**STATUS UPDATE OF IRREGULAR, FRUITLESS & WASTEFUL EXPENDITURE (IFWE)**

The SABC has detailed the following requests by the members of SCOPA for a meeting scheduled for the 17th May 2017:

* Detailed information regarding contract with Sekela Xabiso
* Update report on irregular, fruitless and wasteful expenditure (IFWE)

 The intention of this briefing document is to provide a detailed background to the misunderstanding and the difference in expectation between the SABC and members of SCOPA, emanating from the SCOPA visit on the 28th March 2017. The reasons for the misunderstanding are detailed below:

* **External auditor’s audit opinion**

Below is the IFWE amounts disclosed by the SABC in the annual reports:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Financial Year** | **Irregular expenditure****R’000** | **Fruitless & wasteful expenditure****R’000** | **Overstatement** | **Understatement** | **Poor documentation** |
| **15/16** | 5 148 526 | 92 461 | **X** | **X** | **X** |
| **14/15** | 2 677 521 | 60 985 |  | **X** | **X** |
| **13/14** | 3 376 809 | 42 000 | **X** | **X** | **X** |
| **12/13** | 106 322 | 22 116 |  |  | **X** |
| **11/12** | 136 960 | 104 615 |  |  | **X** |

The SABC has been receiving qualified audit opinion on its disclosure of irregular, fruitless and wasteful expenditure for the past five financial years. The disclosure numbers were reported by the SABC and are cumulative. The external auditors expressed a negative audit opinion that these numbers could not be reliable and accurate. What has been prevalent in these financial years is poor records management.

The R5.1 billion (cumulative for the past five years) was the amount detected and reported by the SABC as irregular expenditure in the 2015/16 financial year. As depicted in the table above, this amount was found to be unreliable, incomplete and inaccurate by the AGSA after they performed their audit tests.

* **Process to resolve audit qualification**

In order to resolve the audit qualification, the process entailed revisiting all the expenditure/ payments made in the financial years when the SABC received the qualification. The process started in the 2012/13 financial year where the SABC had to revisit all expenditure/ payments made in the 2011/12 financial year. This process was performed using the internal capacity (procurement division employees). The process did not yield the anticipated outcome. Similar process was followed again in 2013/14 financial year. Again the process did not yield the anticipated outcome. Deficiencies/ weaknesses noted using this process is as follows:

* Procurement division was not capacitated to under such engagement
* Record management was previously decentralized, meaning procurement documents were located everywhere in SABC
* Electronic filing was not optimally utilized, meaning alternative ways of sourcing such documentation was impractical
* Procurement personnel had to both deliver on their daily operational duties whilst involved in the detecting of IFWE project
* Lack of supply chain analytical expertise to identify expenditure/ payments which meet the definition IFWE

It became apparent that using the internal resources was not resolving the IFWE qualification by the external auditors. The SABC required experienced and reputable independent firm to undertake such project objectively and diligently. This therefore reported in the appointment of Sekela Xabiso (SkX) in the 2014/15 financial year.

* **Scope of the independent firm**
* Phase 1

Appointment date: 7 April 2015 to 31 July 2015

Contract value: R4 797 596

Scope of services (summary):

* Preparation of IFWE disclosure note for the 2014/15 annual financial statements
* Updating of the cumulative IFWE registers/ schedules
* Audit support during the testing by the AGSA (2014/15 audit process)
* Phase 2

Appointment date: 1 December 2015 to 31 July 2016

Contract value: R10 395 375

Scope of services (summary):

* Review of the SCM policy to ensure alignment to applicable laws & regulations
* Assist Supply Chain & Finance division with enforcement controls to prevent IFWE
* Preparation of IFWE registers (including the disclosure note for the annual financial statements)
* Review of IFWE disclosed in the previous years’ annual reports
* Audit support during the testing by the AGSA (2015/16 audit process)
* *Phase 3*

Appointment date: 1 November 2016 to 31 July 2017

Contract value: R9 816 023.52

Scope of services (summary):

* Comprehensive evaluation of expenditure/ payments for the finacila years affected by the audit qualification
* Updating of the cumulative IFWE registers/ schedules
* Review of the IFWE already disclosed by the SABC in the previous annula reports for completeness and accuracy
* Preparation of IFWE disclosure note for the 2016/17 annual financial statements
* Preparation of the portfolio of evidence for the IFWE registers/ schedules
* Determination of IFWE causes/ incidents
* Audit support during the testing by the AGSA (2016/17 audit process)

* **Challenges faced by independent firm (Phase 1 & 2)**

The following core challenges were experienced during the first two phases of the project:

* Not all the procurement documents were retrieved during the detection of irregular expenditure, due to the decentralization
* There wasn’t effective co-operation and co-ordination between divisions and independent firm
* There was insufficient timeline to effectively execute all the services in the scope
* Expenditure/ payments were not easily linked to procurement documents due to poor contract management
* IFWE was possible non-compliances which thereafter had to be followed up and re-verified
* Suggested internal controls were still not fully effectively implemented for both prevention and detection of IFWE by the SABC

The above challenges necessitated a detailed follow up of the possible non-compliances to determine whether they all meet the definition of IFWE. More detailed work was also required in collating all the procurement documents to ensure that they are located centrally. Second phase had to be extended into the third phase, mainly due to:

* Significant amount of ground work which had been performed in the previous phases
* Learning curve benefits which would assist in efficiencies and effectiveness
* Understanding of SABC challenges (highlighted above) and effective methodologies implemented. Elimination of the investment costs in starting a new engagements
* **Project approach/ methodology (Phase 3)**

The project approach followed in this was mainly built in the strides achieved in the previous two phases. The following process was implemented/ being implemented:

* Collate all the procurement documents/ files located in different divisions, especially documents located in the provinces
* Clearly defining to all the SABC personnel what constitutes procurement documents, in ensuring that all documents kept in personal filing cabinets and archives are centralized
* These files were tested for compliance with the SCM policies (including Delegation of Authority) and treasury guidelines
* These files were traced to the respective expenditure/ payments made (for the 2016/17 financial year and previous years)
* Any payments/ expenditure which could not be traced to procurement files, were then traced to the supporting documents electronically attached on the accounting system
* Remainder of the payments/ expenditure which may neither be traced to the physical files nor electronic attachments are then being followed up by the Heads of Divisions
* The draft IFWE registers/ schedules have been shared with the AGSA for the interim audit testing
* The final IFWE and disclosure note will then be submitted to the AGSA when the SABC is submitting the annual financial statements on the 31st May 2017.
* **Analysis of IFWE (status update)**

Below is the analysis of irregular expenditure identified/ verified thus far categorized under respective incidents:

* Content

| **Incidents** | **2016/17****R’000** | **2015/16****R’000** | **2014/15****R’000** | **2013/14****R’000** | **2012/13****R’000** |
| --- | --- | --- | --- | --- | --- |
| Content acquisition process for unsolicited offers not followed |  | 3,297 |  |  |  |
| Re-commissioning process not followed | 10,584 |  | 75 |  |  |
| Evaluation criteria not followed | 358 | 447 | 1,192 | 29,281 | 1,499 |
| No valid (Original) Tax Clearance Certificate | 51,403 | 236,363 | 350,752 | 770,384 | 877,967 |
| Delegation of Authority Framework contravention |  |  |  | 6 |  |
| Insufficient documentation | 916 |  | 72,163 | 215 | 233 |
| **Total** | **63,261**  | **240,107** | **424,182** | **799,886** | **879,699** |

* Normal procurement

| **Incidents** | **2016/17****R’000** | **2015/16****R’000** | **2014/15****R’000** | **2013/14****R’000** | **2012/13****R’000** |
| --- | --- | --- | --- | --- | --- |
| Delegation of Authority Framework contravention | 78,621  | 81,084 | 49,157 | 26,941 | 19,446 |
| Irregular contracts due to lack of planning | 236,211 | 254,388 | 211,796 | 107,584 | 32,986 |
| Minimum number of quotes not obtained | 29,166 | 76,091 | 51,239 | 35,337 | 9,900 |
| No valid (Original) Tax Clearance Certificate | 24,906 | 37,497 | 51,722 | 41,485 | 18,377 |
| Incorrect evaluation of bids | 12,470 | 42,504 | 35,497 | 6,329 |   |
| Bids not advertised for minimum period as per policy | 59,434 | 15,505 | 40,235 | 12,663 | 4,312 |
| Insufficient documentation | 138,758 | 322,733 | 207,871 | 162,347 | 260,831 |
| **Total** | **579,566** | **829,802** | **647,517** | **392,686** | **345,852** |

* Consolidated/ cumulative irregular expenditure

|  |  |  |
| --- | --- | --- |
| **Incidents** | **%** | **Total****R’000** |
| Content acquisition process for unsolicited offers not followed | 0% | 3,297 |
| Re-commissioning process not followed | 0% |  10,659.00  |
| Incorrect evaluation of bids/ not followed | 2% |  129,577.00  |
| No valid (Original) Tax Clearance Certificate | 47% |  2,460,856.00  |
| Delegation of Authority Framework contravention | 5% |  255,255.00  |
| Irregular contracts due to lack of planning | 16% |  842,965.00  |
| Minimum number of quotes not obtained | 4% |  201,733.00  |
| Bids not advertised for minimum period as per policy | 3% |  132,149.00  |
| Insufficient documentation | 22% |  1,166,067.00  |
| **Total** | **100%** | **5,202,558** |

The total cumulative irregular expenditure, thus far, to be disclosed in the 2016/17 annual financial statements will be R5.2 billion. R2.4 billion emanates from the content acquisition, whilst R2.8 billion comes from normal procurement. Bulk of this irregular expenditure was due to the SCM policy in the past not being aligned to the requirements of PPPF Act (original tax clearance not obtained). Historical poor records management is also a driver of the possible irregular expenditure. Due to the impracticability of locating these procurement documents (to the value of R1.2 billion), after the SABC has done everything possible, it is prudent to disclose these as irregular expenditure.

Below is the analysis of fruitless and wasteful expenditure:

|  |  |
| --- | --- |
| **Incidents** | **Amount** |
| **Opening balance** | 92,461 |
| Less: Reversal of incorrectly disclosed prior year amount | (21,655) |
| **Restated opening balance** | 70,806 |
| Impairment of foreign and sports content | 2,706 |
| Travel cancellation fees and penalties | 472 |
| Interest, penalties and fines on late payments | 69 |
| **Closing balance** | **R74 053** |

The majority of fruitless and wasteful expenditure incurred is as a result of international content which is written off due to license contracts expiring without broadcasting.

The AGSA is still yet to express an audit opinion on the accuracy and completeness of these numbers of IFWE before initiating adequate consequence management.

* **Consequence management**

The AGSA will then undertake their final audit process from the 1st June 2017 and will express an audit opinion on the 31st July 2017. Once the IFWE has been confirmed to be accurate and complete, then the process as required by section 51(1)(e) of PFMA will implemented as followed:

* Effective and appropriate disciplinary steps against employees:

Any fruitless and wasteful expenditure maliciously incurred/ permitted in vain and could have avoided would then be recovered from affected employees. For example, an who had a flight booking and did not honour it without giving any valid reasons.

Where there are indications that some fraudulent activities have occurred, these will be referred to the forensic investigation process. Outcome of that process will then determine appropriate steps to be taken to the affected employee.

* Deficiencies in the SABC policies and processes

Instances where it’s clearly evident that irregular expenditure was incurred due to the shortfalls of the policies and procedures, the Board would have to satisfy itself that these have been rectified through updated policies. Then consideration will be given to condone such irregular expenditure. For example, the SCM policy did not specify that original tax clearance had to be obtained from the supplier at the date of award.

The above process will performed from August 2017 onwards until the total R5.2 billion has been condoned/ recovered.

* **Sustainable improvements in the control environment**

The following improvements in the internal control environment have been implemented in order to both prevent and detect IFWE going forward:

* The procurement system has been re-configured in order to:
* Force every employee to attach the procurement documents on the system before proceeding)
* link every payments/ expenditure to unique Request For Quotation/ contract/ deviation
* detect expenditure which has not complied with the SCM processes and include it in the registers
* Improve contract management
* SCM policy and procedure manuals have been updated
* The introduction of National Treasury Central Supplier Database has assisted with the tax clearance certificates deficiencies
* IFWE is tracked and reported on a monthly basis analysis to the CFO
* There is ongoing training of staff by governance personnel within the supply chain division
* **Conclusion**

Due to the above stated reasons, the contractual arrangement with SkX was not to recover IFWE but to detect accurate and complete disclosure note. The deliverables from the firm are the IFWE schedules/ registers and the disclosure note for the annual financial statements for 2016/17 financial year.

The details of the contract and the expected deliverables have been given above.