

REPORT OF THE AUDITOR-GENERAL TO THE GAUTENG PROVINCIAL
LEGISLATURE AND COUNCIL ON THE CITY OF TSHWANE METROPOLITAN
MUNICIPALITY

REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

Introduction

1. I have audited the consolidated and separate financial statements of the City of Tshwane Metropolitan Municipality set out on pages xx to xx, which comprise the consolidated and separate statement of financial position as at 30 June 2012, and the consolidated and separate statement of financial performance, statement of changes in net assets and the cash flow statement for the year then ended, and the notes comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the 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 in the manner required by the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA), and for such internal control as management determines is 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. My responsibility is to express an opinion on these consolidated and separate financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the *General Notice* issued in terms thereof and International Standards on Auditing. 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.
4. 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 and fair presentation 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.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

6. In my opinion, the consolidated and separate financial statements present fairly, in all material respects, the financial position of the City of Tshwane Metropolitan Municipality (municipality) and its entities as at 30 June 2012, and their financial performance and cash flows for the year then ended in accordance with SA Standards of GRAP and in the manner required by the MFMA.

Emphasis of matters

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

Significant uncertainties

8. As disclosed in note 53 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 and / or reliably measured, therefore no provision for any liabilities that may result has been made in the financial statements.

Restatement of corresponding figures

9. As disclosed in note 45 to the financial statements, the corresponding figures for 30 June 2011 have been restated as a result of various errors discovered during the year ended 30 June 2012.

Material losses

10. As disclosed in note 59 to the financial statements, material losses amounting to R389 200 000 (2011: R296 760 000) were incurred as a result of water distribution losses, which represent 24,70% (2011: 28,64%) of total water available for sale and are due to burst pipes, non-metering of water and unauthorised consumption.
11. As disclosed in note 60 to the financial statements, material losses amounting to R673 475 523 (2011: R375 939 558) were incurred as a result of electricity distribution losses which represent 12,11% (2011: 9,32%) of total electricity available for sale. The total technical losses of electricity amounted to R333 675 523 (2011: R242 039 558). Non-technical losses amounted to R339 800 000 (2011: R139 000 000) and are due to theft, tampering and faulty meters.

Material impairments

12. As disclosed in note 19 to the financial statements, receivables have been significantly impaired. The impairment of receivables amounts to R2 945 403 331 (2011: R2 233 923 917) which represent 52% (2011: 46%) of consumer debtors and the contribution to provision for doubtful debts for the year under review amounted to R711 479 414 (2011: R319 839 109).

Additional matter

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

Unaudited supplementary schedules

14. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited this schedule and, accordingly, I do not express an opinion thereon

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

15. In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

PREDETERMINED OBJECTIVES

16. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages ... to ... of the annual report.
17. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury annual reporting principles and whether the reported performance is consistent with the planned objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the *National Treasury Framework for managing programme performance information* (FMPPi).

The reliability of the information in respect of the selected objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).

18. The material findings are as follows:

City of Tshwane (Municipality)

Reliability of information

Accuracy – reported performance not accurate

19. The FMPPi requires that the indicator be accurate enough for its intended use and respond to changes in the level of performance. A total of 31% of the actual reported performance relevant to provision of basic service, roads and storm water and sustainable communities with clean, healthy and safe environments and integrated social services were not accurate when compared to source information. This was due to a lack of monitoring and review by senior management of the recording of actual achievements and non-compliance with internal reporting processes.

Sandspruit Works Association SOC Ltd (Sandspruit Work Association) *ENTITY*

Usefulness of information

Presentation - Measures taken to improve performance not disclosed

20. Improvement measures in the annual performance report that were not achieved for a total of 41% of the planned targets was not disclosed as required by section 46 of the Municipal Systems Act, 2000 (Act No. 32 of 2000)(MSA). This was due to inadequate internal policies and procedures over the processes pertaining to the reporting of performance information.

Housing Company Tshwane SOC Ltd (Housing Company Tshwane) *ENTITY*

Usefulness of information

Presentation - Measures taken to improve performance not disclosed

21. Improvement measures in the annual performance report that were not achieved for a total of 100% of the planned targets was not disclosed as required by section 46 of the MSA. This was due to inadequate internal policies and procedures over the processes pertaining to the reporting of performance information.

Consistency of information

Reported objectives are not consistent with planned objectives/indicators/targets

22. Section 41(c) of the MSA requires that the actual achievements against all planned indicators and targets must be reported annually. One hundred percent of the objectives, indicators and targets as per the annual performance report and the mid year performance assessment report did not agree to the initial objectives, indicators and targets set out in the business plan for 2011-12. This was due to inadequate internal policies and procedures over the monitoring of compliance with laws and regulations and over processes pertaining to the reporting on performance information.

No budget allocation for the reported strategic objectives

23. There was no budget allocation for the reported strategic objectives because the reported objectives were not approved by the parent municipality and are not consistent with the approved business plan which is in line with the service delivery agreement. This was due to inadequate internal policies and procedures over the monitoring of compliance with laws and regulations.

Measurability of information

Performance targets not specific

24. The FMPPI requires that performance targets be specific in clearly identifying the nature and required level of performance. A total of 34% of the targets relevant to the development of up to 1078 new units of affordable and quality rental units by 2014 (Greenfield projects), the promotion and guarantee of excellent service provision, striving for financial stability, the management of rental housing stock effectively and efficiently, ensuring that Housing Company Tshwane is financially sustainable and liquid by 2012-13, improving occupancy rate to 100% on all our buildings under management and effective management of finances, assets, systems and human capital were not specific in clearly identifying the nature and the required level of performance. Management was aware of the requirements of the FMPPI but did not comply with it.

Performance targets not measurable

25. The FMPPI requires that performance targets be measurable. The required performance could not be measured for a total of 80% of the targets relevant to the recovery and rehabilitation of "bad buildings" with rental capacity of 1701 units by 2014 (Brownfields projects), development up to 1078 new units of affordable and quality rental units by 2014 (Greenfields projects), the promotion and guarantee of excellent service provision, striving for financial stability, the management of rental housing stock effectively and efficiently, ensuring that Housing Company Tshwane is financially sustainable and liquid by 2012-13, improving occupancy rate to 100% on all our buildings under management and designing and implementing an institutional transformation plan strategy to improve corporate governance structure and ensure adequate capacity to achieve the 5 year strategic objectives. Management was aware of the requirements of the FMPPI but did not comply with it.

Performance targets not time bound

26. The FMPPI requires that the time period or deadline for delivery be specified. A total of 71% of the targets relevant to the recovery and rehabilitation of "bad buildings" with rental capacity of 1701 units by 2014 (Brownfields projects), development up to 1078 new units of affordable and quality rental units by 2014 (Greenfields projects), the promotion and guarantee of excellent service provision, striving for financial stability, the management of rental housing stock effectively and efficiently, effective management of finances, assets, systems and human capital, designing and implementing an institutional transformation plan strategy to improve corporate governance structure and ensure adequate capacity to achieve the 5 year strategic objectives were not time bound in specifying a time period or deadline for delivery. Management was aware of the requirements of the FMPPI but did not comply with it.

Performance Indicators not well defined

27. The FMPPI requires that indicators/measures should have clear unambiguous data definitions so that data is collected consistently and is easy to understand and use. A total of 30% of the indicators relevant to the development of up to 1078 new units of affordable and quality rental units by 2014 (Greenfield projects), the promotion and guarantee of excellent service provision, striving for financial stability, the management of rental housing stock effectively and efficiently, ensuring that Housing Company Tshwane is financially sustainable and liquid by 2012-13, improving occupancy rate to 100% on all our buildings under management, designing and implementing an institutional transformation plan strategy to improve corporate governance structure and ensure adequate capacity to achieve the 5 year strategic objectives were not well defined in that clear, unambiguous data definitions were not available to allow for data to be collected consistently. Management was aware of the requirements of the FMPPI but did not comply with it.

Indicators not verifiable

28. The FMPPI requires that it must be possible to validate the processes and systems that produce the indicator. A total of 86% of the indicators relevant to development of up to 1078 new units of affordable and quality rental units by 2014 (Greenfield projects), the promotion and guarantee of excellent service provision, striving for financial stability, the management of rental housing stock effectively and efficiently, ensuring that Housing Company Tshwane is financially sustainable and liquid by 2012-13, improving occupancy rate to 100% on all our buildings under management, effective management of finances, assets, systems and human capital and designing and implementing an institutional transformation plan strategy to improve corporate governance structure and ensure adequate capacity to achieve the 5 year strategic objectives were not verifiable in that valid processes and systems that produce the information on actual performance did not exist.

Reliability of information

Validity - reported performance not valid

29. The FMPPI requires that processes and systems which produce the indicator should be verifiable. I was unable to obtain all the information and explanations I considered necessary to satisfy myself as to the validity of the actual reported performance relevant to 64% of the objectives. This was due to lack of processes and information

systems and Housing Company Tshwane's records not permitting the application of alternative audit procedures.

Additional matter

30. I draw attention to the following matters below. These matters do not have an impact on the predetermined objectives audit findings reported above.

Achievement of planned targets

31. Of the total number of 19 targets planned, 8 targets were not achieved during the year under review for the Municipality. This represents 42% of total planned targets that were not achieved. This was mainly due to the fact that indicators and targets were not suitably developed during the strategic planning process and the municipality not considering appropriate systems to measure the objectives during the annual strategic planning process.
32. Of the total number of 32 targets planned, only 19 were achieved during the year under review for Sandspruit Work Association. This represents 41% of total planned targets that were not achieved during the year under review. This was mainly due to the fact that indicators and targets were not suitably developed during the strategic planning process.
33. One hundred percent of planned targets were not achieved during the year under review for Housing Company Tshwane. This was mainly due to the fact that indicators and targets were not suitably set during the strategic planning process and different objectives were adopted by the entity.

Material adjustments to the annual performance report done for municipality

34. Material adjustments in the annual performance report were identified during the audit, all of which were corrected by management.

COMPLIANCE WITH LAWS AND REGULATIONS

35. I performed procedures to obtain evidence that the municipality and its municipal entities has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the *General Notice* issued in terms of the PAA are as follows:

Budget

36. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA.
37. The total unforeseen and unavoidable expenditure incurred exceeded R15 000 000 in contravention of Municipal Budget and Reporting Regulation 72,

Annual financial statements

38. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements in the provision for doubtful debts, liabilities and investment property for the municipality, Sandspruit Work Association and Housing Company Tshwane respectively, identified by the auditors were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.

Procurement and contract management

39. Awards were made to providers whose directors/ principal shareholders are persons in the service of the municipality, in contravention of National Treasury's Municipal Supply Chain Management regulation (SCM regulation) 44. Furthermore the providers failed to declare that they were in the service of the municipality, as required by SCM regulation 13(c). Reasonable steps taken were not fully effective to prevent or combat the abuse of the SCM process in accordance with SCM regulation 38(1).
40. Awards were made to providers whose directors/ principal shareholders are persons in the service of other state institutions for both the municipality and Sandspruit Work Association, in contravention of SCM regulation 44. Similar awards, in contravention of SCM regulation 44, were identified in the prior year and the steps taken were not fully effective to prevent or combat the abuse of the SCM process in accordance with SCM regulation 38(1).
41. Persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM regulation 46(2)(e) and the code of conduct for staff members issued in terms of the MSA.
42. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM regulation 46(2)(e) and the code of conduct for staff members issued in terms of the MSA.
43. Quotations and deviation contracts were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).

Expenditure management

44. The accounting officer of the municipality and Housing Company Tshwane did not take effective steps to prevent unauthorised, irregular and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

INTERNAL CONTROL

45. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control 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

46. The accounting officer inadequately reviewed the monthly and quarterly financial and performance reports. Material adjustments were therefore required on both the annual financial statements and the annual performance report. The municipality and entities did not have sufficient monitoring controls to ensure the proper implementation of the process of reporting on predetermined objectives as information on both Sandspruit Work Association and Housing Company Tshwane were found not to be useful and the actual performance reported for the municipality and Housing Company Tshwane were not reliable.

Financial and performance management

47. The municipality's system of record management that provides for the maintenance of information which supports the reported performance contained in the annual performance report was not fully effective. This includes information that relates to the

collection, collation, verification, storing and reporting of actual performance information. Non-compliance with laws and regulations such as the MFMA, SCM regulations and PPPF Act regulations could have been prevented had compliance been properly reviewed and monitored.

OTHER REPORTS

Investigations

48. In terms of Proclamation no. R62 of 2010, the President of South Africa has assigned the Special Investigation Unit to investigate various issues on the state of affairs of the municipality. The investigation includes SCM, fraud and financial misconduct.

49. The forensic audit section of the internal audit division investigated and finalised 275 cases for the financial year under review. The nature of the cases covered a wide spectrum of activities including supply chain management, fraud and financial misconduct.

Auditor - General

Johannesburg

14 December 2012



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence