losses. Furthermore, the roads around Christiana are in a poor state due to a lack of maintenance over several years. During our visit to the solid waste disposal sites in Bloemhof and Christiana, we noted that the fencing had been vandalised, resulting in no access control to these sites. Looking at these matters, it is then not surprising that community protests demanding service delivery and the removal of the municipal manager are common.

The municipality's irregular expenditure balance was qualified due to material differences between the amount reported in the financial statements and the amount contained in the underlying records. The irregular expenditure is underpinned by many procurement and contract management weaknesses, such as:

- awards to service providers who are also employees of the municipality or in the service of other state institutions
- supply chain management role players with interests in suppliers participating in the contract process
- competitive bids not being invited and deviations not being justified
- weak or no contract management, including contractors not being monitored.

The municipality was placed under administration per section 139(1)(b) of the Constitution from July 2019 to June 2020. However, this did not yield positive results due to conflicts between the administrator, the mayor and the municipal manager. This infighting created an environment in which management did not heed our call to action, including implementing our recommendations, which resulted in a missed opportunity to turn around the municipality's performance. The culture of non-performance has become the accepted norm and no corrective action is taken against transgressors and poor performers. The weak political tone created dysfunctional council committees, with no appetite to take corrective action. This not only resulted in the municipality not collecting revenue, but also diverted the focus of the administrator, who could not implement proper action plans to improve the municipality's performance.

The administrative leadership should prioritise putting the basics in place, including filling and stabilising key positions and capacitating current staff. The new council should prioritise appointing a qualified accounting officer who has experience in the local government sphere to oversee the implementation of basic controls, set the right tone, and implement corrective action for poor performance and transgressions. The accounting officer, once appointed, should be supported by the provincial treasury and provincial cooperative governance department to address prior year matters and institutionalise internal controls. The internal audit unit and the audit committee must support the municipality by ensuring that the action plan is regularly reviewed and monitored. The municipal public accounts committee must be capacitated to monitor the implementation of consequences.

MADIBENG

NW

Funds received for the year

Total equitable share	R695,6 m (2018-19: R624,9 m)
Total conditional grants	R165,9 m (2018-19: R235,0 m)

VS

?

Total bank balance at year-end

R260,7 m
(2018-19: R51,6 m)

Audit outcomes

2019-20	Disclaimed
2018-19	Disclaimed
2017-18	Disclaimed
2016-17	Disclaimed

Previously under administration

1 JULY 2019 – 30 JUNE 2020 (12 MONTHS)

Use of financial reporting consultants

R23,7 m
(2018-19: R35,4 m)

Total salary cost of finance unit

R32,7 m
(2018-19: R33,6 m)

Madibeng is located within the Bojanala Platinum district and serves approximately 554 000 people across urban and rural areas, including villages, farms and an established industrial area. The municipality is known for its diversified economy, with the predominant economic activities being mining, manufacturing, agriculture and tourism.

The current administration inherited a dysfunctional municipality and has done little to improve its status, as reflected in the four consecutive disclaimed opinions received since 2016-17. Current leadership has failed to implement basic controls, including key reconciliations, on a regular and timely basis. Transactions were processed without valid supporting documents and the lack of proper review and supervision allowed such instances to go undetected. Despite the interventions of both the provincial treasury and the National Treasury, the culture of complacency persists.

From July 2019 to June 2020, while the municipality was under administration, the make-up of the administration team was constantly changing, going through two municipal managers and three chief financial officers in that period. This instability has made it difficult for the municipality to implement appropriate and timely consequences and instil financial disciplines. Despite a substantial investment in personnel within the finance unit, we noted an increase in the reliance on consultants to prepare financial statements over the past two years, raising questions about the commitment, competence, and skill levels within the unit. Additionally, the consultants' task of compiling credible statements and upskilling finance staff was made impossible by the poor status of the municipality's underlying records. The same consultants were used to prepare the financial statements for the current and prior years. The onus is on the current leadership to critically assess whether any value is derived from these engagements given the lack of progress being made.

The municipality has operated with less than half of its required senior managers for the past four years. The impact of this is evident in its inability to perform and report against key delivery targets. Due to the complete lack of processes to collect the required financial and performance information, we were unable to determine whether allocated funds had been used for their intended purposes. The lack of improvement despite repeat findings and recommendations echoes the lack of accountability and commitment to quality reporting embedded in this environment.

We could not assess the full extent of irregularities within the procurement processes, as we were not provided with all relevant information. We also could not determine if goods and services had been procured at reasonable prices through an unbiased and fair process. This situation persists because there appears to be no fear of consequences, as most previously identified irregular and fruitless and wasteful expenditure was not investigated.

The municipality relies heavily on the equitable share to provide services to the community. However, the municipality is unable to obtain regular meter readings due to broken meters and resistance from community members, who sometimes prevent municipal officers from accessing the meters. This hostility stems from what some communities consider to be unfulfilled promises made during the 2016 election campaign. As a result, the municipality has, in some instances, relied on estimates as old as five years for billing water, electricity and sewerage. The inaccuracies in billing also contributed to the municipality's inability to collect the money it is owed for these services, and as at 30 June 2020, the municipality did not expect to collect R2,3 billion (89%) of its R2,6 billion in debt. By not issuing demand letters, handing over accounts and disconnecting services, the municipality failed to effectively implement its credit policy.

In November 2020, the National Treasury warned the municipality about its late payments to bulk suppliers. Reported payables amounted to R1,4 billion at year-end, with cash reserves amounting to only R260 million. As reported in 2018-19, an overdue loan of R163 million, due to the Public Investment Corporation, was again not included in the payables despite the municipality having lost its appeal contesting this amount in the Supreme Court of Appeal.

The impact of the continuing deterioration of the internal control environment and the resultant financial strain placed on the municipality can be seen in the growing number of service delivery complaints. Many of these stem from the frequent interruptions in the water supply and the inadequacy of storm-water and sewerage systems. Another serious concern is the poor or non-existent maintenance of wastewater infrastructure, treatment and disposal, with some plants and pump stations completely non-functional. Wastewater overflows and spillage pollute the environment and pose serious health risks to the receiving communities.

A forensic investigation into previously reported financial losses of R31,5 million due to an investment in VBS Mutual Bank has been finalised, but the recommendations have yet to be implemented. The accounting officer has been notified of a material irregularity resulting from the loss. We will assess the adequacy of planned actions to strengthen controls and implement consequences once we have received a response to the notification. Unauthorised debit orders to pay accounts of private individuals, detected in 2018-19, continued in 2019-20 despite the matter having been reported for police investigation.

The persistent disregard of our recommendations and lack of consequences against officials responsible for areas with repeat material findings are concerning. For audit outcomes to improve, there needs to be stability in key leadership positions to bring about a much-needed cultural change. A tone of zero tolerance for poor performance and transgressions has to be set at the top by the administrative team, mayor, municipal manager and senior managers. Senior management must ensure that basic financial internal controls are implemented and reviewed regularly. If critical leadership challenges are not addressed, the municipality runs the risk of further deteriorating and continuing to provide poor services to its residents.

MAMUSA

NW

Funds received for the year

Total equitable share	R55,9 m (2018-19: R51,2 m)
Total conditional grants	R39,2 m (2018-19: R25,8 m)

VS

?

Total bank balance at year-end

R5,2 m
(2018-19: -R0,3 m)

Audit outcomes

2019-20	Disclaimed	2017-18	Disclaimed
2018-19	Disclaimed	2016-17	Disclaimed

Previously under administration

2 MAY 2019 – 31 JANUARY 2020 (9 MONTHS)

Use of financial reporting consultants

R11,8 m
(2018-19: R10,1 m)

Total salary cost of finance unit

R9,4 m
(2018-19: R7,6 m)

Mamusa is located in the Dr Ruth Segomotsi Mompati district, accounting for 7,8% of its total geographical area. The municipality services 15 473 households in the town of Schweizer-Reneke and the surrounding agricultural area. The town is rich in diamond deposits and is also sometimes referred to as the City of Sunflowers. **The municipality holds the unenviable record for the most consecutive disclaimed opinions in the province, which now stands at 12 years.**

The outgoing political leadership took over a municipality lacking both an effective record-management system and respect for daily control activities. We have repeatedly reported this lack of an adequate system to protect documentation that supports the financial statements and performance report. Financial information was also lost due to a fire in June 2017, which occurred when a municipal building and a library were torched by residents protesting the removal of the acting municipal manager. Since then, the situation has only deteriorated. For example, there is no established basic foundation for properly safeguarding records, such as structured furniture for filing. As a result of there being no proper record-management system, leave records and employee files could not be found or made available for audit purposes.

In 2019-20, the municipality incurred a net loss of R39,6 million, its current liabilities exceeded its current assets by R173,2 million, and it operated under an unfunded budget. The financial plan adopted by the council was therefore inadequate to implement the identified priorities for the year and is a leading indicator of impending financial distress. The municipality does not receive as much conditional grants as other municipalities because the district municipality, as water services authority, receives the bulk of the grants for infrastructure development.

The municipality did receive municipal infrastructure grant funding of R15,6 million, of which R13,5 million was spent. However, we were unable to vouch for normal general expenditure, which included limitations on employee-related costs. Due to limitations during our audit, we could not confirm what this grant had been spent on and whether the spending was in line with the conditions of the grant.

As reported in prior years, the municipality has been unable to support awards made and thus we cannot confirm the full extent of irregular expenditure. Most of the time, the municipality did not follow adequate procurement processes, ensure that competitive bidding was observed, and that records to prove compliance with supply chain management prescripts were retained. The irregular expenditure balance has been qualified for the last 12 years.

Unfortunately, while the outgoing political leadership inherited a dysfunctional municipality, it is leaving the municipality in a similar – or even worse – state. With so many years of limitations, it is difficult to identify specific areas of concern due to the cumulative effect of poor record keeping and non-adherence to supply chain management policies and procedures. The municipality has also not effected any consequences, as evidenced by the lack of investigations into irregular expenditure and allegations of financial misconduct. The municipal public accounts committee is not functional and the municipality has a backlog of oversight reports spanning 10 financial years. The working environment and political infighting are preventing the municipality from recovering from years of financial challenges.

The failure of municipal political leadership to exercise oversight resulted in the provincial executive committee resolving to invoke an intervention in terms of section 139(1)(b) of the Constitution from 2 May 2019. The municipality had two administrators over the period of this intervention before the provincial executive committee ultimately resolved to dissolve the council in terms of section 131(1)(c) of the Constitution on 25 September 2019. The first administrator resigned due to death threats and constant intimidation by community members, allegedly in support of a particular faction.

The skills required to operate a municipality as mandated have been absent for many years, as evident in the senior management vacancy rate of 60%. The vacancies at senior management level and allegations of misconduct against those in management positions show that municipal staff have been deprived of an exemplary leadership tone.

Years of continuous neglect of financial affairs, good governance and sound accountability have left the municipality's financial health in a dire state and service delivery in a state of disaster. The National Treasury has repeatedly threatened to withhold the equitable share from the municipality, while Eskom has threatened to suspend the electricity supply due to non-payment. Over the past two years, various court orders have allowed private companies to attach both movable assets and the municipal bank account as a result of debt commitments not being honoured.

Performance planning and reporting is merely a compliance exercise, with the promised services not being delivered as evident in our performance reporting findings on a lack of information and unreliable reporting. The water and sanitation infrastructure has continued to deteriorate despite our detailed reports and recommendations. Some wastewater treatment facilities and infrastructure are dilapidated and not properly operated or maintained, resulting in raw, untreated sewage flowing directly into adjacent rivers and water resources.

Despite our continued efforts to influence positive improvement through our audit recommendations and engagements with provincial leadership, this has had no visible impact. This could be due to the long-term vacancies at the municipality. The tone set by leadership and management is weak and unstable, which has created a culture in which employees do not care and have no sense of accountability, as they do not face corrective action for poor performance and transgressions. For example, every year, most of the prior-period adjustments to the financial statements cannot be explained or accounted for.

The provincial treasury seconded consultants to assist in preparing the financial statements and resolving the long-time qualification findings. However, these consultants had a limited impact on the audit outcomes due to the unreliable underlying financial records provided to them and the weak control environment. Every year, consultants adjust the opening balances on the financial statements in an unsuccessful attempt to resolve issues, as the underlying supporting information is not, and will likely never be, available. Sadly, the trend of unsupported transactions extends to each new financial year without any improvement in record keeping. The inadequately staffed finance unit did not allow for any transfer of skills or support to consultants. The chief financial officer position was vacant for the last nine months of the 2019-20 financial year and the finance unit has had a vacancy rate of 20% or more over the past five years.

As a starting point, filling key vacant leadership positions will help to begin the long process of rebuilding the municipality and instilling in municipal staff the appropriate culture of diligence and performance.

NW MAQUASSI HILLS

Funds received for the year

Total equitable share	R128,4 m (2018-19: R111,1 m)
Total conditional grants	R36,6 m (2018-19: R63,1 m)

VS

Total bank balance at year-end

R24,2 m (2018-19: R16,3 m)

?

Audit outcomes

2019-20	Disclaimed	2017-18	Disclaimed
2018-19	Disclaimed	2016-17	Qualified

Previously under administration

1 SEPTEMBER 2018 – 31 AUGUST 2019 (12 MONTHS)

Use of financial reporting consultants

R15,1 m (2018-19: R6,7 m)

Total salary cost of finance unit

R15,8 m (2018-19: R14,6 m)

Maquassi Hills is one of three municipalities in the Dr Kenneth Kaunda district, accounting for a third of its geographical area. The municipality services about 16 333 households in the main towns of Leeudoringstad, Makwassie, Witpoort and Wolmaransstad. The latter is a maize-farming town between Johannesburg and Kimberley, and an important diamond-mining area.

The municipality regressed from a qualified opinion to a disclaimed opinion in 2017-18 because the consultant that helped the municipality prepare the financial statements did not have well-trained resources who understood the Municipal Standard Chart of Accounts. As a result, the financial statements submitted for auditing contained balances and transactions that could not be supported. The municipality terminated the consultant's contract based on the poor-quality financials, which led to further disputes between the two parties.

The situation at the municipality is worsening each year as the control environment remains weak. The municipal manager position was vacant from 2017-18 until it was filled on 1 March 2019. Due to leadership challenges and infighting, however, the appointed municipal manager was suspended in March 2021. Instability in the accounting officer position resulted in a failure to implement and regularly monitor basic financial controls, the absence of an adequate action plan, and an environment that accommodated poor performance.

The municipality is under financial distress and relies heavily on the equitable share. A significant portion (61%) of the equitable share was spent on employee costs, with the remainder going to bulk purchases. It is therefore concerning that the municipality incurred fruitless and wasteful expenditure of R4 million on interest and penalties, and paid exorbitant consultant costs for financial reporting services, which equate to 96% of the finance staff salary bill.

Based on the disclaimer and concerns about the accuracy, validity and completeness of the performance information, we cannot confirm that the entire total expenditure budget of R446 million, made up of R415 million operational and R30 million capital expenditure, was appropriately spent on service delivery. For example, for one project to upgrade a gravel road in Lebaleng, the municipality terminated the contract with a service provider before the project was completed but after the full amount of R4,12 million had already been paid. A new service provider then had to be appointed. A significant portion of revenue could not be recovered and there was no leadership will to implement a robust collection process. The municipality also provided for a substantial portion of revenue (98%) to be written off as it is highly unlikely to be recovered.

In November 2020, the National Treasury warned the municipality about late payments to bulk suppliers. These late payments resulted in water supply shortages and numerous community protest actions around service delivery. Our site visits confirmed the continuing deterioration of wastewater treatment plants, pump stations, landfill sites and illegal dumping hotspots, which could severely affect the health and safety of the surrounding communities. Our current audit also shows shortcomings in this area. For example, we qualified bulk water purchases due to inadequate supporting documents for the expenses disclosed in the financial statements. The disastrous state of the roads around Wolmaransstad and in Kgakala, as well as the fact that the municipality's reported achievements against the predetermined service delivery objectives were not supported by evidence, clearly illustrate the poor state of service delivery.

The municipality relies on consultants to prepare the financial statements each year. Disappointingly, despite our key message in the previous year about the late appointment of consultants, they were again appointed well after year-end. They were also expected to produce financial statements in a weak control environment characterised by a lack of reconciliations and poor record keeping. For example, the municipality does not have a centralised, access-controlled location for record keeping. As a result, most of the documents required for audit purposes could not be located. Consultants were paid R15,1 million in the current year. This is equivalent to 96% of the finance unit staff cost of R15,8 million, which covers more than 60 employees, including a chief financial officer position that was filled for 10 months of the year. The cost of consultants therefore comes down to expenditure incurred in vain, as it did not result in any improvement in the audit outcome.

The increasing irregular expenditure balance remains a concern and we raised a qualification on the completeness of the irregular expenditure as not all incurred irregular expenditure was included. Shortcomings include contracts that were extended or modified without the appropriate approval, a lack of monitoring of contractors, and local content requirements not being properly applied. The instability in the accounting officer position, the dysfunctional municipal public accounts committee and the lack of political will by the council to take action, contributed significantly to the increased irregular expenditure and the fact that it was not investigated.

The poor audit outcomes and service delivery issues were made worse by infighting at leadership level. The provincial leadership intervened through section 139(1)(b) of the Constitution and placed the municipality under administration during 2018 and 2019. However, the appointed administrator could not intervene and experienced significant pushback from the council, including several court cases. At times, the administrator was not even allowed access to the municipal premises. As a result, most of the audit issues were not responded to and supporting documents were not submitted. The resistance to the interventions demonstrated the lack of political will to change the status quo and improve accountability. This muddled accountability totally disrupted not only the audit process, but also the municipality's operations, as no decisions could be made or actioned.

The new political and administrative leadership will have to put in place a proper turnaround strategy. This must include a functional oversight structure (council), audit committee and municipal public accounts committee to ensure stability. The new council will have to avoid political instability and stabilise the position of the accounting officer, who must ensure that basic financial controls are implemented and monitored regularly. The poor performance culture at the municipality must be addressed by implementing robust performance management and corrective action through effecting consequences.

MATERIAL IRREGULARITIES

05

MATERIAL IRREGULARITIES

05

In this section, we look at the second year of implementation of our expanded mandate and provide insight on the material irregularity process and the material irregularities identified.

OUR EXPANDED MANDATE

The responsibilities and duties of municipal managers are well defined in the Municipal Finance Management Act, which are underpinned by the basic values and principles governing public administration as set out in our country's Constitution. It includes the need for high standards of professional ethics, accountability and transparency as well as the promotion of the efficient, economical and effective use of resources.

Our audits have for many years been highlighting a systemic failure in local government to establish the systems, processes and controls required to make the constitutional principles and the requirements of the Municipal Finance Management Act the norm. Not only are irregularities and the resultant losses, misuse and harm not prevented from happening, they are also not appropriately dealt with when they are identified.

Our mandate has always been to audit and report on these matters in order for corrections to be made by municipal managers. Our reporting to councils enables them to also play their oversight role effectively. Our mandate was expanded by the amendments to the Public Audit Act, which became effective on 1 April 2019, to go beyond audit and reporting in an effort to strengthen the accountability mechanisms.

Rather than a punitive measure, the amendments are intended to act as a complementary mechanism in the broader public sector accountability value chain by strengthening financial and performance management, which in turn will contribute to improved accountability.

Our expanded mandate does not change the role and responsibilities of the municipal manager, mayor or council.

We do not take over the role of the municipal manager who already has the responsibility to prevent irregularities and take action when they occur.

By identifying material irregularities, we support municipal managers by bringing to their attention the irregularities that could have a significant impact on finances, resources and service delivery while also empowering them to take the appropriate steps timeously in terms of legislation. This will lessen the adverse effect of such irregularities on municipalities, set the right tone for accountability, highlight the need for consequences, and encourage a behavioural change at the highest levels.

The amendments to the Public Audit Act and the introduction of the accompanying Material Irregularity Regulations have been shaped in a manner that supports the process of fair, transparent and legally sound administrative justice, by providing an opportunity to the municipal managers to take the actions required to deal with the material irregularities. We use our additional powers only where the municipal manager is not dealing appropriately with such irregularities. This process can be depicted graphically as follows:

If municipal manager does not appropriately deal with material irregularities, our expanded mandate allows us to:

Refer material irregularities to relevant public bodies for further investigation

Take binding remedial action for failure to implement our recommendations for material irregularities

Issue certificate of debt for failure to implement remedial action if financial loss was involved

The oversight and monitoring roles of the mayor and council remain unchanged by the Public Audit Act amendments. We report the material irregularities in the audit report, which also enables municipal public accounts committees to perform their oversight function – focusing on the most material matters affecting municipalities.

If municipal managers, supported by their political leadership, adhere to their legislated responsibilities and commit to take swift action when we notify them of a material irregularity, there will be no need for us to use our remedial and referral powers.

We are fully committed to the implementation of the enhanced powers given to our office, without fear, favour or prejudice. The success of our amended powers will become evident when a culture of responsiveness, consequences, good governance and accountability by municipal managers becomes the norm.

IMPLEMENTATION OF THE MATERIAL IRREGULARITY PROCESS

The amendments to the Public Audit Act introduced the concept of a material irregularity. But what does this mean?

What is a material irregularity?

MATERIAL IRREGULARITY

means any **non-compliance** with, or **contravention** of, legislation, **fraud, theft** or a **breach of a fiduciary duty** identified during an audit performed under the Public Audit Act that **resulted in or is likely to result in** a **material financial loss,** the **misuse or loss of a material public resource** or **substantial harm to a public sector institution or the general public**

As per the definition, there are two main gates through which a matter must pass for it to be classified as a material irregularity – there needs to be an **irregularity** (which is the non-compliance, fraud, theft or breach), and that irregularity must have an **impact** (being loss, misuse or harm).

Irregularities are identified during our normal audit process, as we audit compliance with key legislation as well as consider governance and control as part of the audit. Our audit processes can also identify possible fraud and theft, which we then report to management for investigation.

However, our audit process generally does not consider the impact of the irregularities identified (for example, if a financial loss is likely), as it is not required by the auditing standards. The requirements and processes to follow for a material irregularity as prescribed by the Public Audit Act and the Material Irregularity Regulations introduce additional steps in the audit process, new processes for referrals and remedial action, and the establishment of new structures and additional capacity.

The impact of the expanded mandate on our audit process and organisation as well as the profound implications thereof requires us to implement the changes in a careful, but progressive manner.

As agreed with the Standing Committee on the Auditor-General, we are phasing in the implementation of our expanded mandate. The phasing-in allows us to responsibly align the organisational resources with the demand placed on us by the Public Audit Act and to establish relationships with the public bodies to which we will be referring material irregularities. A phased-in approach also enables us to manage any risks associated with implementation, such as possible disputes and litigation, as well as the costs associated with implementation.

Our phased-in approach is guided by a step-by-step implementation of the material irregularity definition. In 2018-19, our focus was on the non-compliance with legislation scoped in for auditing as part of normal audits that resulted in, or is likely to result in, a material financial loss. In 2019-20, we expanded this to any non-compliance with, or contravention of, legislation that resulted in, or is likely to result in, a material financial loss. We also considered fraud, theft or a breach of a fiduciary duty if it constituted non-compliance with legislation. The prevalence of municipalities with disclaimed opinions at the conclusion of our 2019-20 audits compelled us to expand the definition further by considering the harm caused to a public sector institution (the municipality) by this persistent lack of proper documents and records.

We incrementally increased the number of auditees in local government where the material irregularity process was implemented from nine in 2018-19 to 57 in 2019-20. We focused on those auditees where we were most likely to have the greatest impact. The selected 57 auditees included the metros, most of the secondary cities (classified as such by the National Treasury based on their rapidly increasing population and economic growth) and some of the smaller municipalities and municipal entities that had high irregular expenditure in the past. The selected auditees are shown on the map that follows.

NORTH WEST

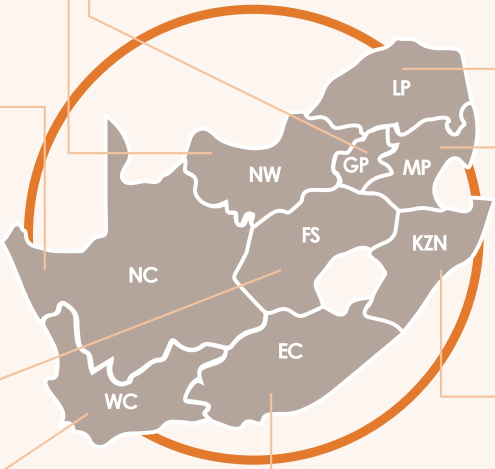
- Dr Ruth Segomotsi Mompati District
- Ngaka Modiri Molema District
- City of Matlosana
- JB Marks
- Madibeng
- Mahikeng
- Rustenburg

GAUTENG

- City of Ekurhuleni Metro
- City of Johannesburg Metro
- City of Tshwane Metro
- Brakpan Bus Company (municipal entity of City of Ekurhuleni Metro)

LIMPOPO

- Vhembe District
- Elias Motsoaledi
- Fetakgomo Tubatse
- Greater Letaba
- Mogalakwena
- Polokwane



NORTHERN CAPE

- Emthanjeni
- Ga-Segonyana
- Hantam
- Joe Morolong
- Nama Khoi
- Sol Plaatje

MPUMALANGA

- Bushbuckridge
- City of Mbombela
- Dr JS Moroka
- Emalahleni
- Govan Mbeki
- Steve Tshwete
- Thaba Chweu

FREE STATE

- Mangaung Metro
- Letsemeng
- Maluti-A-Phofung
- Matjhabeng
- Ngwathe
- Setsoto
- Tokologo

KWAZULU-NATAL

- eThekwini Metro
- uMkhanyakude District
- uMzinyathi District
- uThukela District
- Msunduzi
- Newcastle
- uMhlathuze

WESTERN CAPE

- City of Cape Town Metro
- Garden Route District
- Beaufort West
- Cederberg
- Drakenstein
- George
- Stellenbosch

EASTERN CAPE

- Buffalo City Metro
- Nelson Mandela Bay Metro
- Alfred Nzo District
- Chris Hani District
- OR Tambo District
- King Sabata Dalindyebo

These auditees covered 42% of the expenditure budget, 54% of the irregular expenditure incurred, and 68% of the irregular expenditure balance. We specifically looked at irregular expenditure as an indicator of the level of non-compliance with legislation at an auditee and the potential for material financial losses. This does not mean that irregular expenditure and material irregularities are the same thing, as explained later on in this section.

IDENTIFYING AND REPORTING ON MATERIAL IRREGULARITIES

Our annual regularity audit process has distinct phases, including planning and execution. As the legislated reporting date comes closer, we finalise and conclude on our audits, allowing for the audit report to be signed on time. Thereafter we interact with oversight committees and undertake engagements on the overall audit outcomes and the general report.

The material irregularity process is integrated into the audit process, but is not bound to the audit cycle in the same way as our regularity audits. It does not have a distinct start and stop date, which is quite a different approach than what our auditees are used to. We can identify matters that can potentially be material irregularities at any time of the audit – even right before the audit report is signed. We then do not leave it to the next annual audit, but rather follow our structured material irregularity route to confirm whether the matter meets the definition and start with the process so as not to delay the accountability process.

What did we do to identify material irregularities?

The material irregularity process was applied from 1 April 2019 at the selected auditees, when the amendments became effective. The auditor-general used the discretion allowed by the Public Audit Act to direct that the audit teams only consider material irregularities where it continued to have a financial impact from the effective date. This means that we did not consider non-compliance that took place in prior years except where it continued to financially affect the auditee; for example, if payments were still being made on a contract that had been irregularly awarded in prior years, or if a debt owed to the auditee was still in its books.

We also made sure that we applied the definition of a material irregularity correctly by only reporting it if the non-compliance directly resulted in a financial loss or was likely to result in a financial loss. We considered whether a financial loss was material through considering its value, nature and impact. The value of the financial loss had often already been determined by the auditee and disclosed in the financial statements, such as fruitless and wasteful expenditure (what we refer to as a known financial loss). But for some material irregularities, we estimated the potential financial loss to consider if it was material (what we refer to as an estimated financial loss).

What did we do when we identified a material irregularity?

When we identified a material irregularity, the municipal manager was notified without delay. We gave them 20 working days to respond to the notification by giving us a written submission and evidence on what they have done to address the material irregularity and what their further planned actions are.

We assessed the responses provided and concluded whether their actions (taken or planned) and its outcomes were appropriate in line with their legal obligations. If we found this to be the case, we gave the municipal manager space to implement the further planned actions. We then follow up on the progress made with resolving the material irregularity in the next audit cycle.

Legal obligations of municipal manager to address an irregularity

If a municipal manager is made aware of an irregularity (non-compliance, fraud, theft or a breach of fiduciary duty), the Municipal Finance Management Act and its regulations typically prescribe the following steps to be taken:

1. **Perform a preliminary investigation to determine the facts and collect information on what caused the transgression, who is responsible, and whether a financial loss was suffered (or will be).**

If applicable

↓

2. **Prevent any losses or further losses.**
3. **Institute a formal investigation if there are indications of fraud, corruption or other criminal conduct; if confirmed, take further action (e.g. report matter to the police).**
4. **Recover any financial losses from an external party.**
5. **Take steps against the responsible official(s) (which can include a financial misconduct investigation).**
6. **Recover any financial losses from the responsible official(s).**

The policies and procedures of a municipality typically describe how these steps should be taken and the timing thereof.

The same steps should be taken if a municipal manager is notified of a material irregularity.

If we conclude that it was not appropriate, we include recommendations in the audit report on what the municipal manager should do to address the material irregularity. We also include a deadline by when these recommendations should be implemented.

If it requires further investigation, we also refer the material irregularity to a public body.

What happens with the identified material irregularities?

A material irregularity is only fully resolved if (1) the loss (or further losses) is prevented and/or any losses incurred have been recovered or all possible steps have been taken to recover the losses; and (2) appropriate steps have been taken against the person or party responsible for the loss.

The material irregularities and the progress made in resolving them will be reported in the audit report of the auditee and in general reports until they have been fully resolved to enable accountability and oversight. When an audit report is signed, we report based on the status of the material irregularities that are confirmed at that date. What we typically include are the following:

- New material irregularities identified and the actions the municipal manager is taking to address them – or we include the recommendations or information on referral (as applicable).
- Whether there are other material irregularities in process (if we have not concluded the notification and response process).
- Progress made in resolving material irregularities reported in the previous audit report.

The responsibilities for the further steps to be taken by the municipal manager, mayor, council and public bodies to resolve an identified material irregularity are detailed below.

	Municipal manager (MM) and Auditor-General of South Africa (AGSA)	Mayor and council
MM is dealing with material irregularity	**MM** implements committed actions to address material irregularity and improves controls to prevent recurrence **AGSA** follows up in next audit if actions were implemented and if outcomes were reasonable – if not, can result in referral or recommendation in audit report	**Mayor** monitors progress and supports MM in addressing material irregularity and improving controls **Council** monitors progress and calls MM to account for actions taken and outcomes
Material irregularity is referred to public body	**MM** cooperates with public body and implements any remedial actions/ recommendations made and improves controls to prevent recurrence **AGSA** provides information on material irregularity to public body, monitors progress with investigation, and follows up in audits the implementation of any remedial actions/recommendations	**Mayor** supports public body's investigation and MM in improving controls; if responsible for public body, monitors progress with investigation **Council** monitors progress with investigation and calls public body to account for undue delays in investigation
Recommendation included in audit report	**MM** implements recommendations by date stipulated in audit report and improves controls to prevent recurrence **AGSA** follows up by stipulated date if recommendations were implemented and if outcomes were reasonable; issues remedial action	**Mayor** monitors progress and supports MM in implementing recommendations and improving controls **Council** monitors progress and calls MM to account for actions taken and outcomes

What did we do to follow up on the progress?

The 2019-20 year was the first time we followed up and reported on the progress with the material irregularities reported in the previous year.

We wrote to the municipal managers to enquire on the progress and request evidence on the actions they had planned to take. We also asked what their further planned actions were.

We assessed the responses provided and concluded whether their actions (taken or planned) and the outcome of these were appropriate in line with their legal obligations. If we found these to be appropriate, we gave the municipal manager space to implement the further planned actions, with an undertaking to follow up on the progress with resolving the material irregularity in the next audit cycle. If we concluded that the actions were not appropriate, we included recommendations in the audit report on what the municipal manager should do to address the material irregularity. We also included a deadline by when these recommendations should be implemented.

If we included recommendations in the audit report in 2018-19, we followed a similar approach to obtain feedback and evidence. As recommendations are to be implemented by a certain date, we requested written submissions from the municipal manager by that date, including reasons for recommendations not having been implemented. If the recommendations had not been implemented by the stipulated date, we went through a rigorous process before concluding whether the municipal manager should be allowed more time or if remedial action should be implemented.

It is important to clarify that the municipal managers against whom we can take remedial action and ultimately issue a certificate of debt are not the persons or parties who had lost the money or who had been involved in the irregularity – they are those who did not take action to recover the money, stop further losses and act against the officials involved. Hence we must provide them with the time to take the required action. We will only activate our new powers when such action is not taken or not taken timeously, or if the outcome of the action is not appropriate.

We appreciate our stakeholders' frustration regarding the long time it takes from identifying a material irregularity to issuing a certificate of debt. But we have to be fair, reasonable and adhere to the principles of administrative justice, by providing municipal managers sufficient time to take action, implement recommendations and remedial steps as well as state their case for not taking the required action should that be the case.

The timeline below demonstrates the extent and timing of this process by using an example of a material irregularity identified in April 2021. Please note that this is a 'best case scenario' as there are often delays in the process – some within the control of the municipal manager, and some outside the control of either the municipal manager or ourselves.

1. **April 2021**
Identify material irregularity (MI) during audit

2. **May 2021**
Notify municipal manager of MI – provide 20 working days to respond on actions taken and planned

3. **June 2021**
Conclude based on municipal manager response if appropriate action is taken or planned

4. **July 2021**
If actions were not appropriate, include recommendations in audit report on how MI should be addressed by specific date (e.g. within 6 months)

5. **February 2022**
Follow up whether recommendations have been implemented; if not, issue remedial action to municipal manager that must be implemented by specific date (e.g. within 3 months)

6. **July 2022**
Follow up whether remedial actions have been implemented; if not, issue notice of intention to issue certificate of debt to municipal manager

Request written submission on reasons not to issue certificate of debt within 20 working days

7. **August 2022**
Conclude based on written submission whether certificate of debt process should continue

If it continues, request municipal manager to give oral representation at MI advisory committee on reasons not to issue certificate of debt

8. **September 2022**
MI advisory committee meets to hear oral representation and recommend course of action to auditor-general

9. **October 2022**
Auditor-general issues certificate of debt to municipal manager

MATERIAL IRREGULARITIES IDENTIFIED

By 11 June 2021, we had issued notifications for 96 material irregularities, of which 75 related to non-compliance with legislation that resulted in a material financial loss. We estimate the financial loss associated with these material irregularities to be R2,04 billion.

Nature of identified material irregularities (MIs)

Disclaimers – 21 MIs
Full and proper records not kept as evidenced by **repeat disclaimed opinions** – resulting in substantial harm to municipality (lack of service delivery and/or vulnerable financial position)

Procurement and payments	
Non-compliance in procurement processes resulting in **overpricing of goods and services procured** **1 MI – R2,5 million** estimated loss	Payment for **goods or services not received** or **invalid salary payments** **18 MIs – R285,9 million** estimated loss

Interest and penalties	
Eskom, water boards, lenders and suppliers **not paid on time** resulting in interest **23 MIs – R979,3 million** estimated loss	Payroll and value-added tax returns **not paid on time** or incorrectly calculated resulting in South African Revenue Service interest and penalties **11 MIs – R54,7 million** estimated loss

Revenue management	
Revenue **not billed** **8 MIs – R182,3 million** estimated loss	Debt **not recovered** **2 MIs – R149,4 million** estimated loss

Investments and assets	
Loss of **investments** **3 MIs – R264,9 million** estimated loss	**Assets not safeguarded** resulting in loss **9 MIs – R116,6 million** estimated loss

Material irregularities that resulted in material financial losses emerged in four key areas: procurement and payments, interest and penalties, revenue management, and investments and assets. We have highlighted all of these as areas of vulnerability for a number of years, including in this year's audit outcomes.

These are not complex matters, but some of the basic disciplines and processes that should be in place at auditees, such as procure at the best price, pay only for what was received, make payments on time, recover revenue owed to the state, and safeguard assets and investments.

At the conclusion of the 2019-20 audit cycle, the high number of municipalities that received disclaimed opinions (as detailed in section 4) compelled us to consider the impact of full and proper records not being kept and the lack of credible financial reporting. We concluded that these lapses in accountability caused substantial harm to the majority of these municipalities, as their financial position was so poor that they disclosed in their financial statements a material uncertainty regarding their ability to continue operations. Some of the municipalities were not able to deliver services as required and the Department of Cooperative Governance determined them to be dysfunctional. By 11 June 2021, we had notified the municipal managers of 21 municipalities of this material irregularity. We did not issue the notifications only to disclaimed municipalities if they were part of the 57 auditees selected for implementation, but also to an additional 15 municipalities. We will implement the full material irregularity process at these municipalities from 2020-21.

As reflected below, the number of material irregularities increased significantly from 2018-19 as a result of the increase in auditees selected, the broadening of the definition for implementation, and the continuing refinement of our practices and processes as we learn from the implementation process.

9 auditees
2018-19
6 MIs

57 auditees
2019-20
81 MIs
(+15 MIs to auditees in addition to the originally selected 57 auditees)

Of the 96 material irregularities, 10 were reported in detail in the audit reports of the applicable auditees – six in 2018-19 and four in 2019-20 as the municipal manager response and our assessment of the response had been finalised by the time of audit report signing. We originally reported seven in 2018-19, but closed one based on information subsequently provided through an investigation instituted by the municipal manager. As it is no longer an active material irregularity, we exclude it from our discussion in the rest of this section.

The remaining 86 material irregularities have not yet been reported in detail in the audit reports of the applicable auditees as the response to the notification and assessment process had not been completed by the time we signed the audit reports.

As explained earlier, the material irregularity process is a continuous process and not bound by the audit cycle, which means that it continues even after an audit report has been signed. We will include the details of these material irregularities and the actions taken to resolve them in our 2020-21 audit and general reports.

By 11 June 2021, there were also a high number of matters being considered as potential material irregularities. These include matters identified during our audit of covid-19 expenditure and auditees with disclaimed opinions where the notifications had not yet been issued. These material irregularities, if confirmed and once the municipal managers have been notified, will also be reported in our 2020-21 reports.

STATUS OF REPORTED MATERIAL IRREGULARITIES

STATUS OF 10 MATERIAL IRREGULARITIES REPORTED IN AUDIT REPORT ISSUED BY 11 JUNE 2021

6 **Implementation of appropriate actions by municipal manager in process**

3 **Lack of progress by municipal manager resulting in recommendations issued**

1 **Referred for investigation to a public body**

The six material irregularities where appropriate actions are being taken include three reported in 2018-19, which are being dealt with diligently by the municipal managers and are in various stages of resolution.

We would have wanted to see all of these material irregularities having been resolved but progress overall has been affected by the lockdown measures in response to the covid-19 pandemic as well as instability at municipal manager level.

We included recommendations in the audit report of Ngaka Modiri Molema (North West) for the three material irregularities we reported in 2018-19, as the actions the municipal manager had committed to were not implemented. To date we have not issued remedial actions as municipal managers have been playing their part. However, if the municipal manager of Ngaka Modiri Molema does not implement the recommendations in the audit report by the date stipulated, it could result in remedial action. In general, the municipal managers in North West were not very responsive to the material irregularity process – some notifications were not even responded to.

We are in the process of referring a material irregularity identified at Matjhabeng (Free State) to a public body for investigation, as the municipal manager did not take or plan appropriate actions in response to being notified of the material irregularity.

We now discuss the status of the 10 reported material irregularities in more detail.

DETAIL OF REPORTED MATERIAL IRREGULARITIES

IMPLEMENTATION OF APPROPRIATE ACTIONS IN PROCESS

Auditee and year reported	Description	Actions being taken by audit report date
Mogalakwena (LP) **2018-19**	**Payments** to contractor **for construction work not done** at Moshate stadium. **Financial loss:** R13 million **Notified:** 14 December 2019	Investigation completed in August 2020 confirmed the financial loss and recommended that officials responsible be charged with misconduct. Disciplinary proceedings are underway and attorneys were appointed in February 2021 to recover money from contractor.
City of Tshwane Metro (GP) **2018-19**	**Assets stolen and vandalised** at the Annlin reservoir project in January 2018, as not all reasonable steps were taken to safeguard the assets. **Financial loss:** R5,5 million **Notified:** 11 December 2019	An investigation by the internal forensic division was completed by June 2020. The investigation did not cover adherence to the asset management policy, the verification and quantification of the financial loss or whether there was any fraud, corruption or misconduct related to the material irregularity. The municipal manager committed to conclude the investigation covering the entire scope by 1 July 2021, and will take action against responsible officials and steps to recover financial loss based on the outcome. Steps were taken to improve security at the site, but the appointment of a security company was delayed by the covid-19 lockdown measures. The new date committed to is 30 June 2021. The matter was reported to the South African Police Service for investigation on 11 January 2018 but has not yet been concluded.

Auditee and year reported	Description	Actions being taken by audit report date
City of Tshwane Metro (GP) **2018-19**	**Assets stolen and vandalised** at the Baviaanspoort wastewater treatment works in February 2016, as not all reasonable steps were taken to safeguard the assets. **Financial loss:** R3,9 million **Notified:** 17 December 2019	The matter was reported to the South African Police Service – arrests were made and the perpetrators sentenced. An investigation by the internal forensic division was completed by June 2020. The investigation did not cover adherence to the asset management policy, the verification and quantification of the financial loss or whether there was any fraud, corruption or misconduct related to the material irregularity. The municipal manager committed to conclude the investigation covering the entire scope by 1 July 2021, and will take action against responsible officials and steps to recover financial loss based on the outcome. Steps were taken to improve security at the site, but the appointment of a security company was delayed by the covid-19 lockdown measures. The new date committed to is 30 June 2021.
Nelson Mandela Bay Metro (EC) **2019-20**	**Interest not charged** in 2018-19 on debtors in arrears who had entered into long-term arrangement agreements with the municipality. **Financial loss:** To be quantified by municipal manager **Notified:** 9 December 2019	Preliminary investigation completed in February 2020 by the billing coordination division in consultation with debtor management division. Outcome of investigation indicated that the material irregularity is the result of a system deficiency. Accounting system was re-programmed in February 2020 to make raising interest every month an inherent part of the system. Municipal manager plans to submit proposal to budget and treasury standing committee in June 2021 and to council for consideration and approval that interest on arrangements not be raised retrospectively for the period when the accounting system did not raise such interest.
Nelson Mandela Bay Metro (EC) **2019-20** **(2 material irregularities)**	**Payments** in 2018-19 to two suppliers **for provision of storm-water drain cleaning services that were not received.** **Financial loss:** To be quantified by municipal manager **Notified:** 13 December 2019	Investigation into matter by provincial Hawks unit commenced in January 2020. Municipal manager plans to recover losses incurred and effect consequences against responsible official(s).

RECOMMENDATIONS IN AUDIT REPORT AND REFERRALS TO PUBLIC BODY FOR INVESTIGATION

Auditee and year reported	Description	Recommendation/referral as reported in audit report
Ngaka Modiri Molema (NW) **2018-19**	**Failure by municipality to monitor contract for construction work** to municipal office building and gate house **resulted in contract extension** that included items already paid for as part of original contract. These costs could have been avoided. **Financial loss:** To be quantified by municipal manager **Notified:** 14 November 2019	The municipal manager failed to implement the planned actions. Recommendations to be implemented by 1 October 2021: • The financial loss should be quantified. • Any person liable for the loss should be identified and appropriate action should commence to recover the financial loss. • The non-compliance should be investigated to determine if any official might have committed an act of financial misconduct or an offence in terms of chapter 15 of the Municipal Finance Management Act. • Disciplinary or, when appropriate, criminal proceedings should commence against any official who has allegedly committed an act of financial misconduct or an offence, as required by section 62(1)(e) of the Municipal Finance Management Act and in the manner prescribed by the Municipal Regulations on Financial Misconduct Procedures and Criminal Proceedings. • If it appears that the municipality suffered the financial loss through fraud, this should be reported to the South African Police Service, as required by section 32(6)(b) of the Municipal Finance Management Act.

<table>
<tr><th>Auditee and year reported</th><th>Description</th><th>Recommendation/referral as reported in audit report</th></tr>
<tr><td>Ngaka Modiri Molema (NW)

2018-19</td><td>Overpayment in 2018-19 to supplier for water-tankering services to communities as a result of municipality not having an effective system of expenditure control.

Financial loss: To be quantified by municipal manager

Notified: 28 November 2019</td><td>The municipal manager failed to implement the planned actions.

Recommendations to be implemented by 18 November 2021:
The financial loss in the form of overpayments should be quantified and appropriate action should commence to recover the loss from the supplier.
A system of expenditure control should be implemented, as required by section 65(2)(a) of the Municipal Finance Management Act, for the provision of water-tankering services, to prevent over-invoicing of kilometres and hours.
The non-compliance should be investigated to determine if any official might have committed an act of financial misconduct or an offence in terms of chapter 15 of the Municipal Finance Management Act.
Disciplinary or, when appropriate, criminal proceedings should commence against any official who has allegedly committed an act of financial misconduct or an offence, as required by section 62(1)(e) of the Municipal Finance Management Act and in the manner prescribed by the Municipal Regulations on Financial Misconduct Procedures and Criminal Proceedings.
If it appears that the municipality suffered the financial loss through fraud, this should be reported to the South African Police Service, as required by section 32(6)(b) of the Municipal Finance Management Act.</td></tr>
</table>

Auditee and year reported	Description	Recommendation/referral as reported in audit report
Ngaka Modiri Molema (NW) **2018-19**	**Loss of assets** due to lack of internal control system to safeguard assets. **Financial loss:** To be quantified by municipal manager **Notified:** 9 December 2019	The municipal manager failed to implement the planned actions. Recommendations to be implemented by 1 October 2021: • The asset verification and investigation process should be completed and the financial loss quantified. • Any person liable for the loss should be identified and appropriate action should commence to recover the financial loss. • Reasonable steps should be taken to safeguard these municipal assets from any further losses, as required by section 63(1) of the Municipal Finance Management Act. • The non-compliance should be investigated to determine if any official might have committed an act of financial misconduct or an offence in terms of chapter 15 of the Municipal Finance Management Act. • Disciplinary or, when appropriate, criminal proceedings should commence against any official who has allegedly committed an act of financial misconduct or an offence, as required by section 62(1)(e) of the Municipal Finance Management Act and in the manner prescribed by the Municipal Regulations on Financial Misconduct Procedures and Criminal Proceedings. • If it appears that the municipality suffered the financial loss through fraud, this should be reported to the South African Police Service, as required by section 32(6)(b) of the Municipal Finance Management Act.
Matjhabeng (FS) **2019-20**	**Payments made for** construction of **attenuation** (flood-protection) **dam** on Nyakallong storm-water system **not constructed** resulting in overpayments on project. **Financial loss:** To be determined through public body investigations **Notified:** 5 May 2020	Municipal manager could not provide sufficient and appropriate evidence of actions taken in response to being notified of the material irregularity. Actions taken were also considered to be inadequate. As a result, the material irregularity is being referred to a public body for investigation.

MATERIAL IRREGULARITIES VERSUS IRREGULAR EXPENDITURE

Now that we have looked at the material irregularities in detail, let's address a question that we frequently get asked on the correlation between irregular expenditure and material irregularities. Our stakeholders often expect that all irregular expenditure will also be material irregularities. This is not the case, however, as explained below by looking at how the definition and application of irregular expenditure differ from those of material irregularities.

How irregular expenditure (IE) is different from material irregularities (MIs)

Definition

IE: Expenditure incurred in contravention of, or that is not in accordance with, a requirement of any applicable legislation

MI: Any non-compliance with, or contravention of, legislation, fraud, theft or a breach of a fiduciary duty identified during an audit performed under the Public Audit Act that resulted in or is likely to result in a material financial loss, the misuse or loss of a material public resource or substantial harm to a public sector institution or the general public

Difference: irregularity

IE: Irregularity is only **non-compliance with legislation when incurring expenditure**

MI: Irregularity is **any non-compliance (not limited to expenditure)** as well as **fraud, theft or breach of fiduciary duty**

Difference: impact

Impact is not specified, as MFMA requires municipal manager and council to determine impact

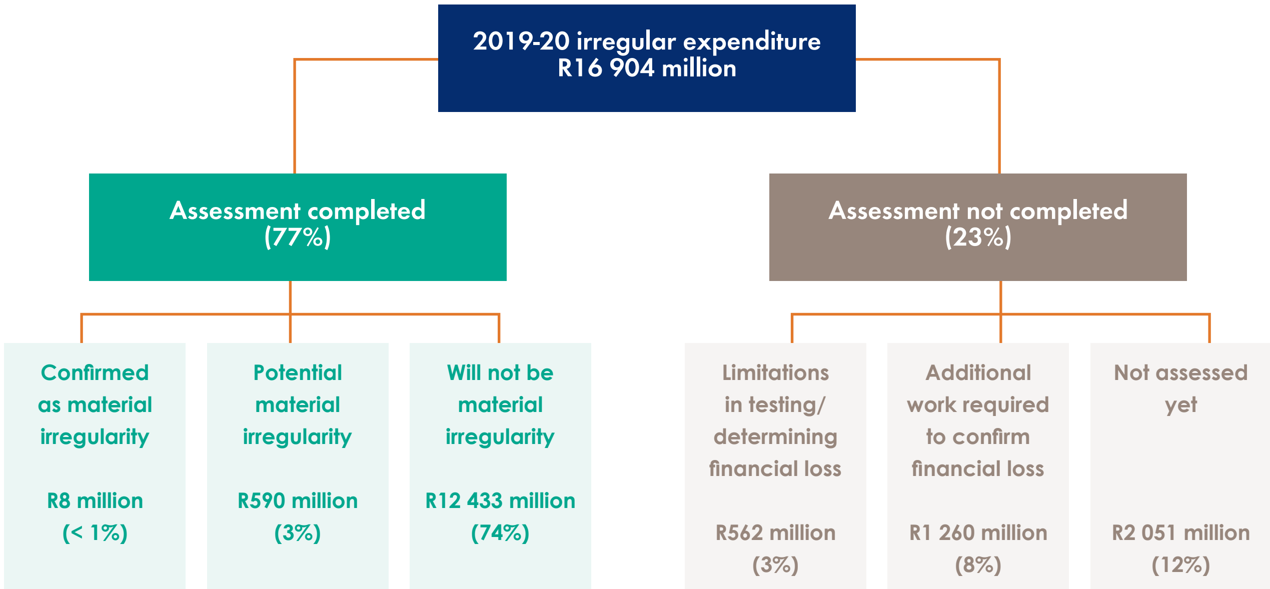
There can be **irregular expenditure that did not result in any financial losses,** misuse or harm

Difference: value

IE: Value is **expenditure to date**

MI: Does not necessarily have a value, but if impact is financial loss, **value we report is estimated financial loss**

One of the sources of potential material irregularities we use, is the irregular expenditure disclosure in the financial statements of auditees and the register of instances they keep. Below we show how we assessed the R16 904 million in irregular expenditure incurred in 2019-20 as disclosed by the selected auditees.



Some assessment work (23% of the value) still needs to be completed due to various reasons such as limitations in determining the loss or additional work that must still be done.

Based on the assessments completed, however, 74% of the irregular expenditure will not translate into material irregularities. There were two main reasons for this:

1. It did not meet the definition of a material irregularity that we are currently applying, as we confirmed that the non-compliance did not result in a financial loss (64%). There was also a portion (8%) that was non-compliance from a prior year that did not continue to have an impact.
2. The value of some of the non-compliance was very low (2%) – these cases typically related to quotations. It is unlikely that such non-compliance will result in financial loss that will be considered material.

CONCLUSION

We have already seen great value from the implementation of the material irregularity process. Based on our experiences to date, the following are our key observations:

- Most **municipal managers are taking appropriate action** to address the material irregularities identified (based on the 60% of material irregularities reported in the audit reports where appropriate action is being implemented, as described earlier under *Detail of reported material irregularities*). We observed that municipalities knew about the irregularities and losses – and even disclosed these as irregular expenditure, fruitless and wasteful expenditure, or impairments. However, little action had been taken before we officially notified the municipal managers of the material irregularities.
- In following up the progress with the material irregularities we reported in 2018-19, we found that the municipal managers of Mogalakwena and City of Tshwane Metro were actively working on resolving the material irregularities, although there were some delays as a result of the impact of covid-19. We were also encouraged by the positive responses received from most municipal managers when we notified them of material irregularities, with the exception of those in North West. It signals

a **behavioural change towards responding in a decisive and timely manner to our findings.** At some auditees, matters we have been reporting for a number of years are finally receiving attention – the non-billing of interest at Nelson Mandela Bay Metro is a good example in this regard.

- The timely resolution of material irregularities is **dependent on investigations** that are thorough but also speedily completed. Municipal managers can monitor the progress made on the investigations they commissioned, and can ensure that the completion is not unduly delayed. However, when a material irregularity is referred to another public sector institution, the municipal manager has little influence. The executive authorities and committees in Parliament and legislatures will need to monitor progress on such investigations and hold the institutions to which they were referred accountable.
- Most of the material irregularities identified were money lost as a result of late payments to Eskom, water boards, the South African Revenue Service, lenders and suppliers, resulting in interest being charged. These material irregularities **are not complex accounting or procurement issues and could have been prevented through basic controls.** The material irregularities resulting from supply chain management non-compliance were also mostly not complex or ambiguous and could have been prevented – or at least detected and dealt with – before they resulted in such material financial losses for the auditees. None of the material irregularities were as a result of human error, but were rather due to poor processes and judgement. There were most definitely indicators of fraud in some of these material irregularities, which have been (or will still be) uncovered by the investigations and referrals.

Preventing material irregularities is more effective than having to deal with the consequences thereof – money is lost, costly investigations have to be instituted and officials are subjected to the discomfort and anxieties associated with these processes, which often take a number of years to be concluded.

As we continue on our journey to implement the material irregularity process, we hope to see a definite move by municipal leadership and oversight towards the prevention of material irregularities to the benefit of the financial management, reputation and service delivery of our auditees – and ultimately the lives of the citizens they serve. As expressed throughout this report, the change needed in local government must be driven by an ethical and accountable leadership.

PROVINCIAL OVERVIEWS

06

PROVINCIAL OVERVIEWS

06

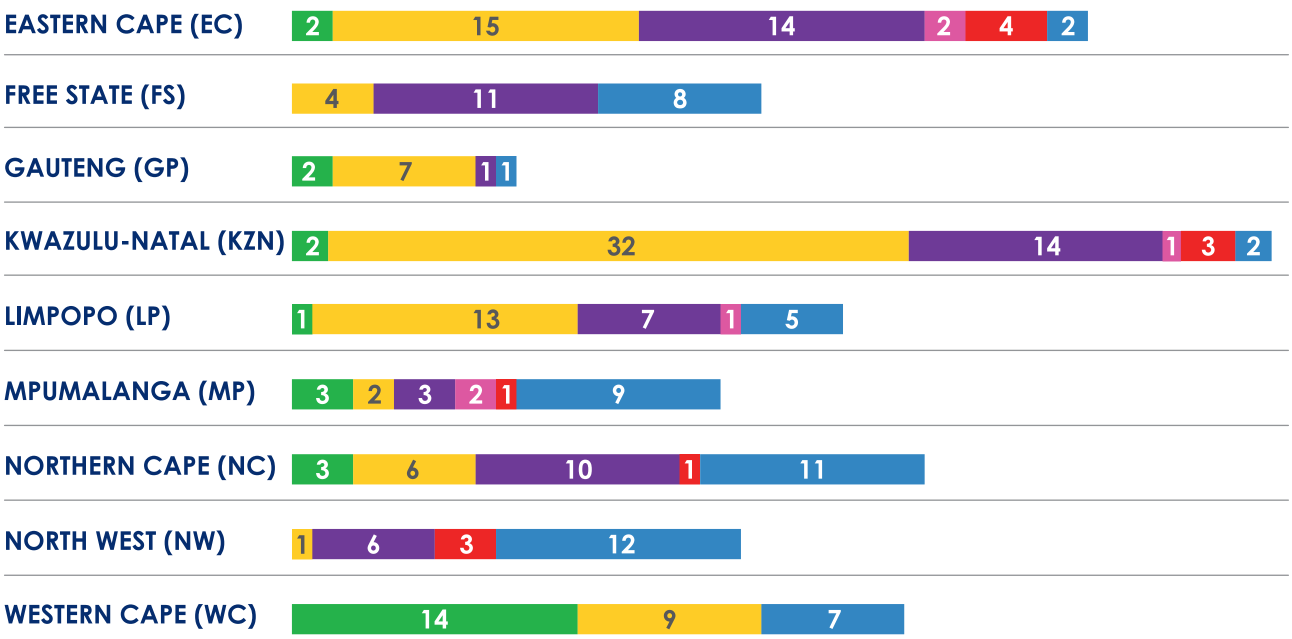
In this section, we provide an overview of the results and reflections per province with a focus on the current state of financial health as well as the financial and performance management of municipalities.

We include the following:

- Overall audit outcomes per province
- Status of outstanding audits and outcomes of those audits finalised after the cut-off date of 23 April 2021 up to 4 June 2021
- High-level summary of each province's performance, including audit outcomes per district

Every province has a unique set of circumstances and diverse solutions to their problems, but the need for leadership – also at provincial level – to step up and turn the tide, remains transversal.

AUDIT OUTCOMES PER PROVINCE



OUTSTANDING AUDITS

Cut-off date for inclusion of the audit outcomes in this report is 23 April 2021

REASONS FOR 25 OUTSTANDING AUDITS

Financial statements submitted late - 9 (36%)

Auditee delays - 10 (40%)

Financial statements outstanding - 5 (20%)

Audit delays - 1 (4%)

RESULTS OF 32 AUDITS SUBSEQUENTLY FINALISED AS AT 4 JUNE 2021

AUDITS SUBSEQUENTLY FINALISED AS AT 4 JUNE 2021	MOVEMENT	2019-20 AUDIT OUTCOMES		
		Audit opinion	Performance report	Compliance with legislation
EASTERN CAPE				
Great Kei	Improved	Qualified with findings	Findings	
FREE STATE				
Mangaung Metro	Improved	Unqualified with findings	Findings	Findings
Mantsopa	Unchanged	Qualified with findings		Findings
GAUTENG				
Emfuleni	Unchanged	Qualified with findings	Findings	Findings
KWAZULU-NATAL				
Ugu District	Unchanged	Qualified with findings	Findings	Findings
Nquthu	Regressed	Disclaimed with findings	Findings	Findings
LIMPOPO				
Mopani District	Unchanged	Qualified with findings	Findings	Findings
Greater Tzaneen	Improved	Unqualified with findings	Findings	Findings
Lepelle Nkumpi	Improved	Unqualified with findings		Findings
MPUMALANGA				
Gert Sibande District	Regressed	Unqualified with findings		Findings
Dipaleseng	Unchanged	Disclaimed with findings	Findings	Findings
Emalahleni	Unchanged	Qualified with findings	Findings	Findings
Lekwa	Unchanged	Disclaimed with findings	Findings	Findings
Nkomazi	Unchanged	Unqualified with findings	Findings	Findings
Dr Pixley Ka Isaka Seme	Unchanged	Disclaimed with findings	Findings	Findings
City of Mbombela	Improved	Unqualified with findings		Findings

▲ Improved ▶ Unchanged ▼ Regressed

Unqualified with no findings · Unqualified with findings · Qualified with findings · Adverse with findings · Disclaimed with findings · Outstanding audits · Findings

AUDITS SUBSEQUENTLY FINALISED AS AT 4 JUNE 2021	MOVEMENT	2019-20 AUDIT OUTCOMES		
		Audit opinion	Performance report	Compliance with legislation
NORTHERN CAPE				
Magareng	Unchanged	Qualified with findings	Findings	Findings
Richtersveld	Unchanged	Qualified with findings	Findings	Findings
Ubuntu	Unchanged	Qualified with findings	Findings	Findings
Umsobomvu	Unchanged	Qualified with findings		Findings
Kgatelopele	Improved	Qualified with findings	Findings	Findings
!Kheis	Unchanged	Disclaimed with findings	Findings	Findings
NORTH WEST				
Ngaka Modiri Molema District	Unchanged	Adverse with findings	Findings	Findings
Matlosana	Unchanged	Qualified with findings		Findings
Lekwa Teemane	Unchanged	Disclaimed with findings	Findings	Findings
Madibeng	Unchanged	Disclaimed with findings	Findings	Findings
Mamusa	Unchanged	Disclaimed with findings	Findings	Findings
Ramotshere Moiloa	Unchanged	Disclaimed with findings	Findings	Findings
WESTERN CAPE				
Beaufort West	Regressed	Disclaimed with findings	Findings	Findings
Kannaland	Regressed	Qualified with findings	Findings	Findings
Laingsburg	Unchanged	Qualified with findings		Findings
Matzikama	Unchanged	Unqualified with findings		Findings

Improved Unchanged Regressed

Unqualified with no findings | Unqualified with findings | Qualified with findings | Adverse with findings | Disclaimed with findings | Outstanding audits | Findings

6.1 EASTERN CAPE

PERFORMANCE SNAPSHOT

The snapshot shows the audit outcomes of 37 municipalities in the province. With the exception of unauthorised, irregular and fruitless and wasteful expenditure, the outcomes of the outstanding audits are not included in the snapshot.

Overall audit outcomes

2 | 15 | 14 | 2 | 4 | 2

MOVEMENT

FROM 2018-19: ▲ 7 ▼ 1

OVER 4 YEARS: ▲ 6 ▼ 12

CHRIS HANI

3 | 2 | 1 | 1

- Chris Hani DM ▶
- Emalahleni LM ▶
- Engcobo LM ▶
- Enoch Mgijima LM ▲
- Intsika Yethu LM ▶
- Inxuba Yethemba LM ▶
- Sakhisizwe LM ▼

JOE GQABI

2 | 1 | 1

- Joe Gqabi DM
- Elundini LM ▲
- Senqu LM ▶
- Walter Sisulu LM ▲

ALFRED NZO

4 | 1

- Alfred Nzo DM ▶
- Matatiele LM ▶
- Winnie Madikizela-Mandela (Mbizana) LM ▶
- Ntabankulu LM ▶
- Umzimvubu LM ▶

AMATHOLE

3 | 2 | 1 | 1

- Amathole DM ▲
- Amahlati LM ▲
- Great Kei LM
- Mbhashe LM ▶
- Mnquma LM ▲
- Ngqushwa LM ▶
- Raymond Mhlaba LM ▶

SARAH BAARTMAN

4 | 2 | 2

- Sarah Baartman DM ▶
- Blue Crane Route LM ▶
- Dr Beyers Naudé LM ▲
- Kou Kamma LM ▶
- Kouga LM ▶
- Makana LM ▶
- Ndlambe LM ▶
- Sundays River Valley LM ▶

NELSON MANDELA METRO ▶

1

BUFFALO CITY METRO ▶

1

OR TAMBO

1 | 4 | 1

- OR Tambo DM ▶
- Ingquza Hill LM ▶
- King Sabata Dalindyebo LM ▶
- Mhlontlo LM ▶
- Nyandeni LM ▶
- Port St. Johns LM ▶

Metropolitan municipality | District | DM District municipality | LM Local municipality | ▲ Improved | ▶ Unchanged | ▼ Regressed

Unqualified with no findings | Unqualified with findings | Qualified with findings | Adverse with findings | Disclaimed with findings | Outstanding audits

Financially unqualified financial statements

46% (17) 2018-19: 41% (15)

Financial statements submitted without material misstatements 16% (6)

No material findings on performance report

35% (13) 2018-19: 16% (6)

Reported achievement reliable 51% (19)

No material findings on compliance with legislation

5% (2) 2018-19: 3% (1)

No findings on compliance with supply chain management legislation 14% (5)

Material irregularities (MIs)

Notified by 11 June 2021

6 MIs with estimated financial loss of **R188,7 m** at **4 municipalities** and likely substantial harm to public sector institution at **3 municipalities** with repeat disclaimers

NATURE

Payment for goods not received
Interest due to late payment
Not billing for services rendered
Full and proper records not kept (repeat disclaimer)

Unauthorised & fruitless and wasteful expenditure

Unauthorised expenditure **R1 752 m**

Fruitless and wasteful expenditure **R241 m**

Irregular expenditure

R3 550 m
2018-19: **R6 684 m**

Closing balance
R27 747 m
2018-19: **R28 110 m**

TOP THREE CONTRIBUTORS	
Nelson Mandela Bay Metro	**R1 372 m**
OR Tambo District	**R696 m**
Buffalo City Metro	**R302 m**

Use of financial reporting consultants

R132 m – 30 municipalities
2018-19: **R111 m – 33 MUNICIPALITIES**

Recurring use of consultants at 76% of municipalities

TOP THREE SERVICES	
Financial statements review/preparation	**R46,6 m**
Tax services	**R45,2 m**
Asset management	**R30,9 m**

Financial health indicators

Going concern uncertainty	**27% (10)**
Deficit	**R1 020 (12)**
Average creditor-payment period	**172 days**
Eskom and water boards' debt in arrears	**R1 037 m (11)**
Creditors > cash available at year-end	**45% (14)**
Average municipal debt not recoverable	**70% (31)**
Average debt-recovery period	**154 days**

PROVINCIAL OVERVIEW

Each province has a unique story...

Improvement in outcomes, but this might not be sustainable due to poor control environments

In our previous general report, the key message we communicated was the widespread lack of financial controls and project management within the province. This contributed to the deteriorating state of financial affairs and accountability failures in local government. We recommended that leadership be accountable for their actions to create a culture of zero tolerance for transgressions and non-compliance with legislation. We also stressed the importance of audit action plans, emphasising that these should provide a road map to address the root causes of audit findings and prevent the situation from spiralling further out of control.

During the current year, we followed up on the prior year recommendations. While there were a number of improved audit outcomes, we identified that this might not be sustainable as most of these municipalities had not embedded the necessary preventative and detective controls. The majority of municipalities, including most of those with improved audit outcomes, submitted financial statements containing material misstatements, which required adjustments to achieve better outcomes. Management did not adequately implement and monitor action plans to improve the control environments and therefore the **lack of standardised processes, poor record management and inadequate review and reconciliation of financial and performance reports persisted.**

A large number of municipalities did not apply strong financial disciplines and then used consultants when there were municipal staff who should have performed some of these functions. We identified material errors in the financial statements at most of the municipalities where consultants were used. This was mainly due to ineffectiveness as municipalities had inadequate internal controls during the year, supplied unreliable information to the consultants, and did not monitor the deliverables of the consultants.

The contravention of legislative requirements that we reported in prior years continued to persist as material non-compliance was reported at 95% of the municipalities. Irregular expenditure incurred also remained high at R3,6 billion. This amount may not be complete as 15 municipalities (41%) were qualified on the completeness of this disclosure. The vast majority of irregular expenditure stems from non-compliance with supply chain management prescripts. Municipalities have not sufficiently dealt with the escalating irregular expenditure, as only R3,7 billion of the prior year closing balance of R28,1 billion had been investigated and written off by the council. Nelson Mandela Bay Metro reported the highest closing balance for irregular expenditure at R17,7 billion.

The province's **irregular expenditure continues to increase** as investigations are not always conducted to determine if any person is liable, which results in consequences not being enforced. The municipal public accounts committee has an oversight responsibility within the executive functionaries of the council and must ensure good governance within the municipality. The inability to deal with the escalating irregular expenditure is a clear indication that these role players are not playing their part in strengthening oversight and accountability.

The poor control environments and leadership's inability to take action against transgressors led to material irregularities, which resulted in financial losses. These financial losses arose from not billing consumers for services rendered, making payments for goods that were not received, and incurring interest due to late payments to Eskom and the South African Revenue Service. Accounting officers should ensure that controls and oversight mechanisms are in place to proactively prevent or detect instances of non-compliance before they can lead to financial losses.

The **accountability failures also had a negative impact on service delivery.** Poor project management was particularly evident at OR Tambo District, where advance payments were made to implementing agents and other service providers for goods and services, but projects were not adequately monitored to ensure that value was derived from the payments made and that service delivery was achieved. The lack of monitoring these projects resulted in delays in the completion of some, while costs exceeded the initial contract price at others. Projects were also completed but not functional. We saw an example of this at a water supply scheme project where a project is now complete but no water is available to the community.

Elundini improved to a clean audit from an unqualified opinion with findings, as basic internal control disciplines were entrenched in the daily and monthly activities, and reinforced by a strong tone set by leadership through holding officials liable for their transgressions. Senqu continued to maintain its clean audit due the strong tone set by leadership in addressing reported deficiencies and holding officials accountable for non-performance and transgressions. The stability at municipal manager and chief financial officer level, coupled with their vast experience in the local government sphere, further contributed to the strong control environment. The implementation of preventative controls in procurement and other compliance processes assisted in them again not having any findings on non-compliance with legislation. Senior management also worked well with the internal audit unit and the audit committee, which strengthened controls and improved oversight.

The financial health of municipalities continued to deteriorate, with an increase in the number of municipalities facing financial difficulties. Municipalities' inability to recover money from consumers for services rendered compounded these financial difficulties and resulted in delays in paying their creditors. At 14 municipalities, the creditors due at year-end exceeded the cash in the bank, which meant that some of the revenue they will receive in the next year will first have to be used to settle outstanding creditor accounts before being used for initiatives planned for that year. Amathole District, which is currently under administration, is an example of a municipality facing financial difficulties. The municipality spent R761 million on employee remuneration in the current year, which exceeded the equitable share of R462 million. Revenue of R372 million was billed for services rendered, but this could not fund the shortfall as most of the debt was impaired. The municipality was unable to pay its creditors of R563 million as their debt fell due because it only had R192 million in the bank at year-end.

We had numerous interactions with municipal leadership, at 'MuniMecs' (technical and political provincial interactions between municipalities and members of the executive council), with the South African Local Government Association, and through various oversight engagements where we provided recommendations for improvement. We presented guidelines for strengthening the control environment to the provincial legislature, which included the member of the executive council for cooperative governance, and discussed these in our regular engagements with the oversight departments and municipalities. We also held regular technical committee meetings with the provincial treasury and the provincial cooperative governance department to escalate audit challenges and disputes in order to resolve them as soon as possible. **Despite these interventions, we continued to identify poor-quality financial statements, unreliable performance reports and transgressions of legislation.**

The provincial treasury and the provincial cooperative governance department provided guidance to the municipalities under administration in order to address the financial difficulties and the root causes of poor audit outcomes. This contributed to the improvement in the audit outcome of Enoch Mgijima. Makana, however, retained its disclaimed audit opinion as the municipality continued to battle with its dysfunctional internal control environment. There is also an ongoing court case by the citizens of Makana requesting that the council be dissolved due to poor service delivery and the lack of infrastructure maintenance. The provincial treasury and the provincial cooperative governance department also provided support to all municipalities with adverse and disclaimed audit opinions by monitoring their action plans, providing technical assistance and assessing their readiness to submit financial statements before the due date. These interventions contributed to the improvement in audit outcomes at Dr Beyers Naudé, Walter Sisulu, and Amathole District. Despite these interventions, Chris Hani District, Ingquza Hill and Sundays River Valley were again disclaimed, as adhering to controls on a daily and monthly basis was not ingrained in the culture of these municipalities due to the vacancies in the municipal manager and chief financial officer positions.

Our key message to municipal managers and senior management is that they should **implement a proactive approach to identify risks** affecting their municipalities **and ensure that these risks are mitigated by implementing preventative controls.** This will have a positive impact in strengthening their control environment. Audit action plans must be developed, based on our recommendations, and then be diligently implemented and monitored to address poor financial and performance management controls. Leadership must promote a culture of zero tolerance for transgressions and non-compliance with legislation, and must continuously monitor the control environment. Municipal councils and municipal public accounts committees must be effective and instil order, institute investigations to determine if anyone is liable for irregular expenditure incurred, and take the necessary corrective action against transgressors. It is imperative that political and administrative leaders support each other and play their roles in creating an environment that is conducive to effectively accounting for the funds allocated to municipalities to ensure that the required services are delivered to citizens.

Improve and focus on controls for sustainable outcomes

6.2 FREE STATE

PERFORMANCE SNAPSHOT

The snapshot shows the audit outcomes of 15 municipalities in the province. With the exception of unauthorised, irregular and fruitless and wasteful expenditure, the outcomes of the outstanding audits are not included in the snapshot.

Overall audit outcomes

4 | 11 | 8

MOVEMENT

3 1 FROM 2018-19

3 7 OVER 4 YEARS

LEJWELEPUTSWA

2 | 2 | 2

- Lejweleputswa DM
- Masilonyana LM
- Matjhabeng LM
- Nala LM
- Tokologo LM
- Tswelopele LM

FEZILE DABI

4 | 1

- Fezile Dabi DM
- Mafube LM
- Metsimaholo LM
- Moqhaka LM
- Ngwathe LM

THABO MOFUTSANYANA

1 | 3 | 3

- Thabo Mofutsanyana DM
- Dihlabeng LM
- Maluti-A-Phofung LM
- Mantsopa LM
- Nketoana LM
- Phumelela LM
- Setsoto LM

XHARIEP

1 | 2 | 1

- Xhariep DM
- Kopanong LM
- Letsemeng LM
- Mohokare LM

MANGAUNG METRO

1

Metropolitan municipality | District | DM District municipality | LM Local municipality | Improved | Unchanged | Regressed

Unqualified with no findings | Unqualified with findings | Qualified with findings | Adverse with findings | Disclaimed with findings | Outstanding audits

Financially unqualified financial statements

27% (4) 2018-19: 27% (4)

Financial statements submitted without material misstatements — 7% (1)

No material findings on performance report

29% (4) 2018-19: 13% (2)

Reported achievement reliable — 29% (4)

No material findings on compliance with legislation

0% (0) 2018-19: 0% (0)

No findings on compliance with supply chain management legislation — 0% (0)

Material irregularities (MIs)

Notified by 11 June 2021

14 MIs with estimated financial loss of **R304 m** at **5 municipalities** and likely substantial harm to public sector institution at **4 municipalities** with repeat disclaimers

NATURE	
Interest and penalties payable to South African Revenue Service	5
Interest on Eskom account	4
Full and proper records not kept (repeat disclaimer)	4
Payments for infrastructure assets not received	1

Unauthorised & fruitless and wasteful expenditure

Unauthorised expenditure **R4 392 m**

Fruitless and wasteful expenditure **R603 m**

Irregular expenditure

R3 089 m

2018-19: **R2 201 m**

Closing balance

R7 319 m

2018-19: **R5 602 m**

TOP THREE CONTRIBUTORS	
Matjhabeng	**R340 m**
Setsoto	**R184 m**
Mohokare	**R183 m**

Use of financial reporting consultants

R47 m – 14 municipalities

2018-19: **R31 m – 13 MUNICIPALITIES**

Recurring use of consultants at 79% of municipalities

TOP THREE SERVICES	
Financial statements review/preparation	**R32 m**
Asset management	**R7 m**
Tax services	**R6 m**

Financial health indicators

Going concern uncertainty	**73% (11)**
Deficit	**R2 020 m (11)**
Average creditor-payment period	**507 days**
Eskom and water boards' debt in arrears	**R10 027 m (10)**
Creditors > cash available at year-end	**67% (10)**
Average municipal debt not recoverable	**71% (15)**
Average debt-recovery period	**558 days**

PROVINCIAL OVERVIEW

Each province has a unique story...

Lack of accountability creates a perpetual disrespect for regulations, resulting in mismanagement of resources and lack of service delivery

Overall, the audit outcomes have regressed since 2016-17, and the province has not achieved a clean audit since Fezile Dabi District's clean audit in 2015-16. Some municipalities fluctuated between audit outcomes, improving one year, but then regressing the next, confirming that when audit outcomes improved, it was not sustainable or due to an improvement in the underlying control environment. It is also concerning that a number of municipalities had stagnated on qualified opinions for three consecutive years. Reporting on performance information had not been prioritised, as most municipalities were still not able to report reliably on the achievement of their service delivery goals. Municipalities' unwillingness to comply with legislation is confirmed by the fact that since 2016-17, we have raised material findings on non-compliance with legislation at all 15 municipalities of which the audits had been completed – mostly relating to supply chain management. This clearly indicates a deliberate lack of accountability by political and administrative leadership to address the root causes of findings.

Since 2016-17, we have recommended that leadership set the correct tone from the top. We advocated that leadership implement and adhere to good governance practices, enforce a culture of ethical behaviour to strengthen systems and processes, implement preventative controls, and effect consequences for poor performance or misconduct – especially to curb pervasive non-compliance with legislation. We engaged with the collective management and municipal leadership, including their audit committees, in various platforms, with the aim of supporting local government leadership to establish sustainable good governance practices. This we did by sharing audit outcomes and the root causes that prevented municipalities from attaining the desired outcomes, providing practical recommendations to improve the control environment, as well as focusing on preventative controls. We further engaged the management and leadership of individual municipalities on the progress of their audit action plans and the key risks identified through our status-of-records reviews, thereby providing them with an early warning system. Sessions were held with chief financial officers and supply chain managers focusing on supply chain management matters, including the weaknesses we identified in procurement and contract management.

In spite of all these efforts, the political and administrative **leadership's inaction created a deliberate obstruction to the effective functioning of municipalities.** Our assessment since 2016-17 has shown that there had been a regression in the assurance provided by political and administrative leadership. None of the assurance providers offered the required level of assurance and the majority of them provided limited or no assurance at all. There was a lack of responsiveness to implement and monitor the audit action plans to enable the implementation of effective accountability. These outcomes were due to no one being held accountable for their actions by those they report to. Mayors did not hold councils accountable for the lack of improvement at poorly operating municipalities, with the lack of accountability cascading to all municipal levels as councils did not hold municipal managers and the senior managers that report to them accountable for not fulfilling their duties.

Also worth mentioning are the municipal public accounts committees. There had been a visible regression in their effectiveness since 2016-17, notwithstanding the investment we made through facilitating training during the member inductions as well as additional on-the-job training by the provincial treasury and the South African Local Government Association. These committees conducted limited or no investigations. Where investigations were conducted, they were not properly performed to enable the council to hold the responsible officials accountable. Ineffective internal audit units and audit committees, combined with the disregard of their contributions by management, also contributed to the poor control environment. Furthermore, the councils did not adequately assess the required legislative reports to set the right tone for prudent financial management and clearly articulate the strategic priorities to improve service delivery.

Municipalities continued to implement ineffective, short-term solutions to address shortcomings in their underlying controls, through the use of consultants – with a limited transfer of skills. Other than Thabo Mofutsanyana District, all municipalities appointed consultants for financial reporting at an aggregate cost of R46,83 million (2018-19: R30,88 million). These consultants performed tasks such as monthly reconciliations, asset verifications and updating irregular and fruitless and wasteful expenditure registers. This situation is even more concerning as there were already people employed to perform such tasks. The chief financial officers relied on the consultants to provide audit support and to assist with the responses to audit findings, even on non-technical matters, instead of municipal staff – in spite of paying R280,28 million in finance unit salaries.

The provincial treasury supported municipalities in clearing audit findings by deploying officials to attend audit steering committee meetings. This support did not yield visible results, however, due to it being reactive in nature instead of coming in the form of proactive support to improve the control environment. Nine of the 23 municipalities (39%) did not submit their financial statements within the legislated deadline, as opposed to 10 in the previous year; yet neither the provincial cooperative governance department nor the provincial treasury intervened to ensure timely submissions.

Since 2016-17, five municipalities have been placed under administration. We were unable to confirm that administrators had developed and implemented sustainable systems and preventative controls to ensure the effective functioning of these municipalities once they left. Consequently, audit outcomes did not improve and stability was not created even though three of them were under administration for at least three years (by the cut-off date of this report, these three municipalities were no longer under administration). They were not able to submit all the outstanding financial statements – even for the period of administration. These municipalities all received a disclaimed audit opinion on their last submitted financial statements, and experienced service delivery challenges over a prolonged period.

The lack of leadership tone for accountability contributed to **an environment that was vulnerable to misappropriation, wastage and the abuse of state funds.** The continued transgression of supply chain management prescripts was reflected in the significant amount of irregular expenditure incurred of R3,09 billion (2018-19: R2,2 billion). The closing balance of irregular expenditure stood at R7,32 billion (2018-19: R5,79 billion), clearly indicating that the practice of incurring irregular expenditure was rising. Another contributing factor to the significant amounts of irregular expenditure was the seven municipalities (47%) that either had a vacancy in the head of supply chain position or did not have such a position on their organogram. Municipalities should ensure that these positions are filled with people who have the required skills, respect the rule of law, are ethical, and can implement controls that would prevent irregular expenditure.

The poor state of financial management contributed to the continued deterioration in financial health. Eleven municipalities (73%) were assessed as having a material uncertainty relating to their going concern. The 15 municipalities of which the audits had been completed, had a net current liability position of R8,57 billion (2018-19: R6,73 billion). This means that their current liabilities exceeded their current assets. Local municipalities were in arrears of R10,03 billion (2018-19: R7,70 billion) with Eskom and the water boards. Some municipalities also failed to pay over contributions deducted from employees' salaries to third parties, such as medical aids and pension funds. We confirmed nine material irregularities at five municipalities relating to the late payment of Eskom and South African Revenue Service accounts, mainly due to municipalities' inability to pay their creditors on time, which resulted in interest and penalties of R296,82 million.

Municipalities continued to suffer extensive distribution losses, which were due to dilapidating infrastructure, unmetered consumption and theft. Municipalities also incurred deficits totalling R2,02 billion due to overspending of their approved budgets, while unauthorised expenditure of R4,39 billion (2018-19: R4,95 billion) was incurred. **Poor budgeting practices and overspending hamper service delivery** as municipalities are unable to build up reserves that would help them continue to provide services in future, such as maintaining or replacing infrastructure assets.

Matjhabeng serves as an example where the continued disregard for supply chain management prescripts and poor financial disciplines have led to the municipality being in a dire financial position, which in turn negatively affected service delivery. The municipality owed Eskom and Sedibeng Water R3,34 billion and R3,68 billion, respectively. In addition, the municipality lost R462,84 million (76%) of the water purchased from Sedibeng Water due to leakages, burst pipes, line losses, tampering and theft. The water lost added to the significant amounts payable to the water boards but could not be billed to consumers to earn revenue. This contributed to the vicious cycle of poor cash flows, leading to further delays in the municipality's ability to render quality services to the community. Also at Matjhabeng, a material irregularity was identified relating to the construction of the Nyakallong storm-water system. The contract of R13,74 million was awarded in April 2017 and the project was to be completed by May 2018. However, the project was found to be incomplete during a site visit, with the contractor abandoning the project site and the work performed not being of the required quality. Estimated payments of R7,21 million were made for an attenuation dam to contain and manage storm water but the dam had not been constructed. This material irregularity was in the process of being referred to a public body for investigation.

Accountability can be realised through a decisive leadership tone. To create sustainable improvements in the control environment and audit outcomes, political and administrative leaders should therefore adopt a zero-tolerance approach when it comes to non-compliance with legislation and poor performance by implementing timely consequences, including disciplinary action. This will change the current culture and set an ethical and service-orientated tone for an enabling environment.

Accountability can be realised through decisive leadership tone

6.3 GAUTENG

PERFORMANCE SNAPSHOT

The snapshot shows the audit outcomes of 10 municipalities and 14 municipal entities in the province. The audit outcomes of municipal entities are included due to the significance thereof in the province. The figures for unauthorised, irregular and fruitless and wasteful expenditure include Emfuleni, which is an outstanding audit.

Overall audit outcomes

MUNICIPALITIES 2 | 7 | 1 | 1

MOVEMENT

FROM 2018-19: 1 improved, 1 regressed

OVER 4 YEARS: 1 improved, 1 regressed

MUNICIPAL ENTITIES 13 | 1

MOVEMENT

FROM 2018-19: 0 improved, 1 regressed

OVER 4 YEARS: 0 improved, 5 regressed

JOHANNESBURG

13

- City of Johannesburg Metro ▶
- Johannesburg City Parks ▶
- City Power Johannesburg ▶
- Joburg City Theatre *
- Johannesburg Development Agency ▼
- Joburg Market ▶
- Joburg Property Company ▶
- Johannesburg Roads Agency ▶
- Johannesburg Social Housing Company ▶
- Johannesburg Water ▶
- Johannesburg Metropolitan Bus Services ▶
- Metropolitan Trading Company ▶
- Pikitup Johannesburg ▶

TSHWANE

3

- City of Tshwane Metro ▶
- Housing Company Tshwane *
- Tshwane Economic Development Agency *

WEST RAND

1 | 3 | 1

- West Rand DM ▶
- Mogale City LM ▶
- Merafong City LM ▶
- Rand West City LM ▼
- West Rand Development Agency *

EKURHULENI

1 | 2 | 1

- City of Ekurhuleni Metro ▲
- Brakpan Bus Company ▶
- East Rand Water Care Company ▶
- Germiston Phase II Housing Company ▶

SEDIBENG

1 | 2 | 1

- Sedibeng District ▶
- Emfuleni LM
- Lesedi LM ▶
- Midvaal LM ▶

* These represent small auditees that are excluded from this report

Metropolitan municipality | District | DM District municipality | LM Local municipality | ▲ Improved | ▶ Unchanged | ▼ Regressed

Unqualified with no findings | Unqualified with findings | Qualified with findings | Adverse with findings | Disclaimed with findings | Outstanding audits

	Municipalities	2018-19	Municipal entities	2018-19
Financially unqualified financial statements	90% (9)	100% (10)	93% (13)	93% (13)
Financial statements submitted without material misstatements	50% (5)		29% (4)	
No material findings on performance report	80% (8)	20% (2)	71% (10)	57% (8)
Reported achievement reliable	80% (8)		93% (13)	
No material findings on compliance with legislation	20% (2)	10% (1)	0% (0)	7% (1)
No findings on compliance with supply chain management legislation	10% (1)		0% (0)	

Material irregularities (MIs) Notified by 8 June 2021

9 MIs with estimated financial loss of **R208,45 m** at **2 municipalities**

NATURE

Assets – 2 prior year MIs (R9,43 m estimated loss)
Interest and penalties – 2 MIs (R22,59 m estimated loss)
Revenue management (interest not charged on outstanding consumer debt) – 1 MI (R9,99 m estimated loss)
Payments – 4 MIs (R166,44 m estimated loss)

Unauthorised & fruitless and wasteful expenditure

Unauthorised expenditure **R4,24 bn** (Municipalities)
2018-19: R2,25 bn

Fruitless and wasteful expenditure **R756,93 m** (Municipalities and Municipal entities)
2018-19: R749,90 m

Irregular expenditure

Municipalities	+	Municipal entities	=	Total	Closing balance
R4,31 bn	+	R2,96 bn	=	R7,27 bn	R21,16 bn
2018-19: R4,98 bn		2018-19: R1,76 bn		2018-19: R6,74 bn	2018-19: R16,28 bn

TOP THREE CONTRIBUTORS (Municipalities)

City of Tshwane Metro	**R2,53 bn**
City of Johannesburg Metro	**R1,05 bn**
Emfuleni (outstanding)	**R309,61 m**

TOP THREE CONTRIBUTORS (Municipal entities)

City Power	**R1,40 bn**
Johannesburg Water	**R735,13 m**
Johannesburg Roads Agency	**R316,04 m**

Use of financial reporting consultants

R230,21 m – 6 municipalities

2018-19: R242,42 m – 6 MUNICIPALITIES

Recurring use of consultants at 83% of municipalities

TOP THREE SERVICES

Asset management	**R224,88 m**
Tax services	**R4,47 m**
Financial statements review/preparation	**R0,86 m**

Financial health indicators

	Municipalities	Municipal entities
Going concern uncertainty	30% (3)	–
Deficit	R3,21 bn (4)	R83,56 m (2)
Average creditor-payment period	300 days	191 days
Eskom and water boards' debt in arrears	R2,77 bn (5)	–
Creditors > cash available at year-end	80% (8)	69% (9)
Average municipal debt not recoverable	65% (10)	46% (13)
Average debt-recovery period	119 days	215 days

Municipalities   Municipal entities

PROVINCIAL OVERVIEW

Each province has a unique story...

Despite pockets of improvements, inadequate monitoring of preventative controls resulted in stagnant outcomes and increasing levels of unauthorised, irregular and fruitless and wasteful expenditure

Reflecting on the previous year, Gauteng municipalities had held steady with good audit outcomes sustained in 2018-19 as a result of a stable control environment. We had urged the provincial leadership to enhance good financial discipline, preventative controls and the effecting of consequences. In response, municipal audit outcomes were sustained in 2019-20, with the significant achievement of the City of Ekurhuleni Metro improving to a clean audit outcome due to addressing material procurement findings, thereby joining Midvaal that maintained its clean audit outcome for the seventh consecutive year.

Gauteng municipalities had generally produced good-quality published financial statements in the preceding three years and was the only province without negative financial outcomes. However, **the emergence of qualifications requires attention,** with Rand West City regressing in the current year to a qualified opinion from an unqualified opinion with findings, due to various material errors in its financial statements. Municipalities should work towards strengthening preventative controls to avoid reliance on the audit process to identify and correct errors, particularly in relation to accounting for assets.

The quality of financials at metros improved overall except at the City of Tshwane Metro, which relied on the audit process to support revenue disclosed in the financials. This was due to the practice of estimating service charges for excessive periods. In addition, material errors on assets were identified and corrected, despite the metro spending R198,43 million (2018-19: R213,14 million) on consultants to verify and correct the fixed asset register. While the province used public funds efficiently by using mostly internal staff to prepare financial statements, care should be taken to ensure that the limited available public funds are spent in an effective manner in all instances.

While compliance outcomes improved, the current level of non-compliance remains high, particularly in relation to procurement management and the prevention of unauthorised, irregular and fruitless and wasteful expenditure. **We remain concerned about the high levels of irregular expenditure** incurred, especially at City of Tshwane and City of Johannesburg metros (which contributed a combined R3,58 billion (83%) at municipal level), and the increased closing balances not yet dealt with due to the slow pace of investigations.

Outcomes on performance reporting improved significantly with the majority of municipalities reporting accurately on service delivery information. This was due to an improvement in the consistent implementation of controls relating to performance information. Municipalities should build on this, and use it as an opportunity to improve the achievement of performance targets and – in turn – service delivery. This is especially significant in the context of the covid-19 pandemic, as the period of lockdown as well as budget constraints had a negative impact on the achievement of planned performance targets in the province. Municipalities should also ensure that controls implemented around the key service delivery programmes audited are replicated across all programmes to sustain positive performance information outcomes going forward and, most importantly, ensure that citizens receive quality services.

Despite efforts made, the financial health of municipalities, including the metros as the economic hubs of the country, remained concerning and fell under further strain due to covid-19. The pandemic worsened existing difficulties relating to poor revenue collection, debt write-offs and credit downgrades. The deteriorating financial position poses a risk towards municipalities achieving their planned service delivery targets. This calls for greater financial prudence over the limited funds available and the elimination of wasteful expenditure and other losses. This will ensure that municipalities are able to provide adequate services to the expanding Gauteng population. While efforts were made to stabilise municipalities, including provincial intervention at West Rand District and Emfuleni, **the implementation of financial improvement strategies** remains in progress and **should be accelerated.**

Notwithstanding some improvements, the combined assurance model is still not as effective as it should be. We encourage all role players – especially accounting officers, senior management (together with internal audit units and audit committees) and executive authorities – to ensure that they contribute positively towards providing assurance regarding the control environment. These controls include regular and accurate reviews of financial and performance reports, proper procurement planning and contract management, and the use of compliance checklists.

In addition, increased oversight by councils and municipal public accounts committees would be instrumental in holding municipal leaders accountable, including ensuring that investigations into unauthorised, irregular and fruitless and wasteful expenditure are done timeously. We also continue to encourage the provincial cooperative governance department, the provincial treasury and the premier to intensify the level of support provided to municipalities going forward, especially in the area of compliance with legislation and the quality of published financial statements.

Gauteng's service delivery model is fairly unique in the country, with a number of specialised municipal entities administered by municipal boards and responsible for a significant portion of the province's municipal expenditure and service delivery programmes. **The overall negative trend in municipal entity outcomes,** primarily due to non-compliance with legislation, **continued** in the current year as the Johannesburg Development Agency regressed from a clean audit outcome, which it had sustained for three years, to an unqualified opinion with findings. This was due to material errors in the submitted financials (which were subsequently corrected), caused by inadequate reviews of the financial statements and supporting schedules. In addition, the Brakpan Bus Company remained disclaimed for the second year, due to instability in the accounting officer and financial manager positions, inadequate record-management controls, and a lack of basic financial disciplines. All other municipal entities sustained their outcomes of unqualified with material findings, including the four largest municipal entities by budget, namely City Power Johannesburg, Johannesburg Water, Pikitup Johannesburg and Johannesburg Roads Agency, which were responsible for a combined R36,13 billion of the total municipal entity budget of R42,8 billion. In the context of the municipal entity administrative model, we reiterate our previous year's recommendation that the municipal leadership and oversight structures pay closer attention to the governance of entities under their control to reverse the negative trend in audit outcomes.

We expanded our implementation of the amended Public Audit Act to four auditees, and identified nine material irregularities at two metros, namely City of Tshwane and City of Johannesburg. The material irregularities related to the current and prior years, indicating that municipalities should prioritise monitoring the implementation of stringent controls over expenditure to ensure that payments are made only when goods and services are received, and that municipal assets are adequately safeguarded. Accounting officers have been responsive towards the process and are taking corrective steps to address the irregularities identified. However, oversight and executive authorities should also continue to monitor the progress made to both address and prevent such material irregularities, thereby ensuring that public funds are only spent for their intended purpose.

Gauteng remains well positioned as a destination of choice for individuals with professional skills seeking employment in the country, with municipalities that have both attracted and retained staff with the right skills benefiting from this continuity. This has had a positive impact on financial management and – in turn – audit outcomes. The province's outcomes have also demonstrated that focused attention by the political and administrative leadership to our messages has yielded some benefits, especially relating to compliance and performance reporting. There remains a need for further improvement, and **we therefore urge oversight structures to monitor and hold accounting officers accountable,** particularly regarding the worrying emergence of qualified financial outcomes; the high levels of unauthorised, irregular and fruitless and wasteful expenditure; and the effecting of adequate consequences for poor performance and transgressions.

While the covid-19 pandemic has brought new challenges to the auditing sphere, we will continue to focus on supporting the public sector to provide the tools to those responsible to strengthen the municipal control environment. This we will do through our ongoing engagements with the political and administrative leadership of the province, including through our communication of key recommendations and guidance on preventative controls.

Improve monitoring of preventative controls

6.4 KWAZULU-NATAL

PERFORMANCE SNAPSHOT

The snapshot shows the audit outcomes of 52 municipalities and 2 entities. With the exception of unauthorised, irregular and fruitless and wasteful expenditure, the outcomes of the outstanding audits are not included in the snapshot.

AMAJUBA

1 2 1

- Amajuba DM
- Danhausser LM
- Emadlangeni LM
- Newcastle LM

UMZINYATHI

2 1 1 1

- uMzinyathi DM
- Endumeni LM
- Msinga LM
- Nquthu LM
- Umvoti LM

ZULULAND

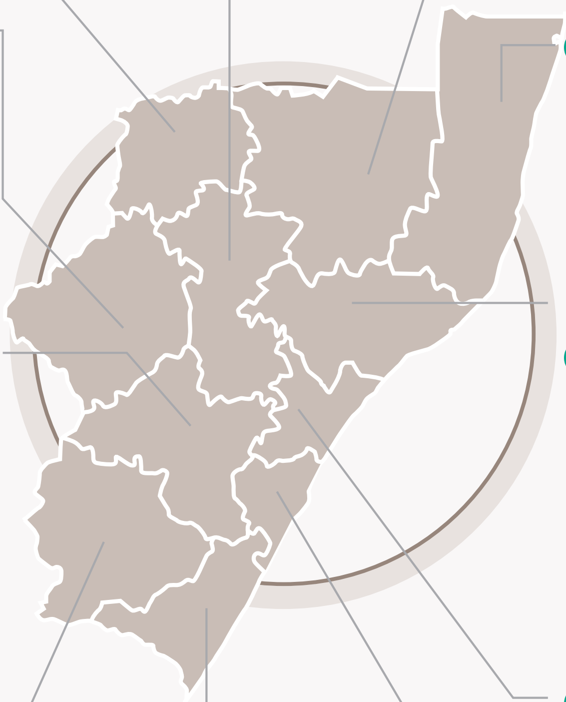
3 3

- Zululand DM
- Abaqulusi LM
- eDumbe LM
- Nongoma LM
- Ulundi LM
- uPhongolo LM

UTHUKELA

1 1 1 1

- Uthukela DM
- Alfred Duma LM
- Inkosi Langalibalele LM
- Okhahlamba LM



UMKHANYAKUDE

2 2 1

- Umkhanyakude DM
- Big 5 Hlabisa LM
- Jozini LM
- Mtubatuba LM
- Umhlabuyalingana LM

UMGUNGUNDLOVU

5 3

- Umgungundlovu DM
- Impendle LM
- Mkhambathini LM
- Mpofana LM
- Msunduzi LM
- Richmond LM
- Umngeni LM
- uMshwathi LM

KING CETSHWAYO

1 5

- King Cetshwayo DM
- Mfolozi LM
- Mthonjaneni LM
- Nkandla LM
- Umhlatuze LM
- Umlalazi LM

ILEMBE

5

- Ilembe DM
- KwaDukuza LM
- Mandeni LM
- Maphumulo LM
- Ndwedwe LM

HARRY GWALA

4 1

- Harry Gwala DM
- Dr Nkosazana Dlamini Zuma LM
- Greater Kokstad LM
- Ubuhlebezwe LM
- uMzimkhulu LM

UGU

3 1 1

- Ugu DM
- Ray Nkonyeni LM
- uMdoni LM
- Umuziwabantu LM
- Umzumbe LM

ETHEKWINI METRO

1

- UThukela Water
- Durban Marine Theme Park

Metropolitan municipality | District | Municipal entity | DM District municipality | LM Local municipality | Improved | Unchanged | Regressed

Unqualified with no findings | Unqualified with findings | Qualified with findings | Adverse with findings | Disclaimed with findings | Outstanding audits

Overall audit outcomes

MOVEMENT

8 8 FROM 2018-19

6 17 OVER 4 YEARS

Financially unqualified financial statements

65% (35) 2018-19: 63% (34)

Financial statements submitted without material misstatements 24% (13)

No material findings on performance report

59% (32) 2018-19: 46% (25)

Reported achievement reliable 74% (40)

No material findings on compliance with legislation

4% (2) 2018-19: 4% (2)

No findings on compliance with supply chain management legislation 2% (1)

Material irregularities (MIs)

Notified by 7 June 2021

18 MIs with estimated financial loss of **R248,36 m** at **5 municipalities**

NATURE	
Interest and penalties	R18,03 m
Assets not safeguarded	R64,58 m
Revenue not billed/collected	R161,24 m

Unauthorised & fruitless and wasteful expenditure

Unauthorised expenditure **R3 666,37 m** Fruitless and wasteful expenditure **R138,94 m**

Irregular expenditure

R4 861,81 m

2018-19: **R6 521,57 m**

Closing balance

R13 511,10 m

2018-19: **R13 467,46 m**

TOP THREE CONTRIBUTORS	
eThekwini Metro	R1 072,03 m
Umkhanyakude	R476,42 m
uMzinyathi	R298,37 m

Use of financial reporting consultants

R109,88 m – 33 municipalities

(excluding amounts paid by other institutions)

2018-19: **R93,37 m – 44 MUNICIPALITIES**

Recurring use of consultants at 76% of municipalities

TOP THREE SERVICES	
Asset management	R38,67 m
Financial statements preparation	R32,26 m
Other financial reporting services	R18,95 m

Financial health indicators

Going concern uncertainty	17% (9)
Deficit	R660,41 m (10)
Average creditor-payment period	136 days
Eskom and water boards' debt in arrears (municipalities only)	R1 098,94 m (16)
Creditors > cash available at year-end	42% (21)
Average municipal debt not recoverable	56% (50)
Average debt-recovery period	196 days

PROVINCIAL OVERVIEW

Each province has a unique story...

Stagnation in audit outcomes – effective accountability and consequences not consistently enforced

In 2018-19, we urged leadership to respond to our constant calls for the effective implementation and monitoring of preventative controls and recommendations to positively influence accountability and basic control disciplines. The overall stagnation in audit outcomes demonstrates complacency from management and leadership when it comes to effectively and decisively addressing key matters of concern. Slow responses by management, coupled with leadership's lack of action in implementing action plans and failure to implement consequences for poor performance, remained the main factors that negatively affected the audit outcomes.

The City of Umhlatuze's improvement to a clean audit was a step in the right direction, attributed to management implementing an action plan to address prior year audit recommendations and to the internal audit unit performing risk-based audits on supply chain management processes. The finance team was sufficiently resourced and skilled, which allowed them to prepare the financial statements in-house. In contrast, the financial statements of Umzinyathi, Amajuba and Inkosi Langalibalele were not supported by sufficient audit evidence, resulting in their **disclaimed opinions.** This **stemmed from senior management's failure to take accountability and institutionalise the basic disciplines** of record management, reconciliations and fundamental reviews of financial reporting.

The quality of the submitted financial statements reflected an improvement at some municipalities due to leadership's commitment to implement and maintain robust transactional level controls. However, there are still a large number of municipalities (76%) that submitted poor-quality financial statements. Municipalities continued to rely on the audit process to identify misstatements, as evident by the 41% of auditees that received an unqualified audit opinion only because material audit adjustments were allowed.

Many municipalities also **continued to rely on consultants even though officials were appointed to perform these functions.** Despite the excessive amounts spent on consultants for financial reporting, only seven (21%) of the 33 municipalities reflected improved audit outcomes, while we identified material misstatements in the consultants' area of responsibilities at 17 municipalities (52%). The poor quality of the underlying data, coupled with poor project management and monitoring of the consultants' work, limited their impact and effectiveness on quality financial reporting.

Fewer auditees had material findings on their reported performance information, although material adjustments had to be made to the submitted performance reports. The improvement could mainly be attributed to enhanced record-keeping practices and detailed reviews and oversight by the internal monitoring and evaluation units. Useful and reliable performance reporting provides communities with credible information that they can use to assess service delivery and hold municipalities accountable. It also allows national and provincial government to track progress towards service delivery goals.

Compliance with key legislation remained a challenge due to inadequate consequences for transgressions and a failure to implement supervisory checks and controls. Non-compliance with supply chain management prescripts contributed to more than 90% of the total irregular expenditure incurred of R4,86 billion. Although some efforts were made to deal with the prior year irregular expenditure closing balance of R13,47 billion, progress in investigating this balance was slow. Irregular expenditure of R4,55 billion was written off as no officials were found to be liable for these transgressions. Municipal councils did not always ensure that investigations were adequately performed to determine if a person was liable before approving the write-off of irregular expenditure.

Financial sustainability remained under stress, aggravated by economic pressures and austerity measures announced by government. Nine auditees reported going concern challenges. At some municipalities, the collection of debt was hampered by ineffective debt-collection systems and processes. This was made even worse by the impact of the covid-19 pandemic and resulted in municipalities struggling to pay outstanding creditors, such as Eskom and water boards, on a timely basis. Municipalities also struggled to practise sound financial management and budget monitoring, as 20% of them reported deficits for the year. The poor financial management practices affected some municipalities' ability to provide adequate service delivery to citizens. Unauthorised expenditure amounted to R3,67 billion in the current year, mostly due to overspending on non-cash items. Non-cash items such as debt-impairment provisions were higher because the covid-19 pandemic affected citizens' ability to pay for services rendered. There was also unplanned additional expenditure due to the pandemic. On a positive note, the City of Umhlatuze (which obtained a clean audit) has, over a number of years, demonstrated the prudent financial management of funds, which has contributed to the achievement of service delivery initiatives.

The material irregularities we identified at five municipalities demonstrate that, in addition to the challenges faced by municipalities relating to poor financial management practices, financial losses were incurred largely as a result of payments for goods or services not received, failure to safeguard assets, fruitless and wasteful expenditure incurred in the form of interest and penalties, as well as the non-billing and collection of revenue due.

The provincial cooperative governance department swiftly intervened at municipalities with maladministration by appointing administrators. However, there were no significant improvements in audit outcomes, mainly due to the late appointment of the administrators, resistance by municipal officials, and vacancies in key positions. Of the seven municipalities that were under administration in the previous year, only two reflected an improved audit outcome, while two regressed and three remained unchanged on unfavourable audit outcomes. Through the municipal support programme, the premier's office (in conjunction with the provincial cooperative governance department and the provincial treasury) helped municipalities to reduce the number of compliance findings and the amount of irregular expenditure reported, and to improve the quality of performance reporting. However, a detailed analysis of the impact of these initiatives, together with the stringent monitoring of their implementation (including the transfer of skills), must be further intensified to trigger sustainable improvements.

As municipalities are at the forefront of service delivery and have a direct impact on the lives of citizens, it is critical that they have sound internal control systems and effective governance structures for them to achieve their goals. Management needs to ensure that the understanding and application of preventative controls is entrenched in day-to day activities through appropriate reviews, monitoring, corrective action and credible reporting by appropriately skilled officials. Municipal managers must also promote a culture of accountability by monitoring corrective action based on our recommendations. Consequences must be enforced for officials who fail to comply with applicable legislation, and strict corrective action must be taken against transgressors.

We continue to encourage key role players such as the provincial cooperative governance department and the provincial treasury to intensify the level of support provided to municipalities going forward, especially in the areas of compliance with legislation and financial management. These coordinating departments need to work efficiently and use a collaborative approach when assessing and responding to the myriad of risks affecting local government. To improve sustainably, **leadership in local government should enforce a culture of ethical behaviour and adhere to good governance practices** in order to strengthen accountability and transparency.

Upscale implementation of preventative controls and drive consistent consequences

6.5 LIMPOPO

PERFORMANCE SNAPSHOT

The snapshot shows the audit outcomes of 22 municipalities in the province. With the exception of unauthorised, irregular and fruitless and wasteful expenditure, the outcomes of the outstanding audits are not included in the snapshot.

Overall audit outcomes

1 | 13 | 7 | 1 | 5

MOVEMENT

	Improved	Regressed
FROM 2018-19	8	0
OVER 4 YEARS	12	0

CAPRICORN

1 | 2 | 2

- Capricorn DM ▶
- Blouberg LM ▲
- Lepelle-Nkumpi LM
- Molemole LM ▶
- Polokwane LM

VHEMBE

4 | 1

- Vhembe DM ▶
- Collins Chabane LM ▲
- Makhado LM ▲
- Musina LM ▲
- Thulamela LM ▶

WATERBERG

2 | 3 | 1

- Waterberg DM ▶
- Bela-Bela LM ▶
- Lephalale LM ▲
- Modimolle-Mookgophong LM ▲
- Mogalakwena LM ▶
- Thabazimbi LM ▶

SEKHUKHUNE

2 | 2 | 1

- Sekhukhune DM
- Elias Motsoaledi LM ▶
- Ephraim Mogale LM ▲
- Fetakgomo Tubatse LM ▶
- Makhudutamaga LM ▶

MOPANI

3 | 1 | 2

- Mopani DM
- Ba-Phalaborwa LM ▶
- Greater Giyani LM ▲
- Greater Letaba LM ▶
- Greater Tzaneen LM
- Maruleng LM ▶

Metropolitan municipality | District | DM District municipality | LM Local municipality | ▲ Improved | ▶ Unchanged | ▼ Regressed

Unqualified with no findings | Unqualified with findings | Qualified with findings | Adverse with findings | Disclaimed with findings | Outstanding audits

Financially unqualified financial statements

64% (14) — 2018-19: 32% (7)

Financial statements submitted without material misstatements — 14% (3)

No material findings on performance report

27% (6) — 2018-19: 27% (6)

Reported achievement reliable — 41% (9)

No material findings on compliance with legislation

5% (1) — 2018-19: 5% (1)

No findings on compliance with supply chain management legislation — 14% (3)

Material irregularities (MIs)

Notified by 14 December 2019

1 MI with estimated financial loss of **R13 m** at **1 municipality**

NATURE

Payments made for services not rendered

Unauthorised & fruitless and wasteful expenditure

Unauthorised expenditure **R2 120 m**

Fruitless and wasteful expenditure **R313 m**

Irregular expenditure

R2 286 m

2018-19: **R2 109 m**

Closing balance

R8 118 m

2018-19: **R7 038 m**

TOP THREE CONTRIBUTORS

Fetakgomo Tubatse	**R458 m**
Mogalakwena	**R437 m**
Elias Motsoaledi	**R83 m**

Use of financial reporting consultants

R176 m – 21 municipalities

2018-19: **R141 m – 21 MUNICIPALITIES**

Recurring use of consultants at 100% of municipalities

TOP THREE SERVICES

Financial statements review/preparation	**R77 m**
Tax services	**R57 m**
Asset management	**R33 m**

Financial health indicators

Going concern uncertainty	**14% (3)**
Deficit	**R48 m (3)**
Average creditor-payment period	**215 days**
Eskom and water boards' debt in arrears	**R961 m (8)**
Creditors > cash available at year-end	**50% (10)**
Average municipal debt not recoverable	**73% (20)**
Average debt-recovery period	**206 days**

PROVINCIAL OVERVIEW

Each province has a unique story...

Improvement in audit outcomes, which is mainly consultant driven and not supported by equivalent improvement in sustainable key control environment

We noted a significant improvement in audit outcomes under the current administration whose term began in 2016. Under the leadership of this administration, Capricorn District sustained its clean audit status and concerted efforts were made to eliminate disclaimers. Whilst these efforts are commendable, there are still a number of municipalities with qualified opinions. The improvements were largely due to the assistance of consultants, not necessarily as a result of an improvement in the control environments of these municipalities. The quality of performance reporting remained a challenge, with 16 municipalities (73%) having material findings in their audit reports in this area, the majority of which related to the reported information not being reliable. The inadequate effecting of consequences continued to be an enabler of non-compliance with legislated prescripts.

Since the onset of the current administration's term, we consistently reported that **municipalities are over-reliant on consultants for financial reporting**; and the year under review was no exception. The province spent R176 million on consultants for financial reporting purposes in addition to the R539 million spent on salary costs in the finance units, which cannot be justified. We recommended that the performance of consultants be properly monitored by management and audit committees to hold consultants accountable for findings raised in the areas for which they were appointed. Due to municipalities' failure to monitor and take ownership of the work that consultants performed, officials could not respond to audit findings and instead referred findings to the consultants. In addition, consultants did not transfer skills to capacitate officials in the finance units. In response to our recommendations, the premier and the members of the executive council for the provincial treasury and for cooperative governance committed to ensure that municipalities design controls to manage the transfer of skills by consultants.

There is a dire need to intensify efforts towards strengthening internal controls around financial and performance reporting processes. Leadership must set the tone for a sound system of financial management to ensure sustainable improvement in the quality of the financial information available for decision-making and submitted for auditing. Senior management did not provide the required assurance over basic financial disciplines and accounting officers failed to take action against poor performance. **The municipal leadership needs to take strong actions against those who undermine the efforts to create a robust internal control environment.**

Complying with laws and regulations remained a challenge. We raised recurring non-compliance findings on material misstatements in the financial statements, weaknesses in procurement management as well as unauthorised, irregular and fruitless and wasteful expenditure. The administrative leadership and senior management were slow to implement corrective actions to address the root causes of these findings. Irregular expenditure continued to rise, with R2,3 billion incurred in the current year. A significant portion was as a result of non-compliance with supply chain management prescripts. The province had a balance of R8,1 billion in irregular expenditure that had not been dealt with.

A lack of consequences was an enabler of unwanted expenditure, and casts doubt on the ability of municipal public accounts committees and municipal councils to conduct timely investigations to ensure that the responsible officials are held accountable. It is alarming that we reported non-compliance with legislation on effecting consequences at most municipalities. We call upon the provincial leadership to ensure that those responsible are held accountable; if they fail to do so, it will ultimately adversely affect service delivery.

Unauthorised expenditure slightly decreased, with R2,1 billion incurred in the current year. The overspending was as a result of poor budget management as municipalities failed to appropriately budget for their cash and non-cash items. There is a need for municipalities to properly manage their budget and control their expenditure. The provincial treasury can play its part by providing guidance when budgets are either initially prepared or adjusted.

The status of financial health continued to deteriorate, with three municipalities reported to be in a vulnerable financial position and three municipalities recording a deficit due to their expenditure exceeding their total revenue. Municipalities continued to struggle with debt collection, with 73% of the debt balance in the province provided for as irrecoverable. **Poor debt collection coupled with the financial impact of covid-19 caused financial challenges for municipalities**, which resulted in suppliers being paid later than the prescribed 30 days and an increase in the average creditor-payment period.

The late payment of suppliers puts pressure on their finances and sustainability, especially small and medium suppliers, which then has an adverse effect on the economy of the province. This trend needs to be curbed as it results in **money earmarked for service delivery being used to pay interest on overdue accounts**, resulting in fruitless and wasteful expenditure. Payments of R170 million were made as a result of interest and penalties charged by suppliers. This clear wastage of resources is alarming considering the service delivery shortages due to budget constraints in the province.

We followed up on a material irregularity identified in the 2018-19 financial year at Mogalakwena involving a payment of R13 million. This payment was made for work not performed, as effective internal controls were not in place for the approval and processing of payments. Once the irregularity had been communicated, the accounting officer acted swiftly by instituting an investigation into the matter, which resulted in the suspension of two officials. Disciplinary processes are underway. We will follow up on this material irregularity in the 2020-21 audit cycle.

The premier tasked the members of the executive council for the provincial treasury and for cooperative governance to investigate and find solutions to curb the rising trend in irregular expenditure. In addition, the provincial treasury was tasked to identify the root causes of the excessive reliance on consultants in the province, specifically focusing on those municipalities who, despite using consultants year on year, show no improvement in their audit outcomes. The progress of these initiatives will be followed up in the next financial year.

To improve the financial health of municipalities in the province, the political and administrative leadership (including the oversight structures) must intervene to ensure the implementation of proper debt-collection strategies. In addition, there must be appropriate terms of reference to provide for the transfer of skills to municipal personnel when consultants are appointed. To ensure the successful transfer of skills, appropriately qualified officials must be appointed in key financial management positions. Furthermore, to curb the increase in transgressions of laws and regulations, **leadership must set the correct tone at the top and act in a consistent and deliberate manner** against those officials who intentionally fail to comply with legislation.

Active leadership supervision will lead to sustainable key control environment

6.6 MPUMALANGA

PERFORMANCE SNAPSHOT

The snapshot shows the audit outcomes of 11 municipalities in the province. With the exception of unauthorised, irregular and fruitless and wasteful expenditure, the outcomes of the outstanding audits are not included in the snapshot.

Overall audit outcomes

3 | 2 | 3 | 2 | 1 | 9

MOVEMENT

3 0 FROM 2018-19

1 4 OVER 4 YEARS

EHLANZENI

1 | 1 | 3

- Ehlanzeni DM ▲
- Bushbuckridge LM ▶
- City of Mbombela LM
- Nkomazi LM
- Thaba Chweu LM

NKANGALA

2 | 2 | 1 | 2

- Nkangala DM ▶
- Dr JS Moroka LM
- Emakhazeni LM ▶
- Emalahleni LM
- Steve Tshwete LM ▲
- Thembisile Hani LM ▶
- Victor Khanye LM ▲

GERT SIBANDE

1 | 1 | 1 | 1 | 4

- Gert Sibande DM
- Chief Albert Luthuli LM ▶
- Dipaleseng LM
- Dr Pixley Ka Isaka Seme LM
- Govan Mbeki LM ▶
- Lekwa LM
- Mkhondo LM ▶
- Msukaligwa LM ▶

Metropolitan municipality | District | DM District municipality | LM Local municipality | ▲ Improved | ▶ Unchanged | ▼ Regressed

Unqualified with no findings | Unqualified with findings | Qualified with findings | Adverse with findings | Disclaimed with findings | Outstanding audits

Financially unqualified financial statements

45% (5) 2018-19: 45% (5)

Financial statements submitted without material misstatements **27% (3)**

No material findings on performance report

36% (4) 2018-19: 36% (4)

Reported achievement reliable **50% (5)**

No material findings on compliance with legislation

27% (3) 2018-19: 9% (1)

No findings on compliance with supply chain management legislation **0% (0)**

Material irregularities (MIs)

Notified by 11 June 2021

7 MIs with estimated financial loss of **R255,23 m** at **4 municipalities** and likely substantial harm to public sector institution at **3 municipalities** with repeat disclaimers

NATURE

Interest and penalties
Full and proper records not kept (repeat disclaimer)

Unauthorised & fruitless and wasteful expenditure

Unauthorised expenditure **R2 190,3 m**

Fruitless and wasteful expenditure **R885,03 m**

Irregular expenditure

R1 556,19 m

2018-19: **R1 594,15 m**

Closing balance

R6 677,09 m

2018-19: **R6 569,46m**

TOP THREE CONTRIBUTORS	
Bushbuckridge	R411,91 m
Govan Mbeki	R222,05 m
Emakhazeni	R104,84 m

Use of financial reporting consultants

R63,73 m – 9 municipalities

2018-19: **R67,14 m – 9 MUNICIPALITIES**

Recurring use of consultants at 67% of municipalities

TOP THREE SERVICES	
Tax services	R25,42 m
Financial statements review/preparation	R21,43 m
Asset management	R14,18 m

Financial health indicators

Going concern uncertainty	18% (2)
Deficit	R318,05 (5)
Average creditor-payment period	279 days
Eskom and water boards' debt in arrears	R3 042,5 m (6)
Creditors > cash available at year-end	63% (5)
Average municipal debt not recoverable	62% (7)
Average debt-recovery period	253 days

PROVINCIAL OVERVIEW

Each province has a unique story...

The state of internal controls, coupled with lack of consequences for transgressions and weakened oversight, is at the centre of the deteriorating accountability in our local government

Over the past four years, the control environment continued to collapse at most of the municipalities in the province due to the ineffectiveness of the various assurance providers. Senior management, including most accounting officers, did not fulfil their responsibility to develop and effectively implement the basic controls that form the foundation of a sound control environment. In response to the recommendations we made in the previous year, provincial leadership committed to establish a practical intervention strategy to strengthen the local government control environment. This included capacitating and skilling the administration and oversight committees of councils and implementing consequences. However, since these commitments had not been effectively implemented by the end of the 2019-20 financial year, the status of the internal control environments worsened.

As detailed in the rest of this section, we have categorised the challenges facing the Mpumalanga local government into four key areas that need urgent attention in order to improve accountability and, consequently, service delivery. These four key areas are:

- ineffectiveness of preventative controls
- deteriorating financial health
- ineffective infrastructure project management and monitoring
- non-adherence to laws and regulations as well as lack of consequences.

The root cause of the outcomes is that **most municipalities have failed to develop or implement effective preventative internal controls** that would have detected or prevented misstatements in the financial and performance information, non-compliance and significant losses. There was a lack of the skills required to accurately apply the relevant accounting standards. There was also no commitment to daily and monthly controls such as document management, proper independent review of work performed, reconciliations, asset verifications, and periodic reporting.

The municipalities seem to have accepted the gaps in the control environment and, rather than addressing them, procured the services of consultants to assist with the responsibilities of the chief financial officers and finance personnel. Despite all chief financial officer positions having been filled, and finance unit salary costs amounting to R251,9 million, municipalities still spent R63,7 million on procuring the skills for financial reporting. After we had completed seven more audits after the cut-off date of this report, the total finance unit salary cost increased to R667,7 million and the total cost for consultants to R112,5 million. However, due to the weak controls around record and document management, as well as a lack of commitment from management, consultants did not bring any sustainable improvement to the outcomes.

Emakhazeni continued to rely on consultants, and paid R2,8 million to have them do bank reconciliations, assist with managing the asset register and prepare financial statements, despite having individuals employed in the finance unit to do so. Management did not perform adequate reconciliations during the year, which resulted in unexplained differences between the financial statements and the municipality's accounting records. The accounting officer also tasked consultants with preparing value-added tax returns. The consultants proposed that management use journals to correct errors; however, since management did not process the journals, the external audit process picked up the same material errors.

The provincial treasury continued to provide support with budget, revenue and debt management, as well as by implementing financial recovery plans at financially distressed municipalities and training bid committees, disciplinary boards and municipal public accounts committees. They were also available during the audit process to provide technical guidance to municipalities. The provincial cooperative governance department continued to offer support in building capacity, aligning the service delivery and budget implementation plan with the integrated development plan, implementing back-to-basics initiatives, addressing community concerns, and maintaining functional committees. Unfortunately, this support did not yield its intended benefits, mainly because of the systemic challenges around internal control environments and the instability at some municipalities.

The financial health of most municipalities in the province continued to deteriorate despite our consistent message in prior years calling on the executive authority and provincial leadership to attend to the financial crisis. Consequently, some municipalities did not achieve their service delivery indicators and targets, which negatively affected citizens' quality of life. The province has also seen a new trend, observed at two municipalities (five if we include audits finalised after the cut-off date for this report), where the respective councils approved unfunded budgets for the financial year under review. At the time of budget approval, the municipalities expected their budgeted expenditure of R1,6 billion to exceed their projected revenue of R1,4 billion. These amounts increase to R9,3 billion and R7,9 billion, respectively, when we include the audits signed off after the cut-off date. This was already an indicator that the projected financial resources were not adequate to achieve the planned priorities. This resulted in operating losses of R142 million (R691,8 million if we include audits that were subsequently signed off), the under-achievement of some service delivery targets, and unauthorised expenditure of R372,1 million (R1,1 billion if we include audits that were subsequently signed off).

Adding to the unfunded budget crisis is municipalities' inability to accurately bill for the sale of basic services. During the 2019-20 financial year, the 11 municipalities covered in this report billed a total of R4,7 billion from the sale of basic services and property rates. This amount increases to R9,9 billion if we include the seven audits that we signed off after the cut-off date. The challenges around the billing system undermined the credibility of these amounts, resulting in eight municipalities being qualified on the inadequacy of controls around the billing function. As an example, Emakhazeni struggled with revenue billing – the municipality issued negative billings to customers, billed developed properties as vacant, did not bill some properties according to their classification in the valuation roll, and billed some properties that we could not trace to the valuation roll. The municipality also did not bill service charges (water, electricity and refuse) for some accounts and for some months, and did not charge interest on late accounts for six months in the financial year under review. All of this took away from potential revenue that would have contributed to funding the budget.

Municipalities also faced significant challenges with debt collection, as only R1,5 billion of the R7,3 billion balance of receivables from the sale of basic services and property rates was recoverable at the end of the 2019-20 financial year. If we consider the seven audits that were signed off after the cut-off date, the picture gets even worse, with only R4,6 billion of the total balance of such receivables of R14,8 billion being considered recoverable. Poor debt collection led to municipalities having limited cash flow to pay for their operations. Thus, municipalities took an average of 279 days to pay their suppliers, attracting interest of R327,3 million, mostly on Eskom accounts. This amount, which increases to R837,9 million when we include the seven audits that were signed off after the cut-off date, resulted in fruitless and wasteful expenditure. Consequently, we issued seven material irregularity notifications to the accounting officers at four municipalities relating to interest incurred due to not paying suppliers within 30 days or the agreed time frames.

Leakages due to unmaintained and deteriorating infrastructure, unmetered consumption and illegal connections crippled an already strained financial system. This resulted in municipalities suffering significant water and electricity losses.

As at 30 June 2020, the municipalities on which we report had creditors amounting to R6 billion and cash of only R1,3 billion. These figures increase to R15,1 billion and R1,8 billion, respectively, if we take into account the seven audits signed off after the cut-off date. The available cash at year-end could not settle the current municipal debt, which means that the next year's budget will have to finance the existing debt, jeopardising the municipalities' ability to realise the next year's priorities.

Limited progress has been made at the municipalities that the province put under its mandatory intervention three years ago, in terms of section 139(1)(a) of the Municipal Finance Management Act. The provincial cooperative governance department and the provincial treasury assisted the municipalities with developing and implementing financial recovery plans. However, this did not bring about any improvements, mainly due to weaknesses in the billing system and a lack of commitment by municipal leadership and management to respond appropriately to the weaknesses.

The management and monitoring of infrastructure projects was ineffective. A total of R1,5 billion in conditional grants (R2,8 billion if we include the seven subsequently completed audits) for infrastructure development was allocated to municipalities. However, accounting officers did not effectively monitor the related spending and performance of contractors in order to derive the intended efficiencies and quality. This indicated that the project management units did not function as expected. At Emakhazeni, we identified deficiencies in the project for the phased closure and rehabilitation of the existing waste disposal site and the commissioning of a waste disposal site at Belfast, valued at R16,5 million. After conducting a site visit, we noted project deficiencies such as overclaiming certain items on the payment certificate, items claimed in excess of the bills of quantities, quantities paid but not found on site, and overpayments for fencing materials and installation.

The deficiencies translated into fruitless and wasteful expenditure of R4,7 million. Although the contractor had completed the project at year-end, the landfill site had not yet been decommissioned and quality defects had not been corrected, leading to waste being dumped illegally. The municipality will incur additional costs to remove the illegally dumped waste from the site, which could have been avoided had the implementation of the infrastructure project been adequately monitored.

Due to **non-adherence to laws and regulations as well as a lack of consequences,** the province continued to struggle with preventing unauthorised, irregular and fruitless and wasteful expenditure. Municipalities procured some goods and services without adhering to relevant supply chain management legislation, which contributed to the irregular expenditure balance. The province has yet to deal with a high balance of R3,5 billion in irregular expenditure, of which R874,9 million related to the current year. This balance increases to R5,4 billion (of which R1,3 billion relates to the current year) if we take into account the seven audits subsequently finalised.

Most municipalities do not have controls to enable adherence to the relevant legislation, let alone to detect any non-adherence. The covid-19 pandemic also put a spotlight on the weak controls around procurement processes. This was evident at four municipalities (eight if we take into account those audits subsequently completed) that were not able to accurately account for their irregular expenditure amounts and that had irregular expenditure as one of the modification paragraphs in their audit reports as a result. While we continued to report on the non-adherence that gave rise to undesirable expenditure, some councils did not investigate the unauthorised, irregular and fruitless and wasteful expenditure reported in prior years. In most instances where councils had investigated such expenditure, they had concluded that no one was liable. While we acknowledge the effort that the councils are starting to put in to address the unauthorised, irregular and fruitless and wasteful expenditure balances, we remain concerned that the process might be superficial, as most of these investigations are not resulting in any consequences being implemented.

Because of the internal control weaknesses highlighted above, only three municipalities improved their audit outcomes for the 2019-20 financial year. Even after taking into account the audits that we signed off after the cut-off date, this number increases to only four. The improvement speaks to the four municipal managers and their teams, who committed to strengthening the internal controls within their municipalities. Two of these municipalities (Ehlanzeni District and Steve Tshwete) reclaimed their clean status. They generally had strong controls but battled with compliance matters, which they managed to address during the year under review. For that reason, and due to the increased number of disclaimed and adverse audit opinions over the past four years, we acknowledge the overall improvement with reservations.

All of these challenges indicate that a culture of 'doing things right' is not embedded at most of the municipalities. Despite the improvement we have seen this year at some of the municipalities, most of the financial and performance reports submitted for auditing were of a poor quality. The financial health of the province's local government continues to worsen. The provincial treasury and provincial cooperative governance department, working with the municipal managers, need to perform a proper analysis to identify the systemic challenges that municipalities face, and then develop a practical intervention strategy that will address the gaps and ensure sustained improvement.

Our message, which is similar to the one we have delivered in prior years, is a call for provincial leadership to take urgent action to restore the failed accountability, as only this will bring about the desired change.

A need for leadership to act on accountability to bring about the desired change

6.7 NORTHERN CAPE

PERFORMANCE SNAPSHOT

The snapshot shows the audit outcomes of 20 municipalities in the province. With the exception of unauthorised, irregular and fruitless and wasteful expenditure, the outcomes of the outstanding audits are not included in the snapshot.

Overall audit outcomes

3 | 6 | 10 | 1 | 11

MOVEMENT

FROM 2018-19: 6 improved, 1 regressed

OVER 4 YEARS: 6 improved, 5 regressed

JOHN TAOLO

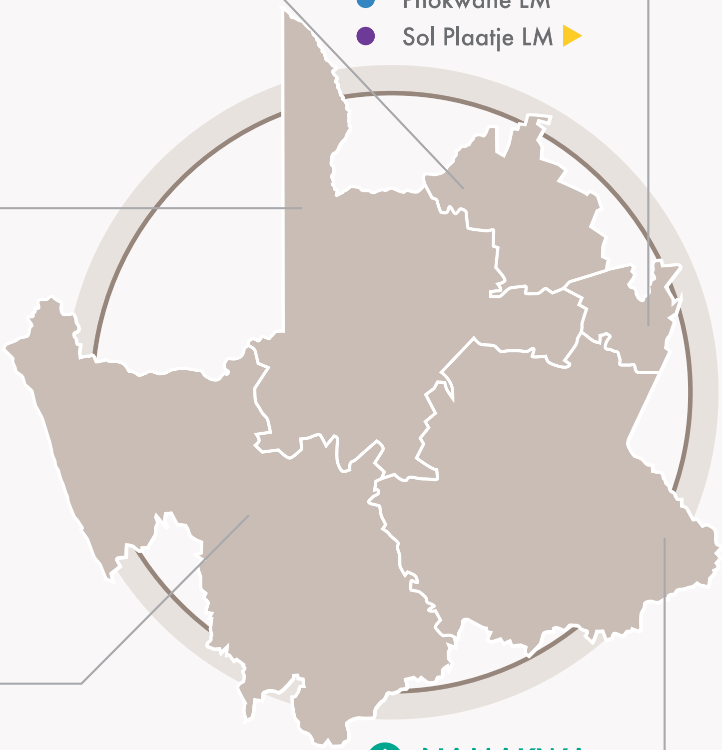
1 | 1 | 1 | 1

- John Taolo Gaetsewe DM ▶
- Gamagara LM ▶
- Ga-Segonyana LM ▲
- Joe Morolong LM

FRANCES BAARD

1 | 2 | 2

- Frances Baard DM ▲
- Dikgatlong LM ▲
- Magareng LM
- Phokwane LM
- Sol Plaatje LM ▶



ZF MGCAWU

1 | 1 | 1 | 3

- ZF Mgcawu DM ▲
- !Kheis LM
- Dawid Kruiper LM ▶
- Kai !Garib LM ▶
- Kgatelopele LM
- Tsantsabane LM

PIXLEY KA SEME

2 | 4 | 3

- Pixley ka Seme DM ▶
- Emthanjeni LM ▶
- Kareeberg LM ▶
- Renosterberg LM
- Siyancuma LM ▼
- Siyathemba LM ▶
- Thembelihle LM ▶
- Ubuntu LM
- Umsobomvu LM

NAMAKWA

2 | 3 | 2

- Namakwa DM
- Hantam LM ▶
- Kamiesberg LM ▲
- Karoo Hoogland LM ▲
- Khai-Ma LM ▶
- Nama Khoi LM ▶
- Richtersveld LM

Metropolitan municipality | District | DM District municipality | LM Local municipality | ▲ Improved | ▶ Unchanged | ▼ Regressed

Unqualified with no findings | Unqualified with findings | Qualified with findings | Adverse with findings | Disclaimed with findings | Outstanding audits

Financially unqualified financial statements

45% (9) 2018-19: 40% (8)

Financial statements submitted without material misstatements **15% (3)**

No material findings on performance report

47% (8) 2018-19: 29% (5)

Reported achievement reliable **62% (8)**

No material findings on compliance with legislation

15% (3) 2018-19: 5% (1)

Findings on compliance with supply chain management legislation at 100% of municipalities where audits had been completed

Material irregularities (MIs)

Notified by 11 June 2021

3 MIs with estimated financial loss of **R12,1m** at **3 municipalities** and likely substantial harm to public sector institution at **2 municipalities** with repeat disclaimers

NATURE	
Eskom not paid on time, resulting in interest	3
Substantial harm to public sector institution (based on repeat disclaimer)	2

Unauthorised & fruitless and wasteful expenditure

Unauthorised expenditure **R836,3 m**

Fruitless and wasteful expenditure **R184,39 m**

Irregular expenditure

R810,71 m

2018-19: R771,38 m

Closing balance

R1 926,9 m

2018-19: R2 414,11 m

TOP THREE CONTRIBUTORS	
Sol Plaatje	R258,03 m
Gamagara	R135,69 m
Hantam	R59,87 m

Use of financial reporting consultants

R99,04 m – 17 municipalities

2018-19: R37,34 m – 17 MUNICIPALITIES

Recurring use of consultants at 100% of municipalities

TOP THREE SERVICES	
Financial statements review/preparation	R41,8 m
Asset management	R21,3 m
Other financial reporting services	R16,9 m

Financial health indicators

Going concern uncertainty	55% (11)
Deficit	R116,87 m (6)
Average creditor-payment period	350 days
Eskom and water boards' debt in arrears	R1 210,69 m (11)
Creditors > cash available at year-end	74% (14)
Average municipal debt not recoverable	58% (18)
Average debt-recovery period	228 days

PROVINCIAL OVERVIEW

Each province has a unique story...

The benefits derived from implementing preventative controls are evident, but there is still a lot to be done to address undesirable audit outcomes

In our previous year's message, we emphasised that the province was in a prolonged state of undesirable audit outcomes, with six regressions and three improvements reported for that year. We urged political and administrative leadership to focus on putting appropriate preventative control measures in place, respond to the lack of capacity in critical positions, improve on the assurance provided by internal audit units and audit committees, and ensure strong accountability to ensure better audit outcomes.

It is encouraging that some of these recommendations were responded to and that this contributed to the overall improvement in audit outcomes for the province. Another contributing factor to the improvement was the revival of the operation clean audit committee driven by the premier. The tone from the premier in improving audit outcomes has played a key role in ensuring that municipal leadership and staff take the audit process seriously. This was evident in the definite improvement in the responses from management and leadership during the audit process.

We further noted that our recommendations on strengthening internal controls and effecting consequences were implemented by some accounting officers and those providing oversight of the respective municipalities. **Where municipalities implemented consequences and are holding their officials accountable, audit outcomes improved and a clean audit status was maintained.** However, the province still has a long way to go in implementing strong accountability at the rest of the municipalities.

Although the audit outcomes improved in the current year, the poor state of internal controls at many municipalities raises questions about the sustainability of the improvements. Sustaining improved audit outcomes is only possible if they are based on a strong internal control environment characterised by regular monitoring and review as well as leadership holding staff accountable for their actions. The state of internal controls relating to the areas of leadership as well as financial and performance management further indicate that the province will struggle to maintain the current audit status, thus limiting the opportunity for further improvement if this fundamental matter is not attended to. We therefore urge oversight, both at municipal and provincial level, to continue ensuring that accounting officers strengthen preventative controls. The prevention and detection of irregular expenditure continues to be a key aspect that accounting officers should pay particular attention to.

Furthermore, **we remain extremely concerned about the status of compliance with legislation.** Almost all municipalities were plagued by findings on non-compliance and we are particularly worried about the fact that 85% of municipalities had findings on the quality of financial statements submitted for auditing. This confirms that municipalities are still relying on the audit process to identify material misstatements that need to be corrected. Six municipalities achieved unqualified opinions only because they corrected all misstatements identified during the audit. Additionally, we raised findings on supply chain management in all our audits. This is concerning as experience has shown that clean audits can regress when recurring compliance findings become material.

The financial health of municipalities in the province remained in a dire state, with more than half being in a vulnerable financial position. More than half are also operating with an unfunded budget, meaning that they commit more than they can generate in revenue and, as a result, fail to pay their creditors. The impact of this is clear from the large arrear amounts pertaining to Eskom and the water boards, which then resulted in significant interest charges. The adoption of unfunded budgets not only poses an imminent threat to the sustainability of municipalities, but also affects their ability to deliver services.

We would like to congratulate the **three municipalities** (Frances Baard, John Taolo Gaetsewe and ZF Mgcawu) that **obtained clean audits.** They took our previous year's message on the importance of preventative controls to heart and put appropriate actions in place to prevent material audit findings. While obtaining a clean audit remains a significant achievement for any auditee, we want to clarify the relationship between clean audits and service delivery.

A clean audit is merely a building block towards good service delivery and should not be seen as a measure of how well services are being delivered. An accurate and complete annual performance report may be a good source of information pertaining to the real state of service delivery at a municipality. In this regard, we noted that more than half of the municipalities in the province had material findings on their performance reports, casting doubt on the usefulness and reliability of these reports.

The rise in the cost of using consultants to, for example, prepare financial statements and update asset registers is concerning. Our concern is not the use of consultants itself, but rather that the province is not receiving a return on investment, as most municipalities (82%) that used consultants had material misstatements in the area of the consultants' responsibility. In addition, 10 of the 17 municipalities (59%) that used consultants still had either a disclaimed or a qualified opinion. All 17 municipalities indicated the reason for using consultants as a lack of skills. Both provincial and municipal oversight thus need to take cognisance of the critical need to employ skilled individuals at municipalities across the province.

We continued to support local government through our status-of-records reviews at selected municipalities and engagements with stakeholders at various levels, and by identifying findings and providing recommendations to assist in responding to the findings. We also continued to implement our extended powers following the amendment of the Public Audit Act and implemented these amendments at six municipalities.

The material irregularity raised at Ga-Segonyana in the previous year, was closed in the current year after the municipality provided additional information. In the current year, we raised five material irregularities and notified the relevant accounting officers of them. The irregularities related to interest payments to suppliers, resulting in fruitless and wasteful expenditure; as well as to causing substantial harm to a public sector institution, based on receiving a repeat disclaimed opinion. In addition, we are currently assessing four potential material irregularities. One of these also relates to interest payments to suppliers resulting in fruitless and wasteful expenditure; one to losses due to the non-billing of customers; one to the disposal of municipal property without following the appropriate process; and one to possible losses due to fraudulent payments. We **encourage the accounting officers** at the relevant municipalities to take the necessary action on the material irregularities raised and **to do everything in their power to build an environment that is free from material irregularities.**

In conclusion, we again recognise the benefits to be derived from implementing preventative controls, but acknowledge that there is still a lot to be done to address undesirable audit outcomes. Best practices at municipalities that achieved clean audits should be replicated throughout the province, while the efforts of the operation clean audit committee should be continued and further enhanced.

Sustainable change starts with the leadership will to drive it

6.8 NORTH WEST

PERFORMANCE SNAPSHOT

The snapshot shows the audit outcomes of 10 of the 22 municipalities in the province. With the exception of unauthorised, irregular and fruitless and wasteful expenditure, the outcomes of the outstanding audits are not included in the snapshot.

Overall audit outcomes

1 | 6 | 3 | 12

MOVEMENT

FROM 2018-19: 2 improved, 0 regressed

OVER 4 YEARS: 3 improved, 3 regressed

NGAKA MODIRI MOLEMA

2 | 1 | 3

- Ngaka Modiri Molema DM
- Ditsobotla LM
- Mahikeng LM ▲
- Ramotshere Moiloa LM
- Ratlou LM ▶
- Tswaing LM ▶

BOJANALA

2 | 4

- Bojanala DM
- Kgetlengrivier LM
- Madibeng LM
- Moretele LM ▶
- Moses Kotane LM ▶
- Rustenburg LM

DR RUTH S MOMPATI

1 | 1 | 4

- Dr Ruth S Mompati DM ▶
- Greater Taung LM
- Kagisano-Molopo LM ▶
- Lekwa Teemane LM
- Mamusa LM
- Naledi LM

DR KENNETH KAUNDA

1 | 1 | 1 | 1

- Dr Kenneth Kaunda DM ▲
- JB Marks LM ▶
- Matlosana LM
- Maquassi Hills LM ▶

Metropolitan municipality | District | DM District municipality | LM Local municipality | ▲ Improved | ▶ Unchanged | ▼ Regressed

Unqualified with no findings | Unqualified with findings | Qualified with findings | Adverse with findings | Disclaimed with findings | Outstanding audits

Financially unqualified financial statements

10% (1) — 2018-19: 0% (0)

Financial statements submitted without material misstatements — 0% (0)

No material findings on performance report

10% (1) — 2018-19: 0% (0)

Reported achievement reliable — 10% (1)

No material findings on compliance with legislation

0% (0) — 2018-19: 0% (0)

No findings on compliance with supply chain management legislation — 0% (0)

Material irregularities (MIs)

Notified by 11 June 2021

17 MIs with estimated financial loss of **R451 m** at **7 municipalities** and likely substantial harm to public sector institution at **8 municipalities** with repeat disclaimers

NATURE	
Investments and assets	R308 m (6)
Interest and penalties	R94 m (6)
Revenue management	R33 m (1)
Procurement and payments	R16 m (4)

Unauthorised & fruitless and wasteful expenditure

Unauthorised expenditure **R2 603 m**

Fruitless and wasteful expenditure **R422 m**

Irregular expenditure

R4 171 m

2018-19: **R5 421 m**

Closing balance

R25 510 m

2018-19: **R21 596 m**

TOP THREE CONTRIBUTORS	
Moses Kotane	R624 m
Dr Ruth S Mompati District	R366 m
JB Marks	R345 m

Use of financial reporting consultants

R123 m – 10 municipalities

2018-19: **R93 m – 10 MUNICIPALITIES**

Recurring use of consultants at 80% of municipalities

TOP THREE SERVICES	
Asset management	R39 m
Financial statements preparation	R37 m
Tax services	R24 m

Financial health indicators

Going concern uncertainty	50% (5)
Deficit	R127 m (3)
Average creditor-payment period	308 days
Eskom and water boards' debt in arrears	R1 025 m (6)
Creditors > cash available at year-end	86% (6)
Average municipal debt not recoverable	79%
Average debt-recovery period	205 days

PROVINCIAL OVERVIEW

Each province has a unique story...

Total neglect of internal control disciplines, resulting in financial and operational collapse, weakened governance and lack of accountability

In our previous report, we shared our insights with the political and administrative leadership of municipalities. We attempted to simplify the root causes and drivers underpinning the poor audit outcomes to enable the provincial leadership to address and improve accountability and the audit outcomes. We also emphasised the systemic breakdown in the disciplines of financial controls, which required urgent attention. Our call to action was that leadership should pay attention to the lack of discipline to submit quality financial statements by the legislated deadline. We urged them to attend to the persistent use of consultants for financial reporting without any improvement in the quality of the financial statements. We elevated our concerns around the ineffective governance structures, including the lack of political will and support for provincial interventions. We concluded our call to action by emphasising that there was a dire need to prevent non-compliance with supply chain management prescripts. This included attending to financially distressed districts, as their role affects service delivery and the maintenance of operations. The leadership was unresponsive, which led to poor audit outcomes over a period of four years that are underpinned by similar root causes. These audit outcomes reflect a total neglect of internal control disciplines, and have resulted in a financial and operational collapse, weakened governance and a lack of accountability.

The non-responsiveness is evident in the regression of audit outcomes and submission of financial statements over the four-year period. We completed the 2019-20 audits of only 10 of the 22 municipalities by the cut-off date for inclusion in this report. This was primarily due to the late submission of financial statements, with only 55% of municipalities submitting their financials on time, which is the same percentage as in 2018-19. This is in sharp contrast to 2016-17 when all municipalities submitted financial statements by the legislated date. By 16 May 2021, we had finalised and signed off five additional audit reports; however, the outcomes of all five of those municipalities remained unchanged from the previous year, with four being disclaimed opinions and one a qualified opinion. This regression in audit outcomes and the rate of non-submission of financial statements show a deterioration in accountability and transparency. Therefore, **leadership's persistent lack of responsiveness and non-implementation of preventative controls require urgent attention.**

In the current-year, the money spent on consultants at 10 municipalities increased to R122,9 million from R93,2 million in the previous year, while the salary bill of the finance units amounted to R168 million. **The use of consultants was a futile exercise as it yielded no tangible value** due to the prevailing issues of proper governance structures not being instituted, poor control environments, persistent lack of proper record keeping, and a disregard for in-year control activities. This has resulted in municipalities continuing to rely on the audit process to identify and correct errors in the financial statements. The accounting officers will have to examine the root causes of this wastage, which would ensure that consultants are used in conducive environments where financial control activities allow, and there is adequate support and transfer of skills. This will require key positions to be filled, as well as stability at senior management level.

The financial health of municipalities remains a concern, with 57% of municipalities being insolvent and unable to meet their financial obligations as they fall due. This is evident at the 60% of municipalities that implemented unfunded budgets due to financial challenges. Concerns remain regarding the inability to implement and manage credit control and debt collection, which resulted in an average of 79% of all billings being impaired. Consequently, critical suppliers such as Eskom and water boards (as well as us as external auditors) are not paid in a timely manner. In certain instances, municipalities are struggling to pay statutory deductions and benefits because of cash-flow challenges. Municipalities are dependent on the equitable share allocations, most of which go towards paying salaries, leaving these financially distressed municipalities with minimal funds for service delivery. The provincial treasury will have to assist the municipalities with revenue-enhancement strategies and budgetary control initiatives, where applicable.

The **lack of funds for service delivery** is most evident in the ever-increasing backlog in the maintenance required to keep infrastructure operational, which has led to these assets being in a dilapidated state at most municipalities. This **has caused significant water and electricity distribution losses at municipalities and had a detrimental impact on the environment.** A follow-up of the environmental impact study performed at 118 water and wastewater treatment plants, infrastructure and landfill sites in the province showed a distinct shift from fair or concerned assessments to operating systems and processes that are in a critical state or that have collapsed. Sites that are in a dire state or on the verge of collapse must be given urgent attention to ensure continued basic service delivery.

Unauthorised, irregular and fruitless and wasteful expenditure incurred by municipalities is gradually increasing each year. The unresolved balance of irregular expenditure now amounts to R25,5 billion due to the culture of non-compliance with procurement and contract prescripts. Most of the municipalities did not take appropriate action to investigate, recover or write off irregular expenditure incurred during prior years. To redress this, the new political leadership must guard against political fluidity and infighting, and must adequately capacitate council committees to ensure robust and timely investigations and consequences against responsible individuals.

The amendments to the Public Audit Act were implemented at seven municipalities during 2019-20, in environments where there is already severe pressure on available resources and cash flow. **Municipalities cannot afford to make investments that cannot be withdrawn, to have assets vandalised or stolen, or to incur penalties and interest charges** on amounts owed to suppliers. Despite this, we notified accounting officers of 14 new material irregularities during the year, in addition to the three raised in the previous year. Most of the material irregularities related to VBS Mutual Bank investments, asset management losses as well as interest and penalties paid. The accounting officers were not very responsive to this process and, in some cases, did not respond to the notifications at all. Where commitments were made, as in the case of the three material irregularities at Ngaka Modiri Molema in the previous year, these were not implemented, which resulted in further losses because of the same matters recurring in the current year. The nature of the irregularities supports the key message on the deteriorating state of affairs in local government. The non-compliance that resulted in these material irregularities must be given attention and addressed across local government, as it is also prevalent at other municipalities in the province. In addition, the executive authorities and oversight structures should hold the accounting officers accountable to ensure that swift action is taken to resolve these material irregularities and prevent them from recurring.

In the previous report, we noted inconsistencies and a lack of clarity on the roles and responsibilities of the appointed administrators as one of the root causes of the section 139 interventions not bearing fruit. While the member of the executive council for cooperative governance has addressed the issue, the lack of acceptance of the interventions by political leadership resulted in these initiatives having little impact. In certain instances, there were no close-out reports for any of the interventions, and we have not seen a change in the state of the municipalities as a result of these interventions. For sustainable solutions, the councils should focus on making sure that there are competent accounting officers in place at all municipalities and then hold them accountable to turn around the sorry state of financial and performance management, as is required of them in terms of the Municipal Finance Management Act. It is encouraging that the members of the executive council for finance and for cooperative governance have indicated that they will intensify their support to municipalities in terms of section 154(1) of the Constitution in an attempt to improve financial reporting and management challenges at municipalities, as section 139 has not achieved the desired impact.

We reiterate the need for the provincial and the incoming local government leadership to focus on implementing preventative controls, with governance structures insisting on in-year preparation and submission of accountability reports. New councils must set a leadership tone that is exemplary and must implement corrective action and consequences where required. To bring about accountability, leadership must be aligned and actively lead.

To bring about accountability, leadership must be aligned and actively lead

6.9 WESTERN CAPE

PERFORMANCE SNAPSHOT

The snapshot shows the audit outcomes of 23 municipalities in the province. With the exception of unauthorised, irregular and fruitless and wasteful expenditure, the outcomes of the outstanding audits are not included in the snapshot.

Overall audit outcomes

14 | 9 | 7

MOVEMENT

5 | 2 FROM 2018-19

2 | 4 OVER 4 YEARS

WEST COAST

2 | 2 | 2

- West Coast DM
- Bergrivier LM
- Cederberg LM
- Matzikama LM
- Saldanha Bay LM
- Swartland LM

CENTRAL KAROO

2 | 2

- Central Karoo DM
- Beaufort West LM
- Laingsburg LM
- Prince Albert LM

CAPE WINELANDS

5 | 1

- Cape Winelands DM
- Breede Valley LM
- Drakenstein LM
- Langeberg LM
- Stellenbosch LM
- Witzenberg LM

CITY OF CAPE TOWN METRO

1

OVERBERG

4 | 1

- Overberg DM
- Cape Agulhas LM
- Overstrand LM
- Swellendam LM
- Theewaterskloof LM

GARDEN ROUTE

1 | 5 | 2

- Garden Route DM
- Bitou LM
- George LM
- Hessequa LM
- Kannaland LM
- Knysna LM
- Mossel Bay LM
- Oudtshoorn LM

Metropolitan municipality | District | DM District municipality | LM Local municipality | Improved | Unchanged | Regressed

Unqualified with no findings | Unqualified with findings | Qualified with findings | Adverse with findings | Disclaimed with findings | Outstanding audits

Financially unqualified financial statements

100% (23) 2018-19: 100% (23)

Financial statements submitted without material misstatements 96% (22)

No material findings on performance report

91% (21) 2018-19: 83% (19)

Reported achievement reliable 91% (21)

No material findings on compliance with legislation

65% (15) 2018-19: 48% (11)

No findings on compliance with supply chain management legislation 30% (7)

Material irregularities (MIs)

Notified by 24 May 2021

2 MIs with estimated financial loss of **R9 m** at **1 municipality**

NATURE	
Payments for services not received	1
Overpricing of goods and services procured	1

Unauthorised & fruitless and wasteful expenditure

Unauthorised expenditure **R195 m**

Fruitless and wasteful expenditure **R10 m**

Irregular expenditure

R1 407 m

2018-19: **R2 692 m**

Closing balance

R2 660 m

2018-19: **R3 337 m**

TOP THREE CONTRIBUTORS	
City of Cape Town Metro	**R669 m**
Bitou	**R119 m**
Matzikama	**R100 m**

Use of financial reporting consultants

R30 m – 20 municipalities

2018-19: **R29 m – 17 MUNICIPALITIES**

Recurring use of consultants at 79% of municipalities

TOP THREE SERVICES	
Financial statements review/preparation	**R22 m**
Asset management	**R3 m**
Accounting services	**R2 m**

Financial health indicators

Going concern uncertainty	**0% (0)**
Deficit	**R18 m (3)**
Average creditor-payment period	**59 days**
Eskom and water boards' debt in arrears	**R74 m (5)**
Creditors > cash available at year-end	**13% (3)**
Average municipal debt not recoverable	**51%**
Average debt-recovery period	**51 days**

PROVINCIAL OVERVIEW

Each province has a unique story…

Good financial accounting controls but inadequate preventative controls on compliance

In our 2018-19 message, we highlighted three broad categories of municipalities within the province. They were (1) those where controls are institutionalised, (2) those that are reactive or susceptible to change, and (3) those with dysfunctional control environments with a weak leadership tone at the top. Recommendations were based on the category into which municipalities had been classified. All municipalities should ultimately strive to attain levels where control environments and robust risk-assessment processes are institutionalised – with clean audits as a by-product.

Despite difficult circumstances, nine municipalities were able to sustain their clean audit outcome while five improved to a clean audit status. These municipalities heeded our request to self-assess, as embedded in the previous year's status-of-records reviews. Our recommendations to institutionalise preventative controls were also taken to heart and cultivated an environment of good governance and clean administration, which formed the foundation to drive service delivery.

In addition, clean audit outcomes were achieved where:

- internal control environments were continually strengthened, institutionalised, preventative in nature and reinforced by a strong tone set by leadership, resulting in fewer deficiencies reported
- the financial statements and performance report submitted for auditing were of a good quality and free from material misstatements
- implemented action plans were credible in that audit findings identified in one year were generally addressed in the following year.

The current provincial picture is, however, slightly distorted due to the seven outstanding audits. A complete reflection will only emerge once these audits have been finalised. The main drivers contributing to the outstanding audits were the effects of covid-19, specifically the second wave, which caused delays in the audit process; and audit findings that were disputed and required further technical deliberations and consultation with the National Treasury.

From a financial health perspective, it is extremely positive that none of the municipalities reported on were in a financially vulnerable position. It is also encouraging that unauthorised expenditure decreased from R434 million in 2018-19 to R195 million in 2019-20. This decrease was underpinned by strong budgeting processes (particularly when budgeting for non-cash items) and effective expenditure control relative to budgets.

While none of the municipalities were in a financially vulnerable position, we have some concerns with regard to the financial sustainability of municipalities. On average, 51% of the revenue due to municipalities for services rendered was deemed to be irrecoverable. The non-collection of money for services rendered can have a negative impact on the longer term financial sustainability of municipalities and their ability to settle obligations. It furthermore contributed to the overall increase in the number of municipalities with unfavourable financial health indicators over the last year.

The material irregularity process was expanded in the period under review to include a further six municipalities in addition to the City of Cape Town Metro. At the time of finalising the audit reports, no material irregularity notifications had been issued. Two material irregularity notices were issued to the City of Cape Town subsequent to the audit report being finalised. These irregularities related to one contract where payments were made for services not received as well as payments for goods and services that were in excess of the rates stipulated in the contract.

While there has been an improvement in the audit outcomes, only some of our recommendations from the previous year were implemented. **Work is still required on the implementation of sound preventative controls in the area of compliance with laws and regulations,** especially relating to procurement and contract management. Although irregular expenditure decreased from R2,6 billion in 2018-19 to R1,4 billion in 2019-20, we remain concerned about the findings raised on contract and supply chain management and the resultant irregular expenditure at the majority of municipalities, as past experience has shown that even clean municipalities are susceptible to regressions when recurring compliance findings become material.

Factors that contribute to the continued reporting of supply chain management findings include the following:

- Municipalities considering procurement legislation to be onerous with many requirements to be complied with and differences in the interpretation of prescripts in some instances.
- The attitude of management in that they believe compliance with all legislative prescripts stifles their ability to deliver services efficiently and effectively.
- Compliance controls failing due to human error or omission.

Although the quality of performance reports improved from 2018-19, it remains concerning that some municipalities again submitted performance reports that contained material misstatements. Two of these municipalities were unable to correct the material misstatements during the audit process. These misstatements were due to corrective action not being implemented to address the control weaknesses identified, a lack of standard operating procedures, and inadequate reviews resulting in differences between the performance reported and the relevant supporting documentation.

Municipalities that were able to maintain their clean audit outcomes for two or more consecutive years are encouraged to continue focusing on the maintenance and improvement of their control environments, inclusive of robust risk assessments to maintain compliance with laws and regulations. Municipalities that were not able to attain this level should implement action plans to improve their control environments as well as design and implement controls that are preventative in nature.

Generally, accounting officers and mayors provided the required level of assurance by instilling an effective leadership culture and oversight. At senior management level there is room for improvement, as the majority of senior managers were rated as providing only some assurance as a result of non-material findings at clean auditees and material findings at other municipalities.

The area of supply chain management and the resultant irregular expenditure must be given increased attention by proactively addressing the issues identified, thereby reducing non-compliance and such unwanted expenditure.

The premier in conjunction with the coordinating provincial local government department and provincial treasury should continue with their oversight roles through the municipal governance review outlook processes and other initiatives aimed at achieving clean administration across the province. **Extra effort and intervention are required at Beaufort West, Kannaland and Laingsburg,** which had been previously categorised as municipalities with control environments that are dysfunctional as their audit outcomes remained the same or regressed.

We remain committed to support all institutions in the drive to embed preventative controls and good governance as a culture in the province.

Improvement but concerns remain

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