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COJ : GROUP AUDIT COMMITTEE	2012-12-14

**OVERSIGHT REPORT OF THE CITY OF JOHANNESBURG GROUP
AUDIT COMMITTEE ON THE MONITORING OF THE 30 JUNE 2012
STATUTORY YEAR END AUDIT, THE EVALUATION OF THE FINAL
AUDITED ANNUAL FINANCIAL STATEMENTS, THE AUDITOR
GENERAL MANAGEMENT REPORT AND FINAL AUDIT OPINION
FOR THE YEAR ENDED 30 JUNE 2012**

1. STRATEGIC THRUST(S)

Good Governance: Responsive, accountable, efficient and productive metropolitan government.

Good Governance: Financial and administratively sustainable & resilient City.

2. OBJECTIVE

The purpose of this report is to communicate to the Mayoral committee and therefore Council, the Group Audit Committee's (GAC) progress to date in carrying out its oversight responsibilities over the statutory audit process for the financial year ended 30 June 2011, as mandated in terms of section 166 (2)(b) of the Municipal Finance Management Act (MFMA). The report also summarises the recommendations of the Group Audit Committee in accordance with section 121 (3)(j) of the MFMA that have been made and discussed with the administration.

3. SUMMARY

3.1 BACKGROUND

The mandate of the Group Audit Committee is legislated in terms of section 166 of the Municipal Finance Management Act, which requires the Audit Committee to advise the Accounting Officer and Council on matters relating to internal financial control and internal audits; risk management; accounting policies; adequacy, reliability and accuracy of financial reporting and information; performance management and performance evaluation; effective governance; compliance with the Municipal Finance Management Act (MFMA), the Annual Division of Revenue Act, and any other applicable legislation; and any other issues referred to it by the municipality.

The MFMA also requires the Audit Committee to review the annual financial statements, respond to Council on matters raised by the Auditor General, and carry out investigations into the financial affairs of the municipality. The responsibilities of the GAC include oversight of the Municipal Entities of the City of Johannesburg from a group perspective, although each of the Municipal Owned Entities ("MOE's") of the City have their own Audit Committees which report to their Boards of Directors.

3.2

The GAC reports that it has complied with its responsibilities arising from section 166 (2) (b) of the Municipal Finance Management Act ("MFMA"), and the Council approved Terms of Reference which require the Group Audit Committee of the City to review the annual financial statements.

3.2.1 Group Audit Committee (GAC) Attendance of meetings

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During the financial year ending 30 June 2012, the GAC held five of the six scheduled meetings, and two special meetings. The meeting that had been scheduled for March 2012 did not take place following the expiry of the term of the members of the GAC. However, all the matters including the internal audit report for the second quarter were deferred to the next meeting of the GAC that was held in June 2012.

Names of Members	Period of Membership	Financial Year 2011/12	
		Total Number of meetings	Number of Meetings attended
		8	7 (1 meeting rescheduled)
1) Ms Jocelyn Armstrong (Chairperson)	Re-Appointed (April 2012)	7	7
Mr Seth Radebe	Term expired (Jan 2012)	6	2
Mr Kumaran Naidoo	Term expired (Jan 2012)	6	0
Mr Grant Dunnington	Term expired (Jan 2012)	6	3
Ms Phumzo Noxaka	Term expired (June 2012)	7	7
Ms Maureen Manyama-Matome	Term expired (Jan 2012)	6	4
2) Mr Victor Nondabula	Term expires Dec 2012	6	4
3) Mr Paul Samuels**	Appointed (April 2012) Resigned (Sept. 2012)	1	1
4) Mr Mdu Zakwe (CA) SA	Appointed (April 2012)	1	1
5) Ms Thandi Sihlaba	Appointed (April 2012)	1	1
6) Mr Langa Dlomo-Ntuli	Appointed (April 2012)	1	1
7) Mr Abel Dlamini CA (SA)	Alternate member	n/a	
8) Mr Piet Fourie CA(SA)	Alternate member	n/a	

TABLE 1: GAC ATTENDANCE OF MEETINGS

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3.2.1.1 Evaluation of Annual Financial Statements for the year ended 30th June 2012

The GAC reports that it has reviewed and discussed with the Auditor-General SA (AGSA) and the management of the City:

- a) the unaudited annual financial statements of the City of Johannesburg Core Administration and the unaudited consolidated annual financial statements of the City of Johannesburg for the financial year ending 30 June 2012, prior to the submission hereof to the Auditor General (SA) for year- end audit purposes;
- b) the audited annual financial statements of the City of Johannesburg core administration for the year ended 30 June 2012;
- c) the accounting policies and practices;
- d) the year-end accruals for revenue, related journals and potential impact on prior year figures;
- e) material or significant adjustments resulting from the audit;
- f) the prior year adjustments and reasons therefore;
- g) contingent liabilities;
- h) fruitless, wasteful and irregular expenditure as reported in the annual financial statements;
- i) the going concern basis for the preparation of the annual financial statements of the core administration and the municipal entities; and the
- j) the audited consolidated annual financial statements of the City of Johannesburg and its group of municipal entities for the year ended 30 June 2012;
- k) the draft and final AGSA management reports on the regularity audit and the audit of performance information of the City of Johannesburg Municipality and its entities, and management's response thereto;
- l) the draft and final AGSA reports on the regularity audit of the municipal owned entities, the core administration and the consolidated Annual Financial Statements for the year ending 30 June 2012; and
- m) the basis of the final AGSA audit opinions, the emphasis of matter and other significant matters.

3.2.2 Group Audit Committee Observations and Recommendations on Year-end audit

- a) Submission of draft unaudited annual financial statements
 - The City of Johannesburg Core Administration and its Municipal Entities met the mandatory deadlines in terms of the MFMA for the submission of unaudited annual financial statements and the consolidated annual financial statements.
 - The annual financial statements were prepared on the going concern basis.

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- b) GAC recommendation for approval of the submission of the Core Administration's unaudited AFS to the Accounting Officer:
- The GAC recommended the submission of the unaudited AFS of the core administration to the AGSA, subject to the Group Chief Financial Officer effecting the adjustments that were highlighted and agreed to at the meeting.
- c) GAC recommendation for approval of the submission of the CoJ Group unaudited consolidated AFS for the year ended 30 June 2012 to the Auditor General SA

In accordance with the provisions of the Municipal Finance Management Act (MFMA), section 166, having reviewed the unaudited consolidated annual financial statements of the City, for the financial year ending 30 June 2012 and made recommendations to management, the GAC approved the submission of the unaudited consolidated annual financial statements.

- d) GAC consideration and recommendation for approval of the audited consolidated group annual AFS, the AGSA final Management Letter and the AGSA audit report for the year-ending 30 June 2012.

The GAC considered the final results of the year-end audit.

Delayed Submissions of management information and supporting documentation

- i) The AGSA reported delays in the submission of required management and accounting information relating to assets under construction and CoJ fleet.

Application of GRAP13

- ii) There is one significant area that was observed by the Committee relating to the accounting treatment of the Rea Vaya/ BRT buses contract which resulted in a qualification. According to the Auditor General, application of the Standards for the Generally Recognised Accounting Practice (GRAP 13) requires that the lease be classified as a finance lease. The Committee noted management representations that engagements had been planned with SA Institute of Chartered Accountants, Office of Accountant General and the Auditor General SA.

AGSA Final Management Report

- iii) The AGSA completed the audit of the final consolidated Annual Financial Statements of the City and its Municipal Entities, and issued its final management report and the audit opinion within the set deadlines.
- iv) The GAC noted the high number of audit queries raised by the AGSA in the management letter, including the matters that resulted in the qualified audit opinion and the matters of emphasis.

AGSA Final Audit Opinion on 2011/12 Consolidated Annual Financial Statements

- v) The Auditor General (SA) has expressed a qualified audit opinion on the

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Consolidated Annual Financial statements for the year ended 30 June 2012:

BASIS OF QUALIFICATION	2011/12	2010/11
Property Rates Revenue	N/A	Yes
Refuse Removal	Yes	N/A
Service Charges Revenue (Sale of Water and Electricity – meter readings)	Yes	Yes
Consumer Debtors	Yes	Yes
Leave Accrual	N/A	Yes
Property, Plant and Equipment (BRT buses, infrastructure assets) (Prior period errors raised in 2011/12)	Yes	N/A

- vi) The municipal entities of the City of Johannesburg received two (2) unqualified audit opinions for the financial year ended 30 June 2012. The municipal entities that received qualified audit opinions for the financial period are:
- City Power
 - Johannesburg Water
- vii) The Committee has deemed it important that the nature of the matters under emphasis be highlighted and comparison with prior year also be done to monitor the areas of weaknesses that could result in possible qualifications should management not address the associated internal controls and non-compliance:

EMPHASIS OF MATTER	2011/12	2010/11
Significant Uncertainties due to Litigation and potential contingent liabilities		
Restatement of corresponding figures (Prior period financial accounting errors)	Yes	Yes
Material Losses due to fraudulent activities	Yes	Yes
Material Losses due to unaccounted for Water	Yes	Yes
Material Losses due to unaccounted for Electricity	Yes	Yes
Material Impairments of accounts receivable (Provision for bad debts of consumer debtors)	Yes	Yes
Going concern of Pikitup The Issue of technical insolvency of Metrobus was raised by the AGSA. This requires close management attention	Yes	Yes

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- viii) While the Auditor General SA does not express an audit opinion on the audit of pre-determined objectives, the AG does report on the outcomes of the audit of the municipality's performance against predetermined objectives, compliance with applicable laws and regulations and internal control. The findings of the Auditor General with regards to the performance information are consistent with the findings of the internal audits completed during the year:
- Performance objectives, targets and indicators not consistent with the objectives, targets and indicators approved in the Integrated Development Plan;
 - Instances where performance targets were not specific, measurable, accurate or smart;
 - Lack of a document management system or performance management system that will assist in ensuring completeness and reliability of performance information;
 - Significant non-achievement of planned performance targets for the year under review across the City.
- ix) The Committee has observed further consistencies in the nature of findings raised by the Auditor General and the issues raised by the Group Assurance Services (JRAS). Some of the reported weaknesses are repeats from prior years, for example:
- Non-compliance with supply chain management laws, regulations and policies
 - Asset Management
 - Revenue Management

e) Going Concern statement for the year ended 30 June 2012

The GAC considered the results of the audits of the annual financial statements of the City of Johannesburg and its Municipal Entities. The annual financial statements were prepared on the going concern basis.

The GAC concurs and accepts that except for the effects of the matters which resulted in a qualified opinion of the Auditor General, the consolidated annual financial statements present fairly, in all material respects, the financial position of the city of Johannesburg Metropolitan Municipality as at 30 June 2012 and its financial performance and cash flows for the year then ended are prepared in all material respects, in accordance with the Municipal Finance Management Act (MFMA) and the South African Statements of Generally Recognised Accounting Practice (GRAP).

The GAC is therefore of the opinion that the audited annual financial statements be accepted and be read together with the report of the Auditor-General.

The GAC is satisfied, based on the audited annual financial statements and cash flow forecast that the City of Johannesburg is a going concern, but highlights to the Mayoral Committee the note 20 in the 2011/12 report of the Auditor General with regard to the going concern status of the municipal entity, Pikitup Johannesburg SOC (Pty) Ltd.

The AGSA also raised an emphasis of matter in the report of the Johannesburg Roads Agency SOC Ltd (JRA) by way of note 10 on financial sustainability and therefore Going Concern of this entity. The JRA Going Concern arises from the accumulated deficit R212 441 235 and its working capital (total liabilities exceeding total assets by R152 201

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056), as at end of the financial year.

Further, the AGSA brought to the attention of the Group Audit Committee, a post balance sheet event associated with the entity, the Johannesburg Metropolitan Bus Service. The AGSA has reported that the entity was technically insolvent as at 30th November 2012. This exposes the City and its municipal entity to the risk of reckless trading and potential reputational risk.

The Group Audit Committee has therefore recommended that the Group Governance department should advise on the actions being taken by the shareholder to address the current financial situation at Metro Bus.

3.2.3 GAC overall observations and recommendations

MFMA section 166

The Group Audit Committee also exercised oversight over the areas as prescribed in terms of the MFMA section 166 and advised on corrective actions to address significant gaps and weaknesses identified. The Committee submitted its quarterly reports to the Mayoral Committee which included the annual report.

The recommendations in the reports to the Committee covered the following:

- Internal Audit Unit and its effectiveness
- Internal and Financial Control systems
- Fraud and Irregular activities
- Performance Management and Performance Evaluation
- Enterprise Risk Management
- Compliance with applicable legislation
- Governance practices
- Combined and Integrated Assurance

Independent oversight committees and integrated approach

- Organisational structure of the independent oversight committees, namely, the Group Risk Management Committee, the Performance Audit Committee, the Audit and/or Risk Committees of the Municipal Entities and the Group Audit Committee.
- Specific recommendations have been made to improve the terms of reference of the independent group oversight committees to enable a more collaborative approach, streamlined advisories and assurance to the Accounting Officer, Mayoral Committee and Council together with its sub-committees, as appropriate.

MFMA section 121 (3)

The detailed observations, discussions, requests and recommendations have been made to management. These recommendations have been made in accordance with section 121 (3) (j) of the MFMA and are itemised in paragraph 4 below.

The management comments and action plans should be of quality that will address the

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underlying causes of weaknesses identified and therefore mitigate the re-occurrence of these findings.

IT IS RECOMMENDED

- 1 That the Mayoral Committee:**
 - (1) Notes the outcomes of the Auditor General external audit of the City and its municipal entities for the year-ended 30 June 2012.**
 - (2) Approves the audited Group Annual Financial Statements for the financial year 30 June 2012, the Auditor General SA (AGSA) Management Letter and the Auditor General audit opinion as contained in the audit report.**
- 2 That the Group Strategy Policy and Relations (GSPR) Department ensures the inclusion in the integrated annual report of the City the governance reports by the Group Audit Committee and the Group Risk Management Committee, assisted by the Group Assurance Services Department.**
- 3 That the Acting Group Chief Financial Officer, with the support of the respective executive management where applicable, develops a detailed management action plan to address the issues raised in the reports of the Auditor General and Group Assurance Services' Internal Audit reports. The management action plan should as recommended by the Group Audit Committee:**
 - **outline the underlying causes for the reported weaknesses in financial controls and financial reporting;**
 - **outline how the Group Finance function, structure and operations will address the identified underlying causes;**
 - **explain how the Group Finance Department inclusive of the Finance functions in the municipal entities will achieve consistently high levels of financial reporting;**
 - **outline the plan to capacitate the group finance function, including the acquisition and retention of the financial reporting skills and experience.**
- 4 The Group Executive Director: Group Corporate and Shared Services should detail how the City's Information and Communication Technology (ICT) governance framework and strategy will going forward ensure alignment to business requirements, ensuring consistent and continuous system availability and adequacy of application systems that will support operational efficiencies.**

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- 5 That the Acting Group Chief Financial Officer should prepare a formal written advisory note on the accounting treatment of the BRT buses contract. The advisory should cover the associated implication of the implementation or non-implementation of the recommended capitalization of the bus leases arising from the application of Generally Accepted Accounting Practice (GRAP 13).
- 6 The Acting Group CFO, should prior to the termination of the City's contract with KPMG, submit to the Accounting Officer and the Group Audit Committee a detailed report on the City's financial management, progress on key projects such as the Finance Development Strategy, as well as any other projects or activities that fall under the responsibility of the Acting Group CFO. This close-out report should be submitted prior to March 2013, to enable effective monitoring and evaluation of the deliverables in terms of the Group CFO contract with KPMG.
- 7 That the responsible senior official should submit a detailed report on the City's Revenue Step Change Programme including the City's Contract with KPMG. The report should be submitted prior to March 2013 to the Group Audit Committee to enable effective monitoring and evaluation of the deliverables in terms of the KPMG contract.
- 8 That the Management of the City designs and implements adequate systems of internal controls to address the reported internal control weaknesses, instances of non-compliance with applicable legislation, instances of irregular expenditure.
 - The Group Assurance Services Department should finalise a Group Internal Control Framework for formal adoption by the City, facilitate internal control self-assessments towards improving the internal control and financial control environment in the City.
 - The City should adopt a zero tolerance policy for instances of irregular, fruitless and wasteful expenditure.
- 9 That the Group Combined Assurance Unit should assess the internal audit findings that have not been resolved and the Auditor General's findings that were the basis of qualification, emphasis of matter and other significant matters.
 - (1) Group Risk Services should identify the key risk exposures associated with internal audit unresolved queries, the qualification matters and areas of emphasis; advise management on the risk mitigation actions, monitor the implementation hereof, and communicate this to management on a regular basis. Quarterly reports to the GRMC and GAC, and where appropriate the Performance Audit Committee should be inclusive of the risk monitoring outcomes.

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- (2) In collaboration with Group Risk Services, Group Internal Audit should conduct the planned follow-up audits to assess the adequacy of the management action plans and the effective implementation of the systems and controls to mitigate the associated risks and therefore avoid recurrence of audit queries. The internal audit outcomes be reported to management, the Audit Committee(s), the Cluster Sub-Mayoral Committees, and the Mayoral Committee.**
- 10 The Group Internal Audit function within Group Assurance Services should complete the quarterly key control reviews as agreed with the AGSA and highlight weaknesses and/or deficiencies in internal controls.**
- 11 That the City finalizes the appointment of members to the Performance Audit Committee so that this Committee can exercise oversight over the Performance Management System, organizational and individual performance.**

J. ARMSTRONG (MS)
CHAIRPERSON: GROUP AUDIT COMMITTEE
City of Johannesburg Metropolitan Municipality

22 January 2013