

Auditor-General of South Africa

**Buffalo City Metropolitan
Municipality and its municipal
entity**

**Audit report for the year ending
30 June 2021**

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

Report on the audit of the consolidated and separate financial statements

Qualified opinion

1. I have audited the consolidated and separate financial statements of the Buffalo City Metropolitan Municipality and its municipal entity (the group) set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2021, the statement of financial performance, statement of changes in net assets, and cash flow statement and the statement of comparison of budget information with actual amounts for the year then ended, as well as notes to the consolidated and separate financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the effects of the matter described in the basis for qualified opinion section of my report, the consolidated and separate financial statements present fairly, in all material respects, the financial position of the group as at 30 June 2021, and its financial performance and cash flows for the year then ended in accordance with the Standards of Generally Recognised Accounting Practice (GRAP) and the requirements of the Municipal Finance Management Act 56 of 2003 (MFMA) and the Division of Revenue Act 4 of 2020 (Dora).

Basis for qualified opinion

Irregular expenditure

3. The municipality did not fully record irregular expenditure in the notes to the consolidated and separate financial statements, as required by section 125(2)(d) of the MFMA. This was because expenditure incurred in contravention of the supply chain management (SCM) legislation was not detected and appropriately disclosed in the consolidated and separate financial statements. Consequently, I was unable to determine the full extent of the understatement of irregular expenditure, stated at R2,7 billion (2019-20: R2,5 billion) in note 59 to the consolidated and separate financial statements as it was impracticable to do so.

Context for the opinion

4. 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 my report.

5. I am independent of the municipality in accordance with the International Ethics Standards Board for *Accountants' International code of ethics for professional accountants (including International Independence Standards)* (IESBA code) as well as other 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.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Emphasis of matters

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

Restatement of corresponding figures

8. As disclosed in note 52 to the consolidated and separate financial statements, the corresponding figures for 30 June 2020 have been restated as a result of errors identified in the consolidated and separate financial statements of the municipality at, and for the year ended, 30 June 2021.

Material losses and impairments

9. As disclosed in notes 12 and 13 to the consolidated and separate financial statements, material impairment allowances of R817,6 million (2019-20: R655,3 million) and R1,9 billion (2019-20: R1,5 billion) were made against receivables from non-exchange and exchange transactions, respectively.
10. As disclosed in note 39 to the consolidated and separate financial statements, the municipality incurred material electricity losses of R368,2 million (2019-20: R295,1 million), which represents 22,8% (2019-20: 19,4%) of total electricity purchased. These losses arose from technical losses which are inherent in the supply of electricity and non-technical losses due to illegal connections, theft, faults and billing errors.
11. As disclosed in note 39 to the consolidated and separate financial statements, the municipality incurred material water losses of R125,5 million (2019-20: R126,1 million), which represents 36,3% (2019-20: 36,3%) of total water purchased. These losses incurred as a result of ageing infrastructure, unbilled water consumption and theft or illegal use.

Other matter

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

Unaudited disclosure note

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

Responsibilities of the accounting officer for the consolidated and separate financial statements

14. The accounting officer is responsible for the preparation and fair presentation of the consolidated and separate financial statements in accordance with the Standard of GRAP and the requirements of the MFMA and Dora, and for such internal control as the accounting officer determines is necessary to enable the preparation of the consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.
15. In preparing the consolidated and separate financial statements, the accounting officer is responsible for assessing the 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 appropriate governance structure either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

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

16. 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.
17. A further description of my responsibilities for the audit of the consolidated and separate financial statements is included in the annexure to this auditor's report.

Report on the audit of the annual performance report

Introduction and scope

18. In accordance with the Public Audit Act 25 of 2004 (PAA) and the general notice issued in terms thereof, I have a responsibility to report on the usefulness and reliability of the reported performance information against predetermined objectives for selected strategic outcome presented in the annual performance report. I performed procedures to identify material findings but not to gather evidence to express assurance.

19. My procedures address the usefulness and reliability of the reported performance information, which must be based on the municipality's approved performance planning documents. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures do not examine whether the actions taken by the municipality enabled service delivery. My procedures do not extend to any disclosures or assertions relating to the extent of achievements in the current year or 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.
20. 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 strategic outcome presented in the municipality's annual performance report for the year ended 30 June 2021:

Strategic outcome	Pages in the annual performance report
Strategic outcome 4: A spatially transformed city	x – x

21. 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.
22. The material findings on the usefulness and reliability of the performance information of the selected strategic outcome are as follows:

Strategic outcome 4: A spatially transformed city

Various indicators

23. Adequate systems and processes were not established to enable consistent measurement and reliable reporting of performance against the predetermined indicator definitions. As a result, I was unable to obtain sufficient appropriate audit evidence for the reported achievements in the annual performance report, as well as the reasons for variances between the planned targets and reported achievements. I was unable to confirm reported achievements and the reasons for variances by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements and the reasons for the variances for the indicators listed below.

Indicator description	Planned targets	Reported achievement
Percentage of wastewater safely treated	75%	74%
Percentage compliance of water treatment works with SANS 241 requirements	98%	98%

Indicator description	Planned targets	Reported achievement
Percentage of water connections metered	98%	89%

Other matters

24. I draw attention to the matters below.

Achievement of planned targets

25. Refer to the annual performance report on pages x to x; x to x for information on the achievement of planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraph 23 of this report.

Adjustment of material misstatements

26. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of strategic outcome 4: a spatially transformed city. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

Report on the audit of compliance with legislation

Introduction and scope

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

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

Annual financial statements

29. 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 of non-current assets and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected. The remaining uncorrected material misstatement of irregular expenditure has resulted in the financial statements receiving a qualified audit opinion.

Strategic planning and performance management

30. The performance management system and related controls were inadequate as it did not describe how the performance measurement, review, reporting and improvement processes should be conducted, organised and managed, as required by municipal planning and performance management regulation 7(1).

Expenditure management

31. Reasonable steps were not taken to prevent irregular expenditure, in contravention of section 62(1)(d) of the MFMA. The full extent of the irregular expenditure could not be quantified, as indicated in the basis for qualification paragraph. The majority of the disclosed irregular expenditure was caused by transgressions of SCM legislation.

Procurement and contract management

32. Some of the goods and services with a transaction value of above R200 000 were procured without inviting competitive bids, in contravention of SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1). Similar non-compliance was also reported in the prior year.
33. Some of the construction contracts were awarded to contractors that did not qualify for the contract in accordance with section 18(1) of the Construction Industry Development Board (CIDB) Act 38 of 2000 and CIDB regulations 17 and 25(7A). This non-compliance was identified in the capital expenditure incurred as part of the municipality's annual contracts.
34. The performance of some of the contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
35. The contract performance and monitoring measures were not in place to ensure effective contract management, as required by section 116(2)(c)(ii) of the MFMA.

Consequence management

36. Some of the irregular expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.

Other information

37. The 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 the selected strategic outcome presented in the annual performance report that have been specifically reported in this auditor's report.

38. 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 on it.
39. 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 strategic outcome presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
40. I did not receive the other information prior to the date of this report. When I do receive and read this information, if I conclude that there is a material misstatement therein, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and re-issue an amended report as appropriate. However, if it is corrected this will not be necessary.

Internal control deficiencies

41. I considered internal control relevant to my audit of the consolidated and separate financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.
42. Leadership's oversight responsibility to ensure credible and reliable financial and performance reporting, as well as compliance with legislation, was limited due to inadequate coordination and monitoring between directorates of the municipality.
43. The SCM policies and procedures were inadequate to ensure fairness, competitiveness and transparency when procuring goods and services. This, together with a lack of monitoring of contracts already procured, resulted in non-compliance with SCM regulations.
44. The daily and monthly disciplines required by management were inadequate to account for all the financial and performance processes of the municipality. Furthermore, management did not prepare regular, accurate and complete financial and performance reports supported and evidenced by reliable information.

Material irregularities

45. In accordance with the PAA and the Material Irregularity Regulations, I have a responsibility to report on material irregularities identified during the audit and on the status of the material irregularities reported in the previous year's auditor's report.

Material irregularities identified during the audit

Unbilled water revenue

46. The municipality did not bill all consumers for water services. A number of properties were identified as having water connections or having access to water for which the consumer was not billed. This resulted in non-compliance with section 64(2)(b) of the MFMA, which requires revenue due to the municipality to be calculated on a monthly basis. The municipality suffered a material financial loss of R9,6 million included in income forgone - sale of water of R36 million disclosed in note 24 to the financial statements for the year ended 30 June 2021. The accounting officer was notified of the material irregularity on 24 March 2021 and invited to make a written submission on the actions taken or that will be taken to address the matter. The accounting officer responded on 23 April 2021.
47. The accounting officer delegated the relevant heads of departments to investigate the root causes of this material irregularity. The outcome of the investigation highlighted a number of control deficiencies, including a lack of integrated processes and systems between the municipality's directorates, and delays in updating systems and registers that linked water meters per property.
48. The municipality notified and commenced billing the affected consumers from the 2020-21 financial year, as per the municipality's credit control policy.
49. The accounting officer instituted disciplinary investigations to identify the persons responsible for the material irregularity. The disciplinary processes were not concluded at the date of this report. I will follow up on this action in the next audit.

Other reports

50. In addition to the investigations relating to the material irregularity, I draw attention to the following engagements conducted by various parties which had, or could have, an impact on the matters reported in the consolidated and separate financial statements, reported performance information, compliance with applicable legislation and other related matters. These reports did not form part of my opinion on the consolidated and separate financial statements or my findings on the reported performance information or compliance with legislation.

51. There were five investigations conducted by external parties during the year under review, all relating to SCM irregularities and financial misconduct cases, which cover the period 2013-14 to 2019-20. These investigations were ongoing at year-end and therefore no recommendations have yet been communicated to management.

Auditor - General

East London

28 February 2022



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 strategic outcome and on the municipality's compliance with respect to the selected subject matters.

Consolidated and separate Financial statements

2. In addition to my responsibility for the audit of the consolidated and separate financial statements as described in this 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 accounting officer.
 - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the consolidated and separate financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists relating to events or conditions that may cast significant doubt on the ability of the group 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 consolidated and separate financial statements about the material uncertainty or, if such disclosures are inadequate, to modify my opinion on the financial statements. My conclusions are based on the information available to me at the date of this auditor's report. However, future events or conditions may cause the group to cease operating as a going concern.
 - evaluate the overall presentation, structure and content of the consolidated and separate financial statements, including the disclosures, and determine whether the consolidated and separate 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 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 provide the accounting officer with a statement that I have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on my independence and, where applicable, actions taken to eliminate threats or safeguards applied.