

**Auditor's report of the Auditor-General to
the Gauteng Provincial Legislature on the
City of Johannesburg Metropolitan
Municipality and its entities for the
year ended 30 June 2010**



A U D I T O R - G E N E R A L
S O U T H A F R I C A

Auditing to build public confidence

The reputation promise of the Auditor-General

“The Auditor-General has a constitutional mandate and, as the Supreme Audit Institution (SAI) of South Africa, it exists to strengthen our country’s democracy by enabling oversight, accountability and governance in the public sector through auditing, thereby building public confidence.”

The mission statement informs the content of the Public Audit Manual (PAM) by recognising that the audits conducted by the SAI of South Africa are unique due to its mandate. This mandate includes responsibilities in terms of laws or regulations that go beyond generally accepted practice of the auditor’s responsibilities in the audit of the financial statements.

These responsibilities include: consideration of issues such as public interest; accountability; probity; effective legislative oversight, in particular as concerns compliance with law, regulation or other authority; performance against pre-determined objectives; and economic, efficient, and effective procurement of resources.

The ultimate goal of the audits is to strengthen the South African democracy.



AUDITOR - GENERAL
SOUTH AFRICA

Mr. Mavela Dlamini
The Accounting Officer
City of Johannesburg Metropolitan Municipality
P O Box 1049
Johannesburg
2000

27 June 2011

Reference: TS 98 19611

Dear Mr Dlamini

Report of the Auditor-General on the financial statements and other legal and regulatory requirements of City of Johannesburg Metropolitan Municipality and its entities for the year ended 30 June 2010.

1. The above-mentioned report of the Auditor-General is submitted herewith in terms of section 21(1) of the Public Audit Act of South Africa read in conjunction with section 188 of the Constitution of the Republic of South Africa and section 121(4) of the Municipal Finance Management Act of South Africa (MFMA).
2. I have not yet received the other information that will be included in the annual report with the audited financial statements and have thus not been able to establish whether there are any inconsistencies between this information and the audited financial statements and the reported performance against pre-determined objectives. You are requested to supply this information as soon as possible. Once this information is received it will be read and should any inconsistencies be identified these will be communicated to you and you will be requested to make the necessary corrections. Should the corrections not be made we will amend and reissue the audit report.
3. In terms of section 121(5) of the MFMA you are required to include the audit report in the City of Johannesburg Metropolitan Municipality's annual report to be tabled.
4. Until the annual report is tabled as required by section 127(2) of the MFMA the audit report is not a public document and should therefore be treated as confidential.
5. Prior to printing or copying the annual report which will include the audit report you are required to do the following:
 - Submit the final printer's proof of the annual report to the relevant senior manager of the Auditor-General of South Africa for verification of the audit-related references in the audit report and for confirmation that the financial statements and other information are those documents that have been read and audited. Special care should be taken with the page references in your report, since an incorrect reference could have audit implications.

- The signature *Auditor-General* in the handwriting of the auditor authorised to sign the audit report at the end of the hard copy of the audit report should be scanned in when preparing to print the report. This signature, as well as the place and date of signing and the Auditor-General of South Africa's logo, should appear at the end of the report, as in the hard copy that is provided to you. The official logo will be made available to you in electronic format if needed.
 - The report must please be referred to the Municipal Public Accounts Committee.
 - **Please send 10 copies of the annual report to the Auditor-General of South Africa for attention Parliamentary Manager, 61 Central Street, Houghton.**
6. **Please notify the undersigned Corporate Executive well in advance of the date on which the annual report containing this audit report will be tabled.**
7. Your cooperation to ensure that all these requirements are met would be much appreciated.

Kindly acknowledge receipt of this letter.

Yours sincerely



Corporate Executive: Gauteng

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AUDITOR'S REPORT OF THE AUDITOR-GENERAL TO THE GAUTENG PROVINCIAL LEGISLATURE AND THE COUNCIL ON CITY OF JOHANNESBURG METROPOLITAN MUNICIPALITY AND ITS ENTITIES

REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying consolidated financial statements of the City of Johannesburg Metropolitan Municipality and its entities, which comprise the statement of financial position as at 30 June 2010, and the statement of financial performance, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information, and the accounting officer's report as set out on pages xxx to xxx.

Accounting officer's responsibility for the consolidated financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (GRAP) and in the manner required by the 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor-General's responsibility

3. As required by section 188 of the Constitution of South Africa, 1996 (Act No. 108 of 1996), section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and section 126 of MFMA my responsibility is to express an opinion on these consolidated financial statements based on my audit.
4. I conducted my audit in accordance with International Standards on Auditing and *General Notice 1570 of 2009* issued in *Government Gazette 32758 of 27 November 2009*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Basis for qualified opinion

Property rates revenue

7. Included in revenue from property rates of R4 219 756 000 (2009: R3 249 024 000) is an amount of R223 361 000 relating to the accrual of revenue that was not billed. Furthermore, included in revenue for property rates for the year 30 June 2010 is R743 363 000 which contained billing errors emanating from incorrect property categories and incorrect market values. Management did not submit appropriate audit evidence to substantiate the accrual raised. I could not quantify the full extent of the error due to insufficient information. Therefore, I was unable to perform alternative audit procedures to verify the accuracy, classification, completeness, occurrence and cut-off of the amounts of R223 361 000 and R743 363 000 included in revenue from property rates of R4 219 756 000 (2009: R3 249 024 000).

Service charges revenue

8. Included in revenue for services charges of R12 016 711 000 (2009: R9 808 541 000) is an amount of R201 620 000, relating to the accrual of revenue not billed. Furthermore, included in service charges revenue is revenue for water and electricity service charges of R1 431 980 000 for the year 30 June 2010 which contained billing errors emanating from incorrect property categories. Management did not submit appropriate audit evidence to substantiate the accrual raised. I could not quantify the full extent of the error due to insufficient information. Therefore, I was unable to perform alternative audit procedures to verify the accuracy, classification, completeness, occurrence and cut-off of the amounts of R201 620 000 and R1 431 980 000 included in revenue from service charges of R12 016 711 000 (2009: R9 808 541 000).

Journals

9. Revenue from property rates and service charges include significant adjusting journal entries processed to correct billing errors amounting to R732 171 725 which were processed in the incorrect accounting period. I was not satisfied that the population corrected by management was free of errors. Therefore, I could not confirm cut-off of

revenue of R732 171 725 included in property rates of R4 219 756 000 (2009: R3 249 024 000) and service charges of R12 016 711 000 (2009: R9 808 541 000).

10. Furthermore, significant adjusting journal entries processed to correct billing errors amounting to R1 875 098 326 included journal entries that were processed in the incorrect accounting period and no appropriate audit evidence to the journals amounting to R1 631 275 962 were submitted for audit purposes. Therefore, I was not able to satisfy myself that the corrected journals submitted by management are free from errors. Therefore, I could not verify accuracy, occurrence, completeness, classification and cut-off of revenue of R1 875 098 326 included in property rates of R4 219 756 000 (2009: R3 249 024 000) and service charges of R12 016 711 000 (2009: R9 808 541 000).

Consumer Debtors

11. As per paragraphs 7 to 10, there were significant shortcomings that were identified during the audit of the revenue billing and management system which raised uncertainties regarding the credibility of significant revenue and receivables financial data. Due to the significance of the errors and insufficient information as mentioned in the preceding paragraphs, I am consequently not able to verify completeness, rights, valuation, presentation and disclosure of debtors amounting to R2 755 764 000 (R2 190 551 000).

Qualified opinion paragraph

12. In my opinion, except for the effects of the matters described in the Basis for qualified opinion paragraph, the consolidated financial statements present fairly, in all material respects, the financial position of the City of Johannesburg Metropolitan Municipality as at 30 June 2010 and its financial performance and its cash flows for the year then ended are prepared, in all material respects, in accordance with GRAP and in the manner required by the MFMA.

Emphasis of matters

I draw attention to the following matters on which I do not express a qualified opinion:

Significant uncertainties

13. As disclosed in note 45 to the consolidated financial statements, the municipality has significant uncertainties as a result of various lawsuits and other uncertainties. Disclosed in the note are amounts totalling R170 557 000 arising from various legal claims.

Restatement of corresponding figures

14. As disclosed in note 46 to the financial statements, material prior period restatements were made to the statement of financial position and financial performance as a result of the various errors as indicated in the note.

Material losses through criminal conduct

15. As disclosed in note 56 to the consolidated financial statements, during the current financial year the City of Johannesburg had cash losses due to fraudulent activities amounting to R14 977 000 (2009 : R45 796 000).

Material losses

16. As disclosed in note 10 to the consolidated financial statements, material losses to the amount of R603 000 000 were incurred as a result of unaccounted for water (UAW).
17. As disclosed in note 10 to the consolidated financial statements, material losses to the amount of R107 543 895 were incurred as a result of electricity distribution losses. The technical losses of electricity incurred amounted to R727 353 000.

Going concern

18. The consolidated statement of financial position of the municipality shows that the total assets exceed total liabilities, fairly valued. However, Pikitup has prepared its financial statements on a going concern basis even though the total liabilities exceed total assets by R387 912 081.

Additional matters

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

Unaudited supplementary schedules

20. The supplementary information set out on pages XX to XX does not form part of the consolidated financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

21. As required by the PAA and in terms of *General Notice 1570 of 2009* issued in *Government Gazette 32758 of 27 November 2009*, I include below my findings on the report on predetermined objectives, compliance with the following key laws and regulations, MFMA, Municipal Regulations (Regulations – GNR/GN), Division of Revenue Act, 2009 (Act No. 12 of 2009) (DoRA), Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA), Municipal Structures Act, 1998 (Act No. 117 of 1998), internal control and financial management.

Predetermined objectives

22. Material findings on the report on predetermined objectives, as set out on pages xx to xx, are reported below:

Non-compliance with regulatory and reporting requirements

Lack of reporting on all predetermined objectives in the annual performance report

23. The Johannesburg Zoo did not report on all the predetermined objectives, as required by section 46 (1) (b) of the MSA, Presentation of reported performance information.

Incomplete reporting on all predetermined objectives, indicators and targets

24. The reported performance information at Johannesburg Metropolitan Trading Company (MTC) to be included in the annual report is not presented in a simple, accessible format, relevant and useful to the intended user.

Usefulness of reported performance information

25. The following criteria were used to assess the usefulness of the planned and reported performance:

- **Consistency:** Has the municipality reported on its performance with regard to its objectives, indicators and targets in its approved integrated development plan, i.e. are the objectives, indicators and targets consistent between planning and reporting documents?
- **Relevance:** Is there a clear and logical link between the objectives, outcomes, outputs, indicators and performance targets?
- **Measurability:** Are objectives made measurable by means of indicators and targets? Are indicators well defined and verifiable, and are targets specific, measurable, and time bound?

The following audit findings relate to the above criteria:

- For the selected programmes at Johannesburg Fresh Produce Market (JFPM), 46% of the planned and reported indicators were not well defined.
- For the selected programmes at JFPM, 39% of the planned and reported performance targets were not specific.
- For the selected programmes at MTC, 33% of the planned and reported performance targets were not specific.
- For the selected programmes at MTC, 33% of the planned and reported targets were not well defined.
- The Johannesburg Zoo did not report throughout on its performance against predetermined objectives which was consistent with the approved annual business plan.

Reliability of reported performance information

26. The following criteria were used to assess the reliability of the planned and reported performance:

- **Validity:** Has the actual reported performance occurred and does it pertain to the entity i.e. can the reported performance information be traced back to the source data or documentation?
- **Accuracy:** Amounts, numbers and other data relating to reported actual performance has been recorded and reported appropriately.
- **Completeness:** All actual results and events that should have been recorded have been included in the reported performance information.

The following audit findings relate to the above criteria:

- For the selected programmes at JFPM, 39% of the reported indicators or targets were not reliable when compared to source information or inadequate source information was provided.
- No multi-year prediction was done at JFPM with regards to key performance indicators.
- Quarterly reports and supporting information at JFPM were not reviewed and evaluated effectively to ensure the validity, accuracy and completeness of progress against key performance indicators.
- The amount of street receptacles at Pikitup could not be verified as no complete list existed with regards to the reported amount of street receptacles.
- For 25% of the targets planned and reported at MTC, the reported data did not agree to the supporting information.
- For the selected programmes at Johannesburg Tourism Company (JTC), 57% of the reported indicators or targets were not accurate when compared to source information or evidence provided.

- For the selected programmes, 22% of the reported indicators or targets were not accurate when compared to source information or considered to be not accurate as inadequate source information was provided.
- For the selected key performance indicators at Metropolitan Bus Service (Metrobus), some of the reported targets were not accurate on the basis of the source information or evidence provided to support the reported targets.
- For the selected objectives the validity, accuracy and completeness at Metrobus, 40% of the reported indicators and targets could not be established as sufficient appropriate audit evidence and relevant source documentation could not be provided for audit purposes.

Compliance with laws and regulations

Municipal Finance Management Act, No 56 of 2003 (MFMA)

The Audit Committee was not properly established or not functioning properly

27. Contrary to the requirements of section 166(1) of the MFMA, the municipality did not have an audit committee that functioned throughout the financial year.

The consolidated financial statements were not prepared in accordance with applicable legislation

28. Contrary to requirements of section 122(1) of the MFMA the consolidated financial statements submitted for audit on the 31 August 2010 did not fairly present the financial position of the municipality, with regards to revenue and consumer debtors. These consolidated financial statements were subject to material amendments as a result of the audit.

Non compliance with applicable laws and regulations on contract management

29. Contrary to section 33(3) of the MFMA, all contracts referred to in sub-section (1) and all other contracts that impose a financial obligation on a municipality were not made available in their entirety to the municipal council.
30. Contrary to section 125(2)(d)(i) and (ii) the municipality did not disclose particulars of material irregular expenditure as well as fruitless and wasteful expenditure that occurred during the financial year. Furthermore, there was insufficient disclosure relating to whether such expenditure was recoverable and whether any criminal or disciplinary steps were taken as a result of the irregular expenditure and fruitless and wasteful expenditure

Payments were not made within the parameters set by applicable legislation

31. Contrary to the requirements of section 65(2)(e) and section 99(2)(b) of the MFMA, the municipality and its entities failed to make certain payments within 30 days from receipt of an invoice or within such period as prescribed for certain categories of expenditure.

Municipal Systems Act (MSA)

Internal auditing of performance measurements

32. The City of Johannesburg did not develop and implement mechanisms, systems and processes for auditing the results of performance measurement as part of its internal audit processes, as required in terms of section 45 of the MSA.

Executive directors' financial interests not declared

33. Contrary to Schedule 2 5 A of the Municipal Systems Act, one of the Executive directors did not declare all interests held in other companies.

Councillors' financial interests not declared

34. Contrary to the Municipal Systems Act- *section 7 of schedule 2* which requires councillors to declare all their financial interests in writing to the municipal manager, some of the councillors did not declare all their financial interests in writing to the municipal manager.

Supply Chain Management Regulations

Supply chain management requirements were not adhered to

35. Certain deviations from the supply chain management process were not in accordance with, *inter alia*, supply chain management regulation 36(1). Municipal Finance Management Act, 2003 (Act No. 56 of 2003).

Non-compliance with Local Government Ordinance 17 of 1939

36. The municipality did not comply with section 79 (18) of the Local Government Ordinance, 1939 (Ordinance 17 of 1939) in that the notice process was completed after the awarding of the contract or signing of the development deal.

INTERNAL CONTROL

37. I considered internal control relevant to my audit of the consolidated financial statements and the report on predetermined objectives as well as compliance with the MFMA, The Municipal Regulations and MSA, but not for the purpose of expressing an opinion on the effectiveness of internal control.

The matters reported below are limited to the significant deficiencies regarding the basis for qualified opinion paragraph, the findings on the report on predetermined objectives and the findings on compliance with laws and regulations.

Leadership

38. The municipality did not adequately implement a system to ensure that revenue is billed correctly and correcting adjusting journal entries are recorded in the correct accounting period.

The municipality did not exercise sufficient monitoring and supervision over the compliance with laws and regulations in respect of supply chain management legislative requirements.

Financial and performance management

39. The accounting officer did not fully fulfil his duties and responsibilities of managing the preparation of the consolidated financial statements to ensure that the consolidated financial statements were not subject to material amendments resulting from the audit.

Manual or automated controls are not designed to ensure that the transactions have occurred, are authorised, and are completely and accurately processed.

Pertinent information is not identified and captured in a form and time frame to support financial reporting.

Internal control deficiencies are not identified and communicated in a timely manner to allow for corrective action to be taken.

The municipality did not exercise sufficient oversight responsibility over reporting, compliance with laws and regulation and internal control.

Governance

40. Mechanisms, systems and processes for auditing the results of performance measurement as part of internal audit processes, as required in terms of section 45 MSA have not been developed and implemented.

The municipality did not have an audit committee throughout the financial year under review as a result the audit committee did not fulfil its responsibility as set out in legislation and in accordance with accepted best practice.

Adequate actions were not taken in all instances to address risk relating to the achievement of complete and accurate financial and performance management.

OTHER REPORTS

Investigations

41. Fifty cases were investigated by the forensic audit section of internal audit from the 2009-2010 financial years. Of these, 23 have been finalised. The nature of the cases covered a wide spectrum of activities, e.g. bribery, theft, financial corruption, tender irregularities and various other issues. These fraudulent activities covered various departments of the City of Johannesburg and 27 cases are still pending as investigations are still in progress.

Agreed upon procedures engagement

42. As requested by the City of Johannesburg, two engagements were conducted during the year under review concerning commercial paper issue (Bond issue). The reports covered the period July 2009 to May 2010 which was issued on 5 July 2010; and the period June 2010 to February 2011 which was issued on 18 March 2011.

Auditor - General

Johannesburg

27 June 2011



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence