

Buffalo City Metropolitan Municipality

Audit Report

For the year ended 30 June 2017

Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on the Buffalo City Metropolitan Municipality

Report on the audit of the consolidated and separate financial statements

Opinion

1. I have audited the consolidated and separate financial statements of the Buffalo City Metropolitan Municipality set out on pages ... to ..., which comprise the consolidated and separate statement of financial position as at 30 June 2017, the consolidated and separate statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the consolidated and separate financial statements, including a summary of significant accounting policies.
2. In my opinion, the consolidated and separate financial statements present fairly, in all material respects, the consolidated and separate financial position of the Buffalo City Metropolitan Municipality as at 30 June 2017, and its financial performance and cash flows for the year then ended in accordance with the 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 Division of Revenue Act of South Africa (Act No.3 of 2016) (DoRA).

Basis for opinion

3. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the consolidated and separate financial statements section of this report.
4. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) and the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Emphasis of matters

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

Restatement of corresponding figures

7. As disclosed in note 51 to the consolidated and separate financial statements, the corresponding figures for 30 June 2016 have been restated as a result of errors discovered during the year ended 30 June 2017 in the consolidated and separate financial statements of the municipality at, and for the year ended, 30 June 2016. These restatements relate to non-current assets, current assets, current liabilities and disclosure items.

Irregular expenditure

8. As disclosed in note 57 to the financial statements, irregular expenditure of R287,3 million (2015-16: R531,6 million) was incurred due to supply chain management (SCM) transgressions that occurred in the year under review and previous financial years. The cumulative balance as at 30 June 2017 was R2,4 billion.

Impairments

9. As disclosed in notes 13 and 15 to the consolidated and separate financial statements, cumulative debt impairment provisions amounted to R1,2 billion (2015-16: R1,1 billion) due to the slow recovery of old consumer debts.

Material losses

10. As disclosed in note 59 to the consolidated and separate financial statements, the municipality incurred material losses. These include the following:
 - Electricity losses totalling R218,8 million (2015-16: R180,5 million) of which non-technical losses comprise R130,4 million (2015-16: R99,7 million) due to technical faults and theft.
 - Water losses totalling R100,8 million (2015-16: R116,7 million) of which non-technical losses comprise R36,9 million (2015-16: R31,3 million) due to bulk water meters not being installed in all rural and semi-rural areas.

Other matter

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

Unaudited disclosure note

12. In terms of section 125(2)(e) of the MFMA, the entity is required to disclose particulars of non-compliance with this legislation. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion thereon.

Responsibilities of accounting officer for the financial statements

13. The accounting officer is responsible for the preparation and fair presentation of the consolidated and separate financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA for such internal control as the accounting officer 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.
14. In preparing the consolidated and separate financial statements, the accounting officer is responsible for assessing the Buffalo City Metropolitan Municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the intention is to liquidate the metropolitan municipality or cease operations, or there is no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

15. My objectives are to obtain reasonable assurance about whether the consolidated and separate financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated and separate financial statements.
16. A further description of my responsibilities for the audit of the consolidated and separate financial statements is included in this annexure to the auditor's report.

Introduction and scope

17. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
18. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
19. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2017:

Development priorities	Pages in the annual performance report
Key performance area (KPA) 2: Municipal basic service delivery and infrastructure development	x – x
KPA 3: Local Economic Development	x – x

20. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
21. The material findings in respect of usefulness and reliability of the reported performance information for the selected development priorities are as follows:

KPA 2: basic service delivery and infrastructure development

22. The reported achievements of the indicators listed below were misstated, as the evidence provided did not agree with the achievements reported in the annual performance report:
- Kilometres of gravel roads rehabilitated (re-gravelled) as the evidence provided indicated 105,197km and not 121,107km as reported.
 - Kilometres of electricity cables installed as the evidence provided indicated 11,146km and not 11 441km as reported.

- Number of SMME and Cooperatives supported through capacity building, business skills and access to market as the evidence provided indicated 661 and not 775 as reported.
- Number of transformers installed as the evidence provided indicated 6 and not 5 as reported.
- Number of informal dwellings provided with a basic electricity service as the evidence provided indicated 517 and not 1 002 as reported.

23. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of the indicators listed below as reported achievements were not supported by sufficient appropriate audit evidence. This was due to limitations placed on the scope of my work. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement of the following indicators:

- Number of households benefiting from informal settlement upgrading closer to the urban edge.
- Number of households benefiting from informal settlement upgrading in rural areas.
- % of households with access to basic solid waste removal services.

KPA 3: local economic development

24. The strategic objective, to ensure BCMM is well structured and capacitated to deliver on its mandate, was reported in KPA 4: good governance in the annual performance report while the planned strategic objective was approved in KPA 3: local economic development in the service delivery and budget implementation plan. This is not in line with the requirements of section 41(c) of the Municipal Systems Act, 2000 (Act No. 32 of 2000).

25. The reported achievements of the indicators listed below were misstated, as the evidence provided did not agree with the achievements reported in the annual performance report:

- Number of people from employment equity target groups (disabled) employed as the evidence provided indicated 2 and not 3 as reported
- Number of programmes implemented to grow Tourism Sector as the evidence provided indicated 11 and not 9 as reported
- Number of businesses provided with export development support as the evidence provided indicated 86 and not 69 as reported

26. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of the indicators listed below as reported achievements were not supported by sufficient appropriate audit evidence. This was due to limitations placed on the scope of my work. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement of the following indicators:

- Number of job opportunities created through LED initiatives including implementation of capital projects
- Number of job opportunities created through the Expanded Public Works Programme

Other matter

27. I draw attention to the matter below.

Achievement of planned targets

28. Refer to the annual performance report on page(s) x to x; x to x for information on the achievement of planned targets for the year and explanations provided for the under/overachievement of a number of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 22 to 26 of this report.

Report on audit of compliance with legislation

Introduction and scope

29. In accordance with the PAA and the general notice issued in terms thereof I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

30. The material findings on compliance with specific matters in key legislation are as follows:

Annual financial statements

31. The consolidated and separate financial statements submitted for auditing were not prepared, in all material respects, in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets, current assets, current liabilities, revenue and disclosure items identified by the auditors in the submitted consolidated and separate financial statements were subsequently corrected, resulting in the consolidated and separate financial statements receiving an unqualified audit opinion.

Revenue management

32. An effective system of internal control for revenue was not in place, as required by section 64(2)(f) of the MFMA, as significant internal control deficiencies were identified in the billing system of the municipality.

Asset management

33. An effective system of internal control for assets (including asset register) was not in place, as required by section 63(2)(c) of the MFMA.

Budget management

34. Reasonable steps were not taken to prevent unauthorised expenditure of R 95,9 million, as disclosed in note 55 to the consolidated and separate annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by non-cash items such as depreciation, impairment and loss on disposal of assets.

Expenditure management

35. Effective steps were not taken to prevent irregular expenditure of R287,3 million, as disclosed in note 57 to the consolidated and separate annual financial statements, as required by section 62(1)(d) of the MFMA.

Other information

36. The Buffalo City Metropolitan Municipality's accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the consolidated and separate financial statements, the auditor's report and those development priorities presented in the annual performance report that have been specifically reported in the auditor's report.
37. My opinion on the consolidated and separate financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
38. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated and separate financial statements and the selected development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work I have performed on the other information obtained prior to the date of this auditor's report, I conclude that there is a material misstatement of this other information, I am required to report that fact. I did not identify any material findings in this regard.

Internal control deficiencies

39. I considered internal control relevant to my audit of the consolidated and separate financial statements, performance reporting and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon. The matters reported below are limited to the significant internal control deficiencies that resulted in the findings on the annual performance report and the findings on compliance with legislation included in this report.
- Management did not adequately respond to previous year's findings relating to reporting on the annual performance report. The municipality did not have a system to collate and report on predetermined objectives. The performance unit was decentralised and did not work in an integrated manner with the other divisions within

the municipality. This resulted in poor and inaccurate quarterly and annual reporting on achievements against targets.

- Management did not ensure adequate implementation and monitoring of controls over daily and monthly processing and reconciling transactions. In addition, information systems were not fully used and integrated to support the accurate preparation of financial statements and performance reporting, as evidenced by the findings on the financial statements that were subsequently corrected and the findings on performance reporting that were not corrected. This contributed to the reported non-compliance.

Auditor - General

East London

8 December 2017



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

Annexure – Auditor-general’s responsibility for the audit

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the consolidated and separate financial statements, and the procedures performed on reported performance information for selected development priorities and on the municipality’s compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the consolidated and separate financial statements as described in the auditor’s report, I also:
 - identify and assess the risks of material misstatement of the consolidated and separate financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
 - obtain an understanding of internal control relevant to the audit 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 municipality’s internal control.
 - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the board of directors, which constitutes the accounting authority.
 - conclude on the appropriateness of the accounting officer’s use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Buffalo City Metropolitan Municipality’s ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor’s report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of the auditor’s report. However, future events or conditions may cause a municipality to cease continuing as a going concern.
 - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
 - obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group to express an opinion on the consolidated and separate and separate financial statements. I am responsible for the direction, supervision and performance of the group audit. I remain solely responsible for my audit opinion.

Communication with those charged with governance

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and where applicable, related safeguards.