

# REPORT OF THE AUDITOR-GENERAL TO THE GAUTENG PROVINCIAL LEGISLATURE AND COUNCIL ON THE EKURHULENI METROPOLITAN MUNICIPALITY

## REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

### Introduction

1. I have audited the accompanying consolidated and separate financial statements of the Ekurhuleni Metropolitan Municipality, which comprise the consolidated and separate statement of financial position as at 30 June 2011, and the consolidated and separate 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 information, as set out on pages xx to xx.

### Accounting officer's responsibility for the consolidated financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these consolidated and separate financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA), and for such internal control as management determines necessary to enable the preparation of consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.

### Auditor-General's responsibility

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996, section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and section 126(3) of the MFMA, my responsibility is to express an opinion on these consolidated and separate financial statements based on my audit.
4. I conducted my audit in accordance with International Standards on Auditing and General Notice 1111 of 2010 issued in Government Gazette 33872 of 15 December 2010. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated and separate 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 and separate financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated and separate financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the consolidated and separate 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 and separate financial statements.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

## **Opinion**

7. In my opinion, the consolidated and separate financial statements present fairly, in all material respects, the financial position of the Ekurhuleni Metropolitan Municipality (municipality) and its entities as at 30 June 2011, and their financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of the MFMA.

## **Emphasis of matters**

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

## **Significant uncertainties**

9. As disclosed in note 44 to the financial statements, the municipality is the defendant in various court cases and disputes. The ultimate outcome of these matters cannot presently be determined or reliably measured, and no provision for any liabilities that may result has been made in the financial statements.

## **Material losses**

10. As disclosed in note 57 to the financial statements, the municipality suffered significant water and electricity losses of 98 859 310 kilolitres and 331 601 611 kilowatts with a value of R402,1 million and R165,1 million respectively, during the year under review.

## **Material under spending of the budget**

11. As disclosed in note 58 to the financial statements, the municipality and its entities materially under spent their capital budget to an amount of R381,1 million out of a final budget of R2,4 billion. As a consequence, the municipality did not fully achieve its service delivery objectives and with respect to the municipal entity, the implementation of the capital development programme and the availability of the new plant capacity were delayed.

## **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

12. In accordance with the PAA and in terms of *General Notice 1111 of 2010*, issued in *Government Gazette 33872 of 15 December 2010*, I include below my findings on the annual performance report as set out on pages xx to xx and material non-compliance with laws and regulations applicable to the municipality and its entities.

## **Report on predetermined objectives**

13. There are no material findings on the annual performance report for the municipality.
14. I was unable to conduct the audit of performance against predetermined objectives for the Ekurhuleni Development Company (Pty) Ltd (EDC) as the entity did not submit the annual performance report as required by section 46 of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) and section 121(4)(d) of the MFMA.

## **Usefulness of information**

15. The reported performance information of the Lethabong Housing Institute (LHI) was deficient in respect of the following criteria:

- **Measurability:** The indicators are not well-defined and verifiable, and targets are not specific and time-bound.

16. The following audit findings relate to the above criteria:

### **Planned and reported indicators were not well defined**

17. For the selected objectives of LHI, 50% of the planned and reported indicators were not clear. Unambiguous data definitions were not available to allow for data to be collected consistently.

### **Planned and reported indicators were not verifiable**

18. For the selected objectives of LHI, valid performance management processes and systems that produce actual performance against the planned indicators did not exist for 25% of the indicators.

### **Planned and reported targets are not specific and time bound**

19. For the selected objective of LHI, 25% of the planned and reported targets were not:

- specific in clearly identifying the nature and the required level of performance;
- time-bound in specifying the time period or deadline for delivery.

## **Compliance with laws and regulations**

### **Municipal Finance Management Act**

#### **Annual financial statements, performance and annual reports**

20. The financial statements submitted for auditing by the municipality were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of receivables from exchange transactions, contingent liabilities and disclosure items, identified by the auditors were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.

21. The municipal council of the municipality did not adopt an oversight report containing the council's comments on the annual report within two months from the date on which the 2009-10 annual report was tabled in the council as required by section 129(1) of the MFMA.

22. The accounting officer of the EDC did not prepare and include an assessment of the performance against any measurable performance objectives set, in terms of the service delivery agreement or other agreement between the entity and its parent municipality as required by section 121(4)(d) of the MFMA.

## **Internal audit**

23. The accounting officer of the East Rand Water Care Company (ERWAT) did not take all reasonable steps to ensure that the entity has and maintains effective, efficient and transparent systems of internal audit complying with and operating in accordance with prescribed norms and standards, as required by section 95(c)(ii) of the MFMA.
24. At ERWAT, the internal audit did not function as required by section 165(2)(b) in that:
- internal audit did not report to the audit committee on the implementation of the internal audit plan;
  - internal audit did not advise the accounting officer and report to the audit committee on matters relating to internal controls and accounting procedures and practices

## **Procurement and contract management**

25. At the municipality, awards were made to providers who were persons in service of the municipality in contravention of supply chain management (SCM) regulation 44. These providers failed to declare that they were in the service of the municipality as required by SCM regulation 13(c).
26. At the municipality, awards were made to providers who were persons in service of other state institutions in contravention of SCM regulation 44. These providers failed to declare that they were in the service of the state as required by SCM regulation 13(c).

## **Human resource management and compensation**

27. Senior managers directly accountable to the accounting officer of the municipality did not sign annual performance agreements for the year under review as required by sections 57(1)(b) and 57(2)(a) of the MSA. These contracts were finalised in the last quarter of the financial year.

## **Expenditure management**

28. The accounting officer of the municipality did not take reasonable steps in certain instances to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA.
29. The accounting officers of the municipal entities, ERWAT, Brakpan Bus Company (Pty) Ltd, and EDC, did not take reasonable steps in certain instances to prevent irregular expenditure, as required by section 95(d) of the MFMA.
30. The accounting officers of the municipal entities, EDC, Germiston Phase II (Pty) Ltd and Pharoe Park Housing Company (Pty) Ltd did not take reasonable steps in certain instances to prevent fruitless and wasteful expenditure, as required by section 95(d) of the MFMA.

## **National Water Act**

31. ERWAT did not comply with Government Notice (GN) 399 of 26 March 2004: Revision of the General Authorisations in terms of section 39 of the National Water Act of South Africa, 1998 (Act No. 36 of 1998), in relation to irrigation of any land with waste or water containing waste

generated through an industrial activity or by a waterwork. Two of the nineteen plants did not comply for certain months with the chemical oxygen demand. Furthermore, two of the nineteen plants did not comply for certain months with respect to suspended solids.

## **INTERNAL CONTROL**

32. In accordance with the PAA and in terms of General Notice 1111 of 2010, issued in *Government Gazette 33872 of 15 December 2010*, I considered internal control relevant to my audit, 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 that resulted in the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

### **Leadership**

33. The municipality and its entities did not have sufficient monitoring controls to ensure adherence to all laws and regulations, specifically in the area of supply chain management.

34. Effective leadership on good governance and internal controls over compliance with all laws and regulations applicable to ERWAT, was not always exercised.

### **Financial and performance management**

35. Material amendments made to the financial statements were mainly due to senior management not adequately reviewing and having sufficient internal processes to ensure accurate and complete financial statements, prior to submission for auditing.

36. The accounting officer of EDC and LHI did not exercise oversight responsibility regarding performance reporting which resulted in the findings on reporting on performance against predetermined objectives.

### **Governance**

37. ERWAT did not have an adequately functioning internal audit unit that identified internal control deficiencies effectively and recommended corrective actions to be taken timeously.

## **OTHER REPORTS**

### **Investigations**

38. In terms of Proclamation No. R 63, 2010, the President of South Africa has assigned the Special Investigating Unit to investigate various issues on the state of affairs of the municipality. The investigation includes areas of supply chain management, fraud and financial misconduct.

39. During the financial year, 70 investigations were conducted by the internal audit division of the municipality. Of these, 28 investigations were finalised. Eighteen investigations were in a draft reporting stage and 24 of the investigations were at the field work stage. Circumstances that resulted in investigations pertained mainly to non-compliance with the SCM regulations,

such as the extending of contracts, abuse of SCM regulation 36(1), irregular awarding of tenders, splitting of payments and quotations from fictitious suppliers.

**Agreed upon procedures engagements**

40. As requested by the municipality, an agreed upon procedure engagement was conducted during the year under review concerning the second issue of R800 million notes under the Domestic Medium Term Note Programme. The engagement covered the period July 2010 to January 2011 and the report was issued on 11 March 2011.

*Auditor - General*

Johannesburg  
14 December 2011



AUDITOR - GENERAL  
SOUTH AFRICA

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