



A U D I T O R - G E N E R A L

**Report of the Auditor-General
to the Western Cape Provincial
Parliament on the Financial
Statements and Performance
Information of the City of Cape
Town**

**FOR THE YEAR ENDED
30 JUNE 2007**

**REPORT OF THE AUDITOR-GENERAL TO THE WESTERN CAPE PROVINCIAL
PARLIAMENT ON THE FINANCIAL STATEMENTS AND PERFORMANCE
INFORMATION OF THE CITY OF CAPE TOWN FOR THE YEAR ENDED 30
JUNE 2007**

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the City of Cape Town which comprise the statement of financial position as at 30 June 2007, statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, and the accounting officer's report, as set out on pages 4 to 52.

Responsibility of the accounting officer for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the basis of accounting determined by the National Treasury as set out in accounting policy note 1 and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA). This responsibility includes:
 - designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
 - selecting and applying appropriate accounting policies
 - making accounting estimates that are reasonable in the circumstances.

Responsibility of the Auditor-General

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996, read with sections 4 and 20 of the Public Audit Act, 2004 (Act No. 25 of 2004), my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with the International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

6. An audit also includes evaluating the:
 - appropriateness of accounting policies used
 - reasonableness of accounting estimates made by management
 - overall presentation of the financial statements.
7. Paragraph 11 et seq. of the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of financial statements* requires that financial reporting by entities shall provide information on whether resources were obtained and used in accordance with the legally adopted budget. As the budget reporting standard is still in the process of being developed, I have determined that my audit of any disclosures made by the City of Cape Town in this respect will be limited to reporting on non-compliance with this disclosure requirement.
8. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Basis of accounting

9. The municipality's policy is to prepare financial statements on the basis of accounting determined by the National Treasury, as set out in accounting policy note 1.

Opinion

10. In my opinion the financial statements present fairly, in all material respects, the financial position of the City of Cape Town as at 30 June 2007 and its financial performance and cash flows for the year then ended, in accordance with the basis of accounting determined by the National Treasury, as set out in accounting policy note 1 and in the manner required by the MFMA.

Emphasis of matters

Without qualifying my audit opinion, I draw attention to the following matters:

Highlighting a matter affecting the financial statements

11. As set out in accounting policy note 1, the Minister of Finance approved a deviation from the basis of accounting applicable to the municipality in terms of *General Notice 552 of 2007*, issued in *Government Gazette No. 30013 of 29 June 2007*.
12. In the financial year under review the gross outstanding consumer debtors balance as at 30 June as disclosed in note 18 on page 31 of the financial statements, has decreased from R5,084 billion in 2006 to R4,083 billion in 2007, after writing off debt amounting to R1,296 billion as irrecoverable during the year under review. This represented a growth in the debtors balance of 6,5% (2006: 12%) reflected by an increase in debtors days' if the bad debt write off is disregarded.
13. Time theft – Included in note 42 on page 41 of the financial statements was an amount of R263 000 paid in respect of time theft. This amount pertained to

payments made to four former city officials over a period during which they were not employed by the city.

14. Duplicate wage payment – A payment totalling R527 368, included in note 42 on page 41 of the financial statements, in respect of wages for personnel working on a one-off project was duplicated.
15. Arrear staff debtors – The recoverability of arrear staff debtors that was assessed as doubtful related to the overpayment of leave encashments totalling R466 359 at the end of June 2007. As the write-off of these arrear debtors as irrecoverable may constitute fruitless and wasteful expenditure as per section 32 of the MFMA, disclosure thereof was made in note 42 on page 41 of the financial statements.

OTHER MATTERS

I draw attention to the following matters that are ancillary to my responsibilities in the audit of the financial statements:

Non-compliance with applicable legislation

16. Deviations from section 66(d) and sections 38(a) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) were found, including employees without signed contracts of employment, employees without performance agreements and, in certain instances, employees without letters of appointment.

Matters of governance

17. As stated in paragraph 4 of the report of the chief financial officer on page 7 of the financial statements the city only spent R1,97 billion of its approved capital expenditure budget of R2,54 billion, resulting in an under-spending of approximately 23% (2006: 29% being R1,52 billion spent of an approved budget of R2,13 billion).

Material corrections made to the financial statements submitted for auditing

18. The financial statements, approved by the municipal manager and submitted for auditing on 31 August 2007, have been significantly revised in respect of the misstatements identified during the audit. The material corrections are detailed below.
 - The revenue recognition calculation was incorrect and, as a result, an adjustment of R149 714 000 was made reducing revenue and impairment costs in the statement of financial performance.
 - Additional disclosure was made in note 51 to the financial statements related to land included in property, plant and equipment at 30 June 2007 that had been identified and earmarked for possible sale after the financial year-end.

Internal control

19. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent

systems of financial and risk management and internal control. The table below depicts the root causes of the matters indicated, as they relate to the five components of internal control. In some instances deficiencies existed in more than one internal control component.

Reporting item	Control environment	Assessment of risks	Control activities	Information and communication	Monitoring
Emphasis of matter					
Highlighting a matter affecting the financial statements	X		X		X
Other matters					
Non-compliance with applicable legislation			X		
Matters of governance			X		
Material corrections made to the financial statements submitted for auditing			X		X
Investigations in progress or completed					X

Control activities

20. The effectiveness of control over business and accountancy processes was not adequate, which resulted in an increase in the debtors balance of 6,5% excluding the write-off of bad debts amounting to R1,296 billion as detailed in paragraph 12.

Control environment

21. The entity did not establish all the key elements of a control environment to achieve sound financial management in the payroll and human resources directorates. This resulted in the fruitless and wasteful expenditure reported in paragraphs 13 to 15.

Monitoring controls

22. The monitoring of controls, such as project management where the anticipated cash flows were not properly identified over the term of the project and delays in project completion that were not identified on a timely basis to facilitate the efficient reallocation of resources to other projects, was not effective.

Investigations in progress or completed

23. The prior year audit of payroll and operating expenditure indicated instances of irregular expenditure amounting to approximately R314,7 million. Disclosure of the individual items, together with council action in terms of section 32(2)(b) of the MFMA, was made in note 42 on page 41 of the financial statements. SCOPA established three subcommittees to investigate these matters with the view to resolving these. SCOPA at a meeting held on 22 November 2007 resolved to recommend to the council its support for the approval and condonation of the expenditure as per the council minutes of 7 December 2006, with the exception of six payments. Three of the payments amounting to R3,3 million were still subject to forensic investigation while it was resolved that three other payments amounting to R3,6 million be referred for full forensic investigation.
24. The City has commissioned forensic investigations into several possible fraudulent and/or irregular acts by officials and suppliers. The monetary amount of the 10 highest priority cases exceed R33 million.

Unaudited supplementary schedules

25. The supplementary schedules to the financial statements set out on pages 53 to 60 have not been audited and as such I do not express an opinion thereon.

OTHER REPORTING RESPONSIBILITIES

Reporting on performance information

26. I have audited the performance information as set out on pages XX to XX.

Responsibilities of the accounting officer

27. In terms of section 121(3)(c) of the MFMA the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the MSA.

Responsibility of the Auditor-General

28. I conducted my engagement in accordance with section 13 of the Public Audit Act, 2004 (Act No. 25 of 2004), read with *General Notice 646 of 2007*, issued in *Government Gazette* No. 29919 of 25 May 2007 and section 45 of the MSA.
29. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.

30. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

Audit findings (performance information)

Non-compliance with the MSA

31. As reported in the previous year's audit report the issues regarding non-compliance with the MSA and the Local Government: Municipal Planning and Performance Management Regulations, 2001 (regulations) still prevailed for the year under review. These included the following:

- Lack of community involvement in the setting of performance indicators and targets, and monitoring of the city's performance, as required in terms section 42 and chapter 4 of the MSA.
- Lack of tracking and monitoring the performance of service providers, with whom the city had entered into service delivery agreements, in terms of a formal documented process.

APPRECIATION

32 The assistance rendered by the staff of the City of Cape Town during the audit is sincerely appreciated.

Auditor-General

Cape Town

30 November 2007



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