



A U D I T O R - G E N E R A L
S O U T H A F R I C A

Municipal Manager
City of Tshwane Metropolitan Municipality
P.O Box 440
Pretoria
0001

17 November 2010

Reference: 60020REG09/10(TEDA JUNE2010)

Dear Sir

**MANAGEMENT REPORT ON THE REGULARITY AUDIT OF THE TSHWANE
ECONOMIC DEVELOPMENT AGENCY (PROPRIETARY) LIMITED (TEDA) FOR
THE PERIOD ENDED 30 JUNE 2010**

INTRODUCTION

1. This management report relates to our audit of the financial statements for the period ended 30 June 2010.
2. The report contains the following main subsections:
 - The Auditor-General's responsibilities
 - The accounting officer's responsibilities
 - Misstatements in the financial statements
 - Matters to be brought to the attention of the users
 - Other legal and regulatory reporting requirements
 - Details of significant deficiencies in internal control relevant to the audit of the financial statements and compliance with laws and regulations
 - Matters that may give rise to future audit findings if not addressed
 - Ratings of the audit findings
 - Summary of detailed audit findings
3. Annexures A and B contain information on the detailed audit findings. The detailed findings were communicated during the course of the audit and this report includes management's responses.

THE AUDITOR-GENERAL'S RESPONSIBILITIES

4. Our responsibility is to express an opinion on the financial statements and to report on findings related to our review of compliance with key laws and regulations. Our engagement letter sets out our responsibilities in detail. These include the following:

- Planning and performing the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements, whether caused by fraud or error.
 - Performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the financial statements.
 - Considering internal controls relevant to the entity's preparation and fair presentation of the financial statements and compliance with laws and regulations.
 - Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management.
 - Evaluating compliance with applicable legislation regarding financial matters, financial management and other related matters.
 - Evaluating the overall presentation of the financial statements.
 - Expressing an opinion on the financial statements based on the audit in accordance with the International Standards on Auditing (ISAs).
 - Reading other information in documents containing the audited financial statements.
5. Because of the test nature and other inherent limitations of an audit, we do not guarantee the completeness and accuracy of the financial statements or compliance with all applicable legislation.
6. Having formed an opinion on the financial statements, we may include additional communication in the auditor's report that does not have an effect on the auditor's opinion. The following paragraphs could be included in the auditor's report:
- An emphasis of matter paragraph to draw users' attention to a matter presented or disclosed in the financial statements which is of such importance that it is fundamental to their understanding of the financial statements.
 - An additional matter paragraph to draw users' attention to any matter, other than those presented or disclosed in the financial statements, that is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

THE ACCOUNTING OFFICER'S RESPONSIBILITIES

7. The accounting officer's responsibilities are set out in detail in the engagement letter. These include the following:
- The preparation and fair presentation of the financial statements in accordance with the applicable reporting framework.
 - Designing, implementing and maintaining internal controls relevant to the preparation of the financial statements.
 - Selecting and applying appropriate accounting policies, and making accounting estimates that are appropriate in the circumstances.
 - Disclosing known instances of non-compliance or suspected non-compliance with laws and regulations, the effects of which should be considered when preparing financial statements.

- Providing access to all information that is relevant to the preparation of the financial statements, such as records and documents.
- Disclosing all matters concerning any risk, allegation or instance of fraud.
- Accounting for and disclosing related party relationships and transactions.

MISSTATEMENTS IN THE FINANCIAL STATEMENTS

Material misstatements not corrected

8. The misstatements included below were identified during the audit and have not been corrected by management at the date of this report. These misstatements were not prevented or detected by the municipal entity's system of internal control. We urge management to address the matters reflected as the internal control deficiency for the misstatements.

The following material misstatements arose from a difference between the disclosures in the financial statements and the disclosures required by the financial reporting framework.

Material misstatements		Amount R	Internal control deficiency
Financial statement line item	Reason for misstatement		
Presentation of financial statements	The municipal entity did not comply with the requirements of GRAP 1 - Presentation of financial statements in the preparation of the financial statements for the period ended 30 June 2010.	N/A	<p><u>Oversight responsibility:</u> There was a lack of oversight responsibility over reporting and compliance with laws and regulations.</p> <p><u>Financial management:</u> The financial statements were not reviewed for completeness and accuracy prior to submission for audit.</p>
Cash flow statement	Non cash items have not been removed from the cash flow statement as required by GRAP 2 - Cash flow statements.	N/A	<p><u>Oversight responsibility:</u> There was a lack of oversight responsibility over reporting and compliance with laws and regulations.</p> <p><u>Financial management:</u> The financial statements were not reviewed for completeness and accuracy prior to submission for audit.</p>

MATTERS TO BE BROUGHT TO THE ATTENTION OF THE USERS

EMPHASIS OF MATTER PARAGRAPH

Going concern

While the municipal entity prepared financial statements on a going concern basis, there are a number of indicators that its financial sustainability is under threat. These include the following:

- The municipal entity has not commenced trading since incorporation in 2006.
- The municipal entity incurred a net loss from operations of R 16 723.
- At the date of this report, the appointment of the board of directors has not been finalised

OTHER LEGAL AND REGULATORY REPORTING REQUIREMENTS

Compliance with laws and regulations

Included below are the findings related to material non-compliance with the acts as indicated.

Municipal Finance Management Act, 2003 (Act No. 56 of 2003)

The annual budget was not prepared, tabled and approved in accordance with the applicable laws and regulations

- Contrary to the requirements of section 87(1) of the MFMA, management failed to submit a proposed budget for the entity to its parent municipality as the entity was dormant.

The financial statements were not prepared in accordance with applicable legislation

- Contrary to the requirements of section 95(c)(i) of the MFMA, the accounting officer did not ensure that the entity has and maintains effective, efficient and transparent systems of financial and risk management and internal control.
- Contrary to the requirements of section 125(2)(e) of the MFMA, the municipal entity did not disclose particulars of non-compliance with the MFMA in the notes to the financial statements.

The internal audit unit was not properly established

- Contrary to the requirements of section 165 of the MFMA, the municipal entity did not have an operational internal audit function in place as it was dormant.

Supply chain management legislative requirements were not implemented

- Contrary to the requirements of section 111, 112 and 115 of the MFMA, the municipal entity did not have and implement a supply chain management policy as it was dormant.

Companies Act, 1973 (Act No. 61 of 1973)

The statutory requirements of the Companies Act have not been complied with

- Contrary to the requirements of section 179(1)(a) of the Companies Act, the municipal entity did not hold an annual general meeting during the period under review.
- Contrary to the requirements of section 286 of the Companies Act, the financial statements for the period ended 30 June 2010 were not laid before an annual general meeting for approval.

Municipal Systems Act, 2000 (Act No. 32 of 2000)

The statutory requirements of the Municipal Systems Act have not been complied with

- Contrary to the requirements of section 93H(1)(b) of the Municipal Systems Act, management did not ensure compliance with all applicable legislation and agreements.

INTERNAL CONTROL

Internal control table

The following table indicates the achievement of the objectives of internal control as they relate to the three fundamentals of internal control. The assessment is based on significant deficiencies which give rise to matters included in the auditor's report as the basis for the qualified opinion on the financial statements and compliance with laws and regulations. The reasons for this assessment are discussed below. Other deficiencies in internal control, which require the attention of management, are included in the detailed findings attached to this report.

Fundamental of internal control Objectives of Internal control	Operational	Accountability and reporting	Compliance	Safeguarding of resources
	Achieved? "Yes" / "No"	Achieved? "Yes" / "No"	Achieved? "Yes" / "No"	Achieved? "Yes" / "No"
Leadership				
• Oversight responsibility	No	No	No	N/A
• Tone at the top	Yes	Yes	Yes	N/A
• Action to mitigate risks	No	No	No	N/A
Financial and performance management				
• Quality reliable AFS	Yes	No	No	N/A
• Proper record keeping	Yes	Yes	No	N/A
• Adequate systems	Yes	Yes	No	N/A
Governance				
• Risk identification	No	No	No	N/A
• Fraud prevention	No	No	No	N/A
• Internal audit	No	No	No	N/A
• Audit committees	Yes	Yes	Yes	N/A

Achievement of internal control objectives

9. Below is a summary of the internal control deficiencies that resulted in the above assessment and that gave rise to the basis for the qualified opinion on the financial statements as well as findings on compliance with laws and regulations. Additional information on significant internal control deficiencies is provided later in this report.

Leadership

As the entity is dormant, there was no oversight over reporting and compliance with laws and regulations and internal control. Furthermore, there were no internal policies and procedures pertaining to the monitoring and reporting of compliance with laws and regulations, resulting in numerous instances of non-compliance.

Financial and performance management

As the entity is dormant there were no systems in place to facilitate the preparation of the financial statements and the financial statements were not reviewed for completeness and accuracy prior to submission for audit.

Governance

As the entity is dormant, no internal audit function was in place to ensure that ongoing monitoring and supervision were undertaken and to enable an assessment of the effectiveness of internal control over financial reporting.

DETAILS OF SIGNIFICANT DEFICIENCIES IN INTERNAL CONTROL RELEVANT TO THE AUDIT OF THE FINANCIAL STATEMENTS AND COMPLIANCE WITH LAWS AND REGULATIONS

LEADERSHIP

Oversight responsibility over reporting

10. The municipal entity did not have sufficient monitoring controls in place to ensure the proper implementation of the overall process of planning, budgeting, implementation and reporting.

Adequacy and competence of personnel responsible for reporting

11. The entity is dormant and therefore no employees were appointed for the financial year under review. The municipal entity appointed consultants to prepare the financial statements for the period ended 30 June 2010. Furthermore, these financial statements were not reviewed prior to submission for audit resulting in various instances of non compliance with the applicable reporting framework as well as with laws and regulations.

Implementation of appropriate key controls (policies and procedures)

12. The entity did not have documented policies and procedures in place to guide the operations and as a result numerous instances of non compliance with the MFMA, the Companies Act and the Municipal Systems Act were noted.

FINANCIAL AND PERFORMANCE MANAGEMENT

Accounting policies and disclosures

13. There was a lack of monitoring and review in place to ensure adequate disclosures were made in the financial statements in accordance with the applicable reporting framework.

Budget process as well as measurement and achievement

14. The municipal entity is dormant and therefore no operating budgets were prepared for the period under review.

GOVERNANCE

Risk identification and management

15. The municipal entity did not conduct a risk assessment as required by section 95(c)(i) of the MFMA.

Fraud prevention, detection and response

16. The municipal entity did not undertake a risk assessment to assess any risks of fraud and consequently did not develop a fraud prevention plan, as required by section 95(c)(i) of the MFMA

Internal audit

17. The municipal entity did not have an internal audit function in place as it is dormant and no transactions have taken place.

Audit committee

18. The audit committee did not meet prior to the submission of the financial statements for auditing on 30 July 2010, to review the adequacy, reliability and accuracy of the financial statements.

MATTERS THAT MAY POTENTIALLY IMPACT THE AUDITOR'S REPORT IN THE COMING YEAR

Accounting and compliance matters

19. Compliance with applicable reporting framework

Should the SA Standards of GRAP not be applied correctly when preparing the financial statements, the auditor's report could potentially be modified.

20. Compliance with legislation

Should the municipal entity not comply with all applicable laws and regulations, the auditor's report could potentially be modified.

RATINGS OF DETAILED AUDIT FINDINGS

21. For the purposes of this report, the detailed audit findings included in annexures A and B have been classified as follows:

- Matters to be included in the auditor's report.
These matters should be addressed as a matter of urgency.
- Other important matters – deficiencies that could adversely affect the entity's ability to initiate, record, process and report financial data consistent with the assertions of management on the financial statements and in accordance with the applicable basis of accounting. Unacceptable risk that errors and irregularities may occur that will not be prevented or detected by the internal controls in good time.
These matters should be addressed within the next 12 months.

22. Failure to address matters reported in a particular category may result in the matter being rated as more significant in the next financial year.

Yours sincerely



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City of Tshwane head of internal audit

SUMMARY OF DETAILED AUDIT FINDINGS

Page no.	Finding	Classification				Rating			In which year was it reported		
		Missstatements in Financial statements	Compliance	Internal control deficiency	Service delivery	Matters affecting the auditor's report	Other important matters	Administrative matters	Feb 2010	Feb 2009	Feb 2008
10	GRAP 1: Presentation of Financial Statements	<				<					
10	GRAP 2: Cash flow statements	<				<					
12	Non compliance with the MFMA	<	<			<					
13	Non-compliance with the Companies Act	<	<			<					
14	Non-compliance with the Municipal Systems Act	<	<			<					
15	Other non-compliance with the MFMA	<	<			<	<				
16	Other non-compliance with the Companies Act	<	<			<	<		>	>	>

ANNEXURE A: MATTERS AFFECTING THE AUDITOR'S REPORT

COMPLIANCE WITH APPLICABLE REPORTING FRAMEWORK

1. Compliance with SA Standards of GRAP

Audit finding

1.1 GRAP 1: Presentation of financial statements

The following paragraphs of GRAP 1 *Presentation of financial statements* were not complied with in the preparation of the annual financial statements:

Par. 09	The municipal entity did not use a permitted alternative name for the statement of financial performance.
Par. 23	No information was included in the financial statements regarding departure from the requirements of GRAP 1 in respect of budgetary information.
Par. 60	No disclosure has been made in the financial statements regarding the reason for the shortened financial period as well as the fact that the comparative figures were for a full financial year.
Par 141(c)	No reference has been made in the financial statements as to the legislation that governs the operations of the entity.

1.2 GRAP 2: Cash flow statements

SA Statements of GRAP, GRAP 2 *Cash flow statements* states that investing and financing activities that do not require the use of cash or cash equivalents shall not be included in the cash flow statements.

The inclusion of the movement in the shareholders loan does not represent a cash item and should therefore not be included in the cash flow statement. The municipal entity has not complied with this requirement.

Internal control deficiency

Leadership

The council is currently in the final stages of finalising the appointment of the board of directors of the entity. Therefore no oversight over the preparation of the financial statements occurred to ensure compliance with laws and regulations and internal control.

Financial management

The financial statements were not reviewed for completeness and accuracy prior to submission for audit.

Recommendation

All required disclosures in the financial statements should be made in accordance with SA Standards of GRAP.

Management response

The findings are noted. The statements will be amended accordingly and will be resubmitted to you.

Auditor's conclusion

The financial statements were amended to correct the above mentioned non compliance with GRAP 1, however, no amendments were made to correct the statement of cash flows to comply with GRAP 2. Furthermore, the following additional instances of non compliance with GRAP 1 were identified after the amendments were made:

- Par 110 (a) - The deficit for the period is referred to as "Total comprehensive loss for the 4 months" in the statement of changes in net assets and not deficit for the period.
- Par 101 - The balance of R16 723 disclosed as audit fees includes a balance of R3 681 incurred in respect of annual duties of the municipal entity as well as R13 042 incurred in respect of accounting fees. This has resulted in the incorrect classification of expenditure.
- Par 98 – The above annual duties and accounting fees are material due to the stage of operations of the entity. They are therefore required to be separately disclosed by the standard.
- Par 124(a) - The measurement base of the financial statements has not been disclosed under the accounting policy note.
- In addition to the above, management have disclosed that certain GRAP standards are not yet effective and that the municipal entity will adopt these standards when they become effective. They have indicated that only GRAP 1, 2 and 3 are applicable for the current year. As per *General Notice 522* issued in *Government Gazette 30013* dated 29 June 2007, municipal entities are required to be fully GRAP compliant from 30 June 2010. The following is a list of all GRAP standards that are applicable for the 30 June 2010 year end.

- GRAP 4 *The Effects of Changes in Foreign Exchange Rates*
- GRAP 5 *Borrowing Costs*
- GRAP 6 *Consolidated and Separate Financial Statements*
- GRAP 7 *Investments in Associates*
- GRAP 8 *Investment in Joint Ventures*
- GRAP 9 *Revenue from Exchange Transactions*
- GRAP 10 *Financial Reporting in Hyperinflationary Economies*
- GRAP 11 *Construction Contracts*
- GRAP 12 *Inventories*
- GRAP 13 *Leases*
- GRAP 14 *Events After the Reporting Date*
- GRAP 16 *Investment Property*
- GRAP 17 *Property, Plant and Equipment*
- GRAP 19 *Provisions, Contingent Liabilities and Contingent Assets*
- GRAP 100 *Non-current Assets Held for Sale and Discontinued Operations*
- GRAP 101 *Agriculture*
- GRAP 102 *Intangible Assets*

Due to the above findings, the audit report will be qualified on non-compliance with the SA Standards of GRAP.

COMPLIANCE WITH LAWS AND REGULATIONS

2. Non compliance with the MFMA

Audit finding

As per section 125 (2) (e) of the MFMA, all instances of non-compliance with the MFMA should be disclosed in the financial statements. No disclosures have been made in respect of the following non- compliance:

Section not complied with	Details of non compliance
Section 87(1)	No budget was prepared by management and submitted to the parent municipality for approval as the entity was dormant.
Section 95(c)(i)	The accounting officer did not ensure that the entity maintained effective, efficient and transparent systems of financial and risk management and internal control.
Section 111,112 and 115	No supply chain management policy was implemented by management as the entity was dormant.
Section 165	The municipal entity did not have an operational internal audit function in place as it was dormant.

Internal control deficiency

Leadership

The council is currently in the final stages of finalising the appointment of the board of directors of the entity. Therefore no oversight over the preparation of the financial statements occurred to ensure compliance with laws and regulations and internal control.

Financial and performance management

The municipal entity did not have appropriate systems to facilitate the preparation of the financial statements and reporting on non compliance with the MFMA.

Recommendation

All necessary disclosures should be made in the financial statements as prescribed by the MFMA and adequate oversight should be carried out to ensure that compliance is maintained.

Management response

The findings are noted. The entity is currently not operational. No transactions have been concluded. All the issues listed are only applicable if the entity is operational. Once the entity becomes operational, the matters listed will be addressed.

Auditor's conclusion

The financial statements have not been amended to include the above disclosures. The findings will therefore be included in the auditor's report.

3. Non compliance with the Companies Act

Audit finding

The following non compliance with the Companies Act was identified:

Section not complied with	Details of non compliance
Section 179(1)	The municipal entity did not hold an annual general meeting and no notice of waiver thereof was issued.
Section 286	The financial statements were not laid before the annual general meeting for approval.

Internal control deficiency

Leadership

Management did not exercise oversight responsibility over reporting and compliance with laws and regulations and internal control.

Recommendation

All relevant sections of the Companies Act should be complied with and the statutory documentation should be maintained and kept at the registered office of the entity.

Management response

The findings are noted. Once the board of directors has been appointed, the issues raised will be addressed.

Auditor's conclusion

Noted, however non-compliance with the Companies Act will be reported in the auditor's report.

4. Non compliance with the Municipal Systems Act

Audit finding

The municipal entity did not comply with section 93H(b) of the Municipal Systems Act as management did not ensure compliance with all applicable legislation and agreements. Various sections of the MFMA and the Companies Act were not adhered to.

Internal control deficiency

Leadership

Management did not exercise oversight responsibility over reporting and compliance with laws and regulations and internal control.

Recommendation

Management should ensure compliance with all applicable legislation and agreements.

Management response

The findings are noted. No accounting officer has been appointed. The entity is currently non-operational. The matter will be addressed once the board of directors has been appointed.

Auditor's conclusion

Noted, however non-compliance with the Municipal Systems Act will be reported in the auditor's report.

ANNEXURE B: OTHER IMPORTANT MATTERS

6. Other non compliance with the MFMA

Audit finding

As per section 125(2)(e) of the MFMA, all instances of non-compliance with the MFMA should be disclosed in the financial statements. No disclosures have been made in respect of the following non-compliance.

Section not complied with	Details of non compliance
Section 85(1)	The municipal entity did not open or maintain at least one bank account during the period as prescribed by this section.
Section 88	No mid-year budget performance assessment was performed due to the budget not being prepared.
Section 166(2)(b)	The entity's audit committee did not meet prior to the submission of the annual financial statements

Internal control deficiency

Leadership

The council is currently in the final stages of finalising the appointment of the board of directors of the entity. Therefore no oversight over the preparation of the financial statements occurred to ensure compliance with laws and regulations and internal control.

Financial and performance management

The municipal entity did not have appropriate systems to facilitate the preparation of the financial statements and reporting on non compliance with the MFMA.

Recommendation

All necessary disclosures should be made in the financial statements as prescribed by the MFMA and adequate oversight should be carried out to ensure that compliance is maintained.

Management response

The findings are noted. The entity is currently not operational. No transactions have been concluded. All the issues listed are only applicable if the entity is operational. Once the entity becomes operational, the matters listed will be addressed.

Auditor's conclusion

The financial statements have not been amended to include the above disclosures. The effect of this non-compliance is considered to be immaterial and will therefore not be included in the auditor's report.

7. Other non compliance with the Companies Act

Audit finding

The following non compliance with the Companies Act was identified:

Section not complied with	Details of non compliance
Section 92(1)	Cash or other consideration has not been received for the full value of shares issued.
Section 105 and 93	The authorised and issued share capital could not be confirmed with the register of members and share allotments.

Internal control deficiency

Leadership

Management did not exercise oversight responsibility over reporting and compliance with laws and regulations and internal control.

Recommendation

All relevant sections of the Companies Act should be complied with and the statutory documentation should be maintained and kept at the registered office of the entity.

Management response

The findings are noted. Once the board of directors has been appointed, the issues raised will be addressed.

Auditor's conclusion

Noted. The effect of this non-compliance is considered to be immaterial and will therefore not be included in the auditor's report.