

BUFFALO CITY ECONOMIC ENTITY

Annual Financial Statements for the year ended 30 June 2010

Notes to the Annual Financial Statements

Figures in Rand	Economic entity		Controlling entity	
	2010	2009	2010	2009

48. Related parties

Buffalo City Development Agency (BCDA) (a Section 21 company registration no 2004/016829/08):
The BCDA was incorporated on 18 June 2004 as a Municipal entity of BCM. BCDA is 100% controlled by BCM. BCM Council resolved to report all Agency related pre-incorporation financial transactions for the first time at 30 June 2005.

One of the envisaged corner-stones of the Agency's business model is the asset base of unutilised or underutilised public land and infrastructure that falls within the Agency's demarcated area, namely the extended waterfront and CBD area of East London.

In Buffalo City, this asset-base constitutes a resource of significant value that could be used as leverage to unlock beneficial synergies with other significant prospective investors, private and public.

Buffalo City Municipality has issued grants of R3 212 957 (VAT exclusive) to the development agency during the current financial year (2009: R 1 000 000 - VAT exclusive).

BCDA has paid consumer accounts of R22 633 during the current financial year (2009: R19 732).

There is an outstanding amount of R449 814 for the payment of output VAT by BCM at 30 June 2009.

Key management personnel information:

Annual Remuneration of the Chief Executive Officer (BCDA), 1 officer, was R524 265 (2009: R707 964)

Annual Remuneration of Senior Management (BCDA), 2 officers, was R879 189 (2009: R1 057 053)

No remuneration was paid to family of key personnel.

There are no share based payments.

There are no post-employment benefits for key personnel.

All Councillors and Employees have disclosed their interest in related parties and no one has the ability to control or exercise significant influence over Council in making financial and operating decisions.

BUFFALO CITY ECONOMIC ENTITY

Annual Financial Statements for the year ended 30 June 2010

Notes to the Annual Financial Statements

Figures in Rand	Economic entity		Controlling entity	
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49. Correction of errors				
During the year the following adjustments were made to transactions whereby amounts were erroneously stated in previous financial periods:				
The correction of the error(s) results in adjustments to the accumulated surplus as follows:				
Corrections included:				
Reversing creditors in correctly accrued - trade payables overstated	-	998,089	-	998,089
Adjusting rental income iro operating leases incorrectly calculated in prior years	-	828,463	-	828,463
Operating grants included under unspent conditional grants, was understated due to more information relating to operating grants/subsidies coming to attention during 2010	-	13,968,447	-	13,968,447
Capitalizing leased assets which were not raised in 2009	-	372,733	-	372,733
Expenditure included under wip/under construction was overstated due to more information relating to expenditure i.r.o. weighbridge design coming to attention during 2010	-	(345,311)	-	(345,311)
Reversing retentions due to contractors as contracts were cancelled - retention monies overstated	-	5,510,417	-	5,510,417
Over expenditure grants operating projects	-	(906,195)	-	(906,195)
Correction of movable assets taken on in prior years	-	6,166,953	-	6,166,953
Correction to lease assets not recognised in prior years	-	97,619	-	97,619
Correction of accumulated depreciation i.r.o.roads and electricity network not recognised in prior years	-	(298,055)	-	(298,055)
Adjustment to operating lease asset	-	7,467,201	-	7,467,201
Adjustment of revaluation reserve from initial measurement to remeasurement	-	4,955,054,926	-	4,955,054,926
	-	4,988,915,287	-	4,988,915,287

Financial Period 2009

Corrections summarised:

Trade and other payables	22	-	6,508,506	-	6,508,506
Unspent conditional grants	23	-	13,968,447	-	13,968,447
Trade and other receivables from non-exchange transactions	6	-	(906,195)	-	(906,195)
PPE	15	-	5,621,206	-	5,621,206
Operating lease asset	8	-	8,295,664	-	8,295,664
Finance lease obligation	20	-	372,733	-	372,733
Revaluation reserve		-	4,955,054,928	-	4,955,054,926
Net effect on accumulated surplus		-	4,988,915,289	-	4,988,915,287

The correction of the error(s) results in adjustments to the statement of financial performance as follows:

Statement of financial performance 2009

BUFFALO CITY ECONOMIC ENTITY

Annual Financial Statements for the year ended 30 June 2010

Notes to the Annual Financial Statements

Figures in Rand	Economic entity		Controlling entity	
	2010	2009	2010	2009
49. Correction of errors (continued)				
Public contributions-PPE Accrued income included under other debtors (BCMET) was overstated due to more information relating to DBSA funding coming to attention during 2010 - accrued income overstated.	-	(4,546,053)	-	(4,546,053)
Service charges - Apportioning prepaid electricity purchased in advance for 2009.	-	(6,762,976)	-	(6,762,976)
Interest received- investments: reversing interest earned on unspent conditional grants incorrectly recognised	-	(36,752,771)	-	(36,752,771)
General expenses insurance: adjusting transaction Coid and insurance i.r.o 2009	-	8,225,024	-	8,225,024
Overspending of grant funds adjusted 08/09	-	(3,461,136)	-	(3,461,136)
Correction of accumulated depreciation i.r.o. roads, electricity network, water network, and sewer network not recognised in prior years	-	(187,340,839)	-	(187,340,839)
Adjustment of interest on investments incorrectly capitalised against unspent grants.	-	18,527,281	-	18,527,281
Overspending of grant funds after adjustment of interest capitalised	-	(648,705)	-	(648,705)
Adjustment of depreciation landfill site KWT	-	(3,875,417)	-	(3,875,417)
Time value for money on payables.	-	2,515,474	-	2,515,474
	-	(214,120,118)	-	(214,120,118)
Total correction of error				
Statement of financial performance	-	(214,120,118)	-	(214,120,118)
Accumulated surplus	-	4,988,915,287	-	4,988,915,287
	-	4,774,795,169	-	4,774,795,169

50. Risk management

Capital risk management

The economic entity's objectives when managing capital are to safeguard the economic entity's ability to continue as a going concern in order to provide returns for member and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

The capital structure of the municipality consists of debt, which includes the borrowings, cash and cash equivalents and equity.

There have been no changes to what the economic entity manages as capital, the strategy for capital maintenance or externally imposed capital requirements from the previous year.

Financial risk management

The economic entity's activities expose it to a variety of financial risks: market risk (including currency risk, fair value interest rate risk, cash flow interest rate risk and price risk), credit risk and liquidity risk.

The economic entity's overall risk management program focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the economic entity's financial performance. Risk management is carried out under policies approved by the accounting officer. The accounting officer provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk and investment of excess liquidity.

Liquidity risk

The economic entity's risk to liquidity is a result of the funds available to cover future commitments. The economic entity manages liquidity risk through an ongoing review of future commitments and credit facilities.

BUFFALO CITY ECONOMIC ENTITY

Annual Financial Statements for the year ended 30 June 2010

Notes to the Annual Financial Statements

Figures in Rand	Economic entity		Controlling entity	
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50. Risk management (continued)

Cash flow forecasts are prepared and adequate utilised borrowing facilities are monitored.

Interest rate risk

As the economic entity has no significant interest-bearing assets, the economic entity's income and operating cash flows are substantially independent of changes in market interest rates.

The economic entity's interest rate risk arises from long-term borrowings. Borrowings issued at variable rates expose the group to cash flow interest rate risk. Borrowings issued at fixed rates expose the economic entity to fair value interest rate risk.

Cash flow interest rate risk

Financial instrument	Current interest rate	Due in less than a year	Due in one to two years	Due in two to three years	Due in three to four years	Due after five years
Trade and other receivables	9.00 %	458,602,463	-	-	-	-
Trade and other receivables - normal credit terms	- %	(231,600,150)	-	-	-	-
Cash in current banking institutions	5.00 %	57,302,936	-	-	-	-
Call investment deposits	6.56 %	502,168,153	-	-	-	-
Trade and other payables	8.00 %	(231,600,150)	-	-	-	-
Long term borrowings	10.69 %	(39,905,379)	(32,091,653)	(67,424,305)	(106,121,729)	(291,168,059)

These amounts best represent maximum exposure to credit risk at the end of the reporting period without taking account of any collateral held or other credit enhancements.

Sensitivity Analysis of Market Risk

Effect of a 1% change in the prime rate	%	Value 30/06/2010	Discounted value at current rate	Discounted value at current rate (-1%)	Discounted value at current rate (+1%)
Amortisation of financial instruments					
Trade and other receivables	9.00 %	458,602,463	420,736,205	424,631,910	416,911,330
Trade and other payables	8.00 %	(231,600,150)	(214,444,583)	(216,448,738)	(212,477,202)
Cash and cash equivalents					
Cash in current banking institutions	5.00 %	57,302,936	54,574,225	55,098,977	54,059,374
Call investment deposits	6.56 %	502,168,153	471,253,897	475,718,220	466,872,586

The sensitivity analysis was based on the assumption that a 1% increase or decrease in the prime rate could occur. The method used to prepare the sensitivity analysis was based on the discounted value of the respective cash flow for 1 year using the respective current interest rate in order to determine the effect of applicable market risk of a 1% increase or decrease in the prime rate.

Credit risk

Credit risk consists mainly of cash deposits, cash equivalents and trade debtors. The municipality only deposits cash with major banks with high quality credit standing and limits exposure to any one counter-party.

Trade receivables comprise a widespread customer base.

51. Going concern

The annual financial statements have been prepared on the basis of accounting policies applicable to a going concern. This basis presumes that funds will be available to finance future operations and that the realisation of assets and settlement of liabilities, contingent obligations and commitments will occur in the ordinary course of business.

The ability of the economic entity to continue as a going concern is dependent on a number of factors. The most significant of these is that the accounting officer continue to procure funding for the ongoing operations for the economic entity.

BUFFALO CITY ECONOMIC ENTITY

Annual Financial Statements for the year ended 30 June 2010

Notes to the Annual Financial Statements

Figures in Rand	Economic entity		Controlling entity	
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52. Events after the reporting date

At the time of preparing and submitting the Annual Financial Statements there were no subsequent events to disclose.

53. Fruitless and wasteful expenditure

Payment of commitment fee to DBSA	199,703	-	199,703	-
Payment of interest to SARS	164	3,368	-	-
	199,867	3,368	199,703	-

Incident - During November 2008 DBSA issued an invoice amounting to R 199 703 with regard to commitment fees due as a result of the slow rate of capital expenditure. BCM'S application to waive the commitment fee has been unsuccessful. A report was submitted to the Mayoral Committee.

54. Irregular expenditure

Add: Irregular Expenditure - current year	46,622	-	-	-
	46,622	-	-	-

Analysis of expenditure awaiting condonation per age classification

Prior years	-	23,390,731	-	23,390,731
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Details of Irregular Expenditure – Current year

Procurement process not followed				4,790
Contracts expired				41,832
				46,622

Details of Irregular Expenditure not recoverable (not condoned)

Payment made from investment vote whereby supporting documentation - misplaced/missing	880,654
Tender award - Irregularities - Neo Solutions	2,278,189
Tender award - Irregularities - Waste Rite	20,231,888
	23,390,731

BUFFALO CITY ECONOMIC ENTITY

Annual Financial Statements for the year ended 30 June 2010

Notes to the Annual Financial Statements

Figures in Rand	Economic entity		Controlling entity	
	2010	2009	2010	2009
55. In-kind donations and assistance				
BCM received the services of Dr. J Rausch - German Development Services	159,642	476,256	159,642	476,256
FELA donated amount to BCM	-	54,241	-	54,241
FELZOO donated amount to BCM	-	71,594	-	71,594
	159,642	602,091	159,642	602,091

56. Additional disclosure in terms of the Municipal Finance Management Act

Contributions to SALGA

Opening balance	-	-	-	-
Council subscriptions	3,972,247	2,642,289	3,972,247	2,642,289
Amount paid - current year	(3,972,247)	(2,642,289)	(3,972,247)	(2,642,289)
Balance unpaid	-	-	-	-

Contributions to SA Cities Network

Opening balance	-	-	-	-
Council subscriptions	241,577	219,615	241,577	219,615
Amount paid - current year	(241,577)	(219,615)	(241,577)	(219,615)
Balance unpaid	-	-	-	-

Audit fees

Opening balance	-	-	-	-
Current year fee	3,783,357	3,006,765	3,783,357	3,006,765
Amount paid - current year	(3,783,357)	(3,006,765)	(3,783,357)	(3,006,765)
Balance unpaid	-	-	-	-

PAYE and UIF

Opening balance	-	-	-	-
Current year payroll deductions	88,990,900	76,513,646	88,990,900	76,513,646
Amount paid - current year	(88,990,900)	(76,513,646)	(88,990,900)	(76,513,646)
Balance unpaid	-	-	-	-

Pension and Medical Aid Deductions

Opening balance	-	-	-	-
Current year payroll deductions and Council contributions	185,123,351	155,612,404	185,123,351	155,612,404
Amount paid - current year	(185,123,351)	(155,612,404)	(185,123,351)	(155,612,404)
Balance unpaid	-	-	-	-

VAT

VAT output payables and VAT input receivables are shown in note 7 as net VAT receivable.

All VAT returns have been submitted by the due date throughout the year. VAT is only declared to SARS on receipt of payment from consumers.

Councillors' arrear consumer accounts

BUFFALO CITY ECONOMIC ENTITY

Annual Financial Statements for the year ended 30 June 2010

Notes to the Annual Financial Statements

Figures in Rand	Economic entity		Controlling entity	
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56. Additional disclosure in terms of the Municipal Finance Management Act (continued)

Arrear Councillors accounts totalling R 870 were outstanding for more than 90 days at 30 June 2010 for which mechanisms are in place to deduct amounts from the monthly allowances of each Councillor.

Material losses

Unaccounted electricity losses for the 2009/10 financial year amounted to 8.59% i.e. R 2 833 270. (2008/09 : 8.56% i.e. R 1 539 480)

Unaccounted water losses for the 2009/10 financial year amounted to 39.91% i.e. R 68 776 198. (2008/09 : 44.86% i.e. R 76 243 345)

Irregularities were identified whereby fuel pump readings differed from fuel issue forms which resulted in irregular expenditure in respect of fuel usage. The irregular expenditure identified was in the amount of R 27 474 which when extrapolated over the total fuel expense of R 24 652 027 amounts to R 6 412 493. A electronic fuel master system is being considered to eliminate these problems.

57. Utilisation of Long-term liabilities reconciliation

Long-term liabilities raised	-	65,719,967	-	65,719,967
Finance leases taken up	1,637,433	639,302	1,637,433	639,302
Used to finance property, plant and equipment & finance leases i.r.o 2009/10	(1,637,433)	(66,359,269)	(1,637,433)	(66,359,269)
Cash set aside for the repayment of long-term liabilities	-	2,385,344	-	2,385,344

Long-term liabilities have been utilized in accordance with the Municipal Finance Management Act.

58. Retirement benefit information

The employees of the Council as well as the Council as employer, contribute to Municipal Pension, Retirement and various Provident Funds as listed below:

- Cape Joint Pension Fund
- Cape Joint Retirement Fund
- Eastern Cape Local Authorities Provident Fund
- Government Employees Pension Fund
- SAMWU National Provident Fund
- SALA Pension Fund
- East London Municipal A Band Provident Fund
- Old Mutual Orion Provident Fund
- Aftredevoorsieningsfonds vir Kaapse Plaaslike Owerhede
- Municipal Employees Pension Fund

The Cape Joint Pension Fund's last actuarial valuation was at 30 June 2009 conducted by S. Neethling from Metropolitan Life Limited. The fund was in a sound financial position. Although this fund is a defined benefit plan it cannot be accounted as such as it is part of a multi-employer plan. In the event of the fund being under funded Council's liability would be limited to increased monthly contributions.

The Eastern Cape Local Authorities Provident Fund's last valuation was at 30 June 2009 conducted by E. Du Toit from Alexander Forbes Financial Services who certified that the structure of the assets and the matching of the assets with the liabilities is adequate.

The Government Employees Pension Fund's last valuation was at 31 March 2008 conducted by G. Barnard from Alexander Forbes Financial Services. The fund was considered to be financial sound.

SAMWU National Provident Fund's last actuarial valuation was at 30 June 2005 conducted by E. Potgieter from Fifth Quadrant Actuaries & Consultants (Pty) Ltd. The report stated that the fund was in a sound financial position.

The SALA Pension Fund's last valuation was at 30 June 2009 conducted by J.F. Rosslee of Genesis Actuarial Solutions. The fund was 96% funded as at valuation date. Low investment returns resulted in a decrease from 110% .Although this fund is a defined benefit plan it cannot be accounted as such as it is part of a multi-employer plan. Although the fund is less than 100 % funded no additional action was recommended.

The Municipal Employees Pension Fund's last valuation was at 29 February 2009 prepared by Itakane Consultants and Actuaries (Pty) Ltd. The funding level was 102.2% at this date.

BUFFALO CITY ECONOMIC ENTITY

Annual Financial Statements for the year ended 30 June 2010

Notes to the Annual Financial Statements

Figures in Rand	Economic entity		Controlling entity	
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58. Retirement benefit information (continued)

It is Council's policy to fund 60% of Pensioner's medical aid expenses. The current costs amount to approximately R 11.6 million.

An amount of R 126.7 million (2009: R 107.3 million) was contributed by Council, Councillor's and employee's in respect of Councillor and employee's retirement funding. These contributions have been expensed.

The East London Municipal A Band and Old Mutual Orion Provident Funds as well as the Afredevoorsieningsfonds vir Kaapse Plaaslike Owerhede are fixed/ defined contribution funds. It is therefore not necessary to perform actuarial valuations for these funds.

The Cape Retirement Fund's last actuarial valuation was at 30 June 2009 conducted by S Neethling from Metropolitan life Limited who certified that the fund was in a sound financial position.

59. Change in estimate

Property, plant and equipment

The useful lives and residual values of certain vehicles were estimated in 2008 and have since been reviewed by management during the current period. The effect of this revision has increased /(decreased) the depreciation charges for the current and future periods as indicated in the table below.

Effect on depreciation

Change in residual values	-	1,487,907	-	1,487,907
Change in estimated useful lives	-	669,151	-	669,151
	-	2,157,058	-	2,157,058

Other

A lease escalation of 10% was not exercised by the supplier but the entity applied this escalation. This escalation has been reversed and treated as a change in accounting estimate.

The impact on the current year is to decrease the carrying amount of the deferred lease liability and increase the surplus by R 12 168.

60. Financial assets by category

The accounting policies for financial instruments have been applied to the line items below:

Economic entity - 2010

	Loans and receivables	Fair value through surplus or deficit - designated	Total
Trade and other receivables	458,132,377	-	458,132,377
Cash and cash equivalents	559,471,089	-	559,471,089
Non current investment	2,442,805	1,968,141	4,410,946
	1,020,046,271	1,968,141	1,022,014,412

Economic entity - 2009

	Loans and receivables	Fair value through surplus or deficit - designated	Total
Trade and other receivables	337,950,245	-	337,950,245
Cash and cash equivalents	696,859,146	1,428,755	698,287,901
	1,034,809,391	1,428,755	1,036,238,146

61. Mapping adjustments to prior statements

BUFFALO CITY ECONOMIC ENTITY

Annual Financial Statements for the year ended 30 June 2010

Notes to the Annual Financial Statements

Figures in Rand	Economic entity		Controlling entity	
	2010	2009	2010	2009
61. Mapping adjustments to prior statements (continued)				
The reason for reclassifications as detailed hereunder was because of incorrect mapping of accounts on the caseware system in the 2008/09 financial year. As management's intention is to add value to the fair presentations of the AFS it was necessary to initiate these mapping adjustments.				
Statement of financial performance				
Dividends received from Revenue to Investment revenue	-	165,458	-	165,458
General expenses				
Commission paid from collection costs to commission paid	34	6,961,296	-	6,961,296
Legal fees from collection costs to consulting and professional fees		5,770,602	-	5,770,602
Collection costs from detailed income statement to other expenditure		(12,731,898)	-	(12,731,898)
Materials from stores and materials to consumables		4,547,257	-	4,547,257
Stores and materials		(4,547,257)	-	(4,547,257)
Expenditure on books from other expenses to magazines, books and periodicals		1,730,677	-	1,730,677
Fuel and oil from other expenses to fuel and oil		449,089	-	449,089
Courier services from other expenses to postage and courier		15,270	-	15,270
Motor vehicle licenses to motor vehicle expenses from other expenses and royalties and licenses		2,490,641	-	2,490,641
License fees paid reallocated to royalties and licence fees from other expenses		5,979,291	-	5,979,291
Royalties and license fees		(908,839)	-	(908,839)
Departmental fire service charges		(67,913)	-	(67,913)
Other expenses		(9,688,216)	-	(9,688,216)
		-	-	-
Revenue				
From rendering of services to rates and rates penalties imposed	28	363,493,111	-	363,493,111
Transfers from revenue		-	-	-
Dividends received from Revenue to Investment revenue		165,458	-	165,458
From other services to other income (Admin fees)		1,846,962	-	1,846,952
		365,505,531	-	-
Statement of financial performance				
Dividends received from Revenue to Investment revenue	38	1,658,458	-	165,458
Service charges				
From refuse removal to sewerage charges	30	128,521,741	-	128,521,741
From other services to other income (Admin fees)		1,846,952	-	1,846,952
		130,368,693	-	130,368,693

BUFFALO CITY ECONOMIC ENTITY

Annual Financial Statements for the year ended 30 June 2010

Notes to the Annual Financial Statements

Figures in Rand	Economic entity		Controlling entity	
	2010	2009	2010	2009
61. Mapping adjustments to prior statements (continued)				
Government grants and subsidies 31				
Government grants and subsidies AFS 2009	-	31,701,952	-	31,701,952
Less: trf to public contr operating exp - detailed I&E statement	-	(10,596,479)	-	(10,596,479)
trf to public contr PPE - detailed I&E statement	-	(85,382)	-	(85,382)
	-	21,020,091	-	21,020,091
Employee related costs 35				
Adjustment made incorrectly to other allowances transferred to 13th cheques	-	107,157	-	107,157
Grants and subsidies paid 44				
Transferred from general expenses	-	11,667,489	-	11,667,489
Other revenue 32				
Other income per AFS 2009	-	98,392,497	-	98,392,497
Transferred from other services - note 28	-	1,846,952	-	1,846,952
	-	100,239,449	-	100,239,449
62. VAT payable				
Tax refunds payables	405,894	681,545	-	-
63. Impairment of assets				
Impairments				
Property, plant and equipment	-	255	-	-
Describe the events and circumstances that led to the recognition or reversal of the impairment loss. The recoverable amount of the asset was based on its fair value less costs to sell or [its value in use.]				
64. Taxation				
Major components of the tax expense				
Deferred				
Deferred tax	5,774	2,636	-	-
Reconciliation of tax expense				
Accounting gain or (loss)	733,676	(423,260)	-	-
Taxation				
Taxation at the applicable tax rate 28% (2009: 28%)	205,429	(118,513)	-	-
Tax losses carried forward	-	121,149	-	-
Tax losses utilised	(199,655)	-	-	-
	5,774	2,636	-	-