



AUDITOR - GENERAL  
SOUTH AFRICA

# **Budgetary Review and Recommendations Report**

## **Portfolio Committee on Public Enterprises**

9 November 2021

## Our mission and vision

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### OUR MISSION

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We have a constitutional mandate and, as the supreme audit institution of South Africa, exist to strengthen our country's democracy by enabling oversight, accountability and governance in the public sector through auditing, thereby building public confidence.



### OUR VISION

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To be recognised by all our stakeholders as a relevant supreme audit institution that enhances public sector accountability

# Mandate for the AGSA and portfolio committees

## AGSA mandate

### Constitution section 188

AGSA must audit and report on accounts, financial statements and financial management of government institutions

### PAA section 20(2)

- AGSA must prepare an audit report containing an opinion/conclusion on:
  - the fair presentation of the financial statements
  - compliance with applicable legislation
  - reported performance against predetermined objectives
- Discretionary audits (including special audits, investigations and performance audits).

### Section 5(1B)

- Auditor-General has the power :
  - to take an appropriate remedial action
  - where an accounting officer/authority has failed to comply with remedial action, to issue a certificate of debt, as prescribed.

## Portfolio committees

### National Assembly Rule 227

Portfolio committees may, amongst other things, perform the following functions:

- Deal with bills and other matters falling within their portfolio, as referred to them in terms of the constitution, legislation or rules, or by resolution of the Assembly
- Maintain oversight of their portfolios of national executive authority, including implementation of legislation
- Consult and liaise with any executive organ of state or constitutional institution
- Monitor, investigate, enquire into and make recommendations concerning any such executive organ of state, constitutional institution or other body or institution, including the legislative programme, budget, rationalisation, restructuring, functioning, organisation, structure, staff and policies of such organ of state, institution or other body or institution

## Role of the AGSA in the reporting process

Our role as the Auditor-General of South Africa (AGSA) is to reflect on the audit work performed to assist the portfolio committee in its oversight role of assessing the performance of entities, taking into consideration the committee's objective to produce a *Budgetary review and recommendations report* (BRRR).



# What we understand as the role of oversight

Use information in audit report on material irregularities for accountability and oversight purposes, insisting on timeous implementation of recommendation

Obtain reports on investigations conducted into transgressions and irregularities and effecting entity

Use reports tabled on progress with material irregularities to oversee and influence progress made by public bodies with investigations and executive authorities (for recovery of debt).

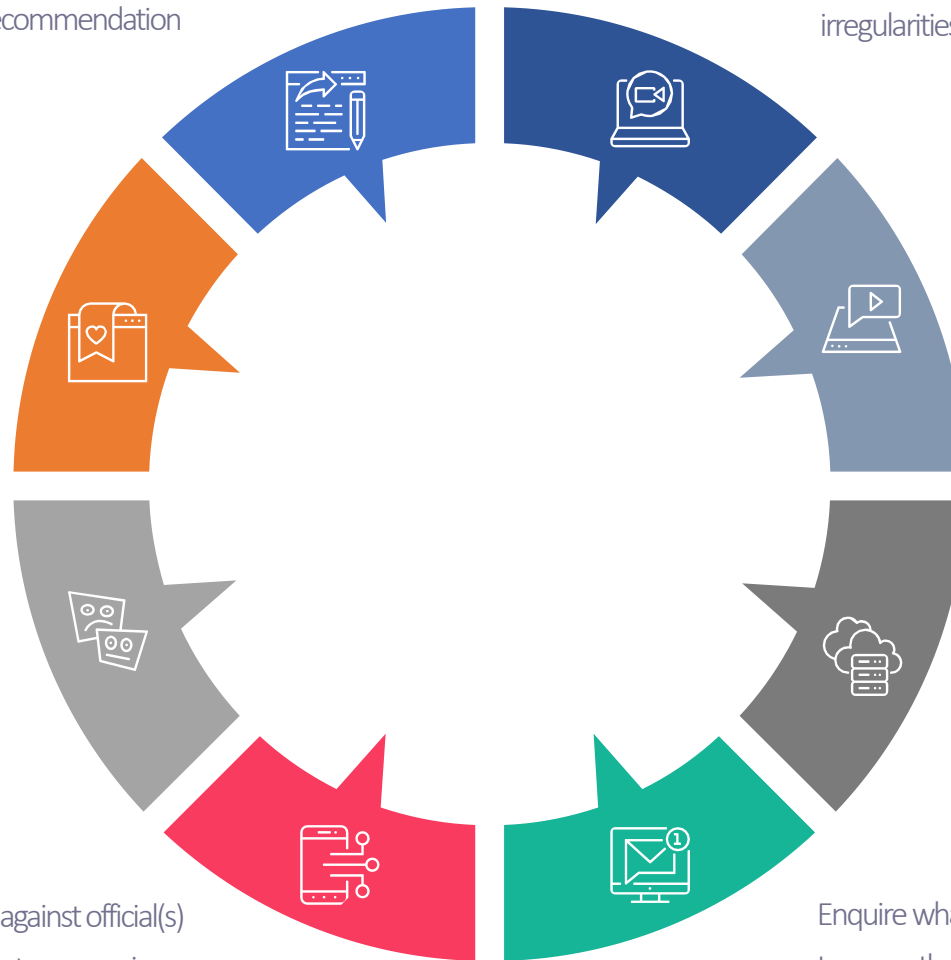
Follow up annually on previous commitments made by accounting officers

Hold executive authorities accountable for failures in control environment.

Determine if corrective steps are taken to address shortcomings in internal control environment

Follow up on actions taken against official(s) responsible for transgressions.

Enquire what training and support is given to officials to enable them to correctly execute their responsibilities










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# Focus



# AGSA audit outcomes


**NB:** Percentages in this presentation are calculated based on **completed audits of 13 auditees**, unless indicated otherwise.

Unqualified opinion with no findings (clean audit)	Financially unqualified opinion with findings	Qualified opinion	Adverse opinion	Disclaimed opinion
				
<p>Auditee:</p> <ul style="list-style-type: none"> <li>produced credible and reliable financial statements that are free of material misstatements</li> <li>reported in a useful and reliable manner on performance as measured against predetermined objectives in the annual performance plan (APP)</li> <li>complied with key legislation in conducting their day-to-day operations to achieve their mandate</li> </ul>	<p>Auditee produced financial statements without material misstatements or could correct the material misstatements, but struggled in one or more area to:</p> <ul style="list-style-type: none"> <li>align performance reports to the predetermined objectives they committed to in APPs</li> <li>set clear performance indicators and targets to measure their performance against their predetermined objectives</li> <li>report reliably on whether they achieved their performance targets</li> <li>determine the legislation that they should comply with and implement the required policies, procedures and controls to ensure compliance</li> </ul>	<p>Auditee:</p> <ul style="list-style-type: none"> <li>had the same challenges as those with unqualified opinions with findings but, in addition, they could not produce credible and reliable financial statements</li> <li>had material misstatements on specific areas in their financial statements, which could not be corrected before the financial statements were published.</li> </ul>	<p>Auditee:</p> <ul style="list-style-type: none"> <li>had the same challenges as those with qualified opinions but, in addition, they had so many material misstatements in their financial statements that we disagreed with almost all the amounts and disclosures in the financial statements</li> </ul>	<p>Auditee:</p> <ul style="list-style-type: none"> <li>had the same challenges as those with qualified opinions but, in addition, they could not provide us with evidence for most of the amounts and disclosures reported in the financial statements, and we were unable to conclude or express an opinion on the credibility of their financial statements</li> </ul>

The AG's annual audits examine:

1. Fair presentation and absence of significant misstatements in financial statements
2. Reliable and credible performance information for predetermined objectives
3. Compliance with laws and regulations governing financial matters

Movement over the previous year is depicted as follows:

-  Improved
-  Unchanged
-  Regressed



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# Portfolio outcome





# Public Enterprises portfolio auditees



public enterprises

Department:  
Public Enterprises  
REPUBLIC OF SOUTH AFRICA



## Portfolio overall message

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The overall outcomes in the portfolio has remained stagnant when compared to the prior year, with two **(DPE and SAFCOL)** auditees receiving unqualified audit opinions with findings on compliance with legislation. **Eskom** and **Transnet** audit opinion remains qualified.

**SAA** was in business rescue until 30 April 2021 and **SA Express** is currently in provisional liquidation both audits remains outstanding.

**Denel** did not submit financial statements as it is currently experiencing financial difficulties, loss of key resources and is addressing significant financial statement issues raised in 2019-20 audit.

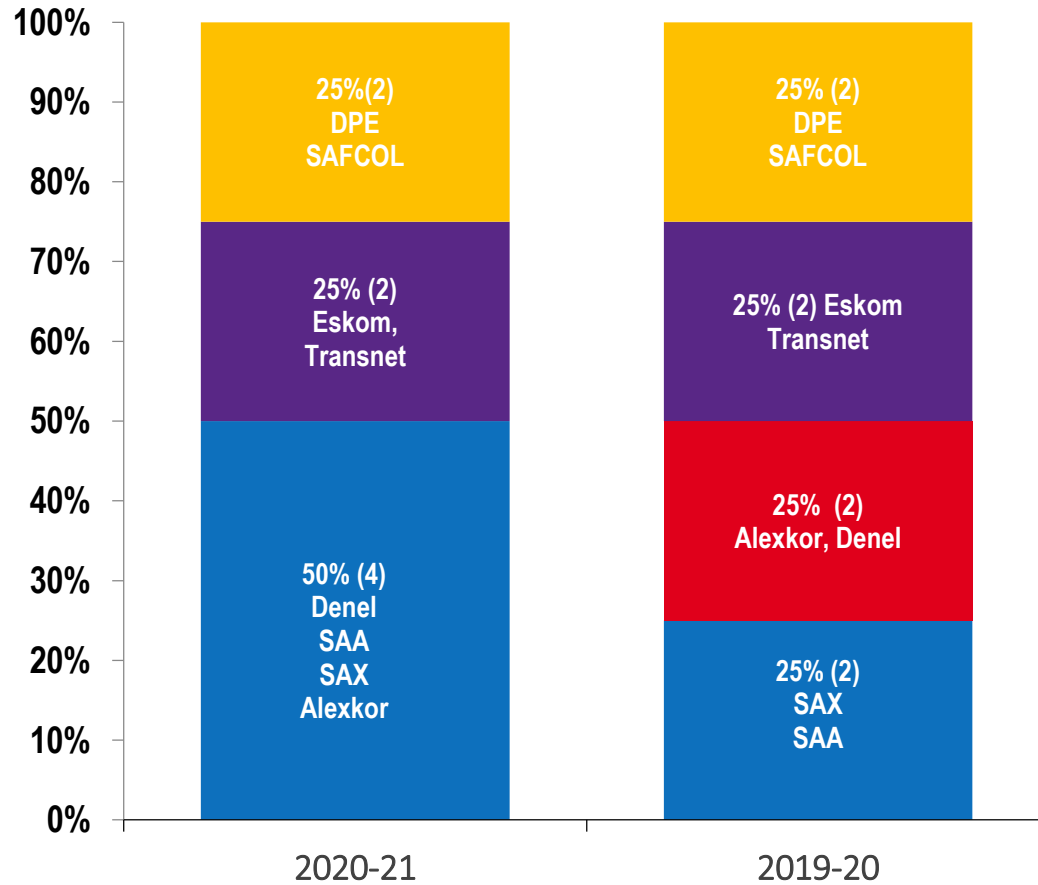
**Alexkor** audit is still in progress and is set to finish during November.

The prevalent instances of non-compliance are in the areas of expenditure management, supply chain management, revenue management, consequence management and material misstatements identified in the financial statements submitted for auditing.

In most instances, findings raised are reoccurring, indicating weaknesses in the implementation of audit action plans and an effective culture of accountability.

Leadership should put measures in place to ensure that there are adequate reviews on the annual financial statements (AFS), annual performance reports (APR) and monitoring of compliance with laws and regulations.

# Audit outcomes of the portfolio over 2 years



**Movement**

▶ 4

**Outstanding audits**

4 (Alexkor, Denel, SAA, SA Express)

Audit outcomes are depicted as follows:

- Unqualified with no findings
- Unqualified with findings
- Qualified with findings
- Adverse with findings
- Disclaimed with findings
- Outstanding audits



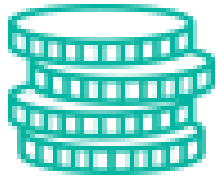
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# Quality of financial and performance reporting



# First focus area: credible financial reporting

## Financial statements --100% = 4 audits



Submission of financial statements by legislated date

Financial statements submitted without errors

Quality of final submission after audit

Movement



2020-21

2019-20

100% (4/4)

83% (5/6)

0% (0)

0% (0)

50% (2)

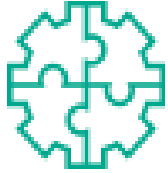
33% (2)

### Analysis

- At all four audits, material misstatements were identified in the AFS submitted for auditing.
- **DPE** and **SAFCOL** managed to correct the errors resulting in unqualified opinions, while **Transnet** and **Eskom** had uncorrected material misstatements on the completeness and accuracy of the irregular expenditure disclosure.
- Material misstatements in annual financial statements (AFS) weaknesses in the financial reporting process, inadequate reviews and reconciliations to underlying records.

# Second focus area: credible performance reporting

## Performance report



Performance report submitted without errors (SAFCOL and ESKOM)

### Movement



2020-21

2019-20

50% (2)

33% (2/6)

Performance report adjusted for material misstatements to improve reliability (DPE,TRANSNET)



50% (2)

33% (2)

Reliable reporting of achievements (DPE,TRANSNET)



100% (4)

67% (4)

Usefulness of performance indicators and targets



100% (4)

67% (4)

We commend **SAFCOL** and **ESKOM** for submitting the annual performance report without material errors which was consistent with the previous year.

## Root cause analysis

- **DPE** and **TRANSNET** had findings on the reliability of reported performance information, which were subsequently corrected. The supporting evidence did not always agree with the reported performance on the annual performance report. This was due to inadequate monitoring and reporting of reliable performance information which was consistent with the previous year.



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# Compliance with legislation

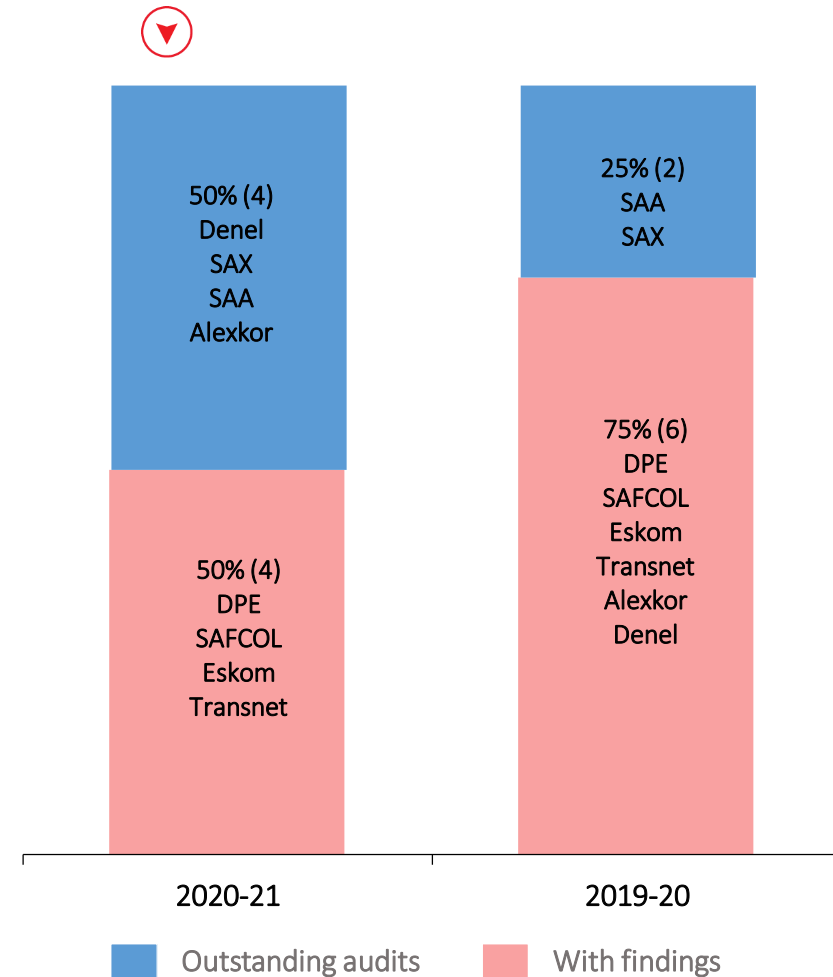


## Third focus area: compliance with legislation

The areas of material non-compliance reported are:

- Material misstatements identified in financial statements submitted for auditing: **(Transnet, Eskom, DPE and SAFCOL)**
- Ineffective steps to prevent irregular expenditure **(Transnet, Eskom and SAFCOL)**;
- Ineffective steps to prevent fruitless and wasteful expenditure **(Eskom)**;
- Uncompetitive and unfair procurement processes **(Eskom and Transnet)**
- Inadequate consequence management **(Eskom and Transnet)**
- Effective and appropriate steps were not taken to collect all revenue due. **(Eskom)**

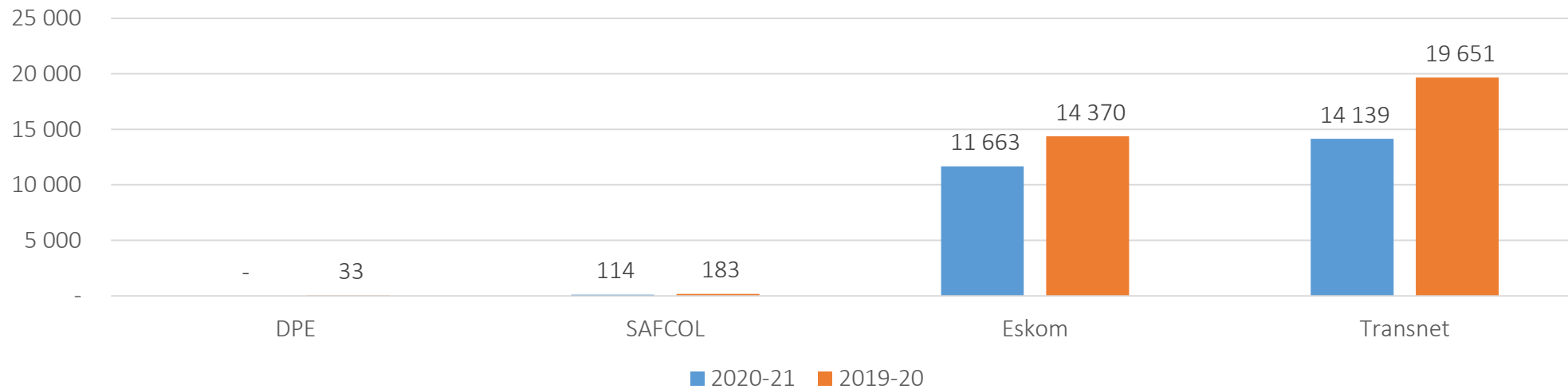
Findings on compliance with key legislation





# Irregular, unauthorised, fruitless and wasteful expenditure

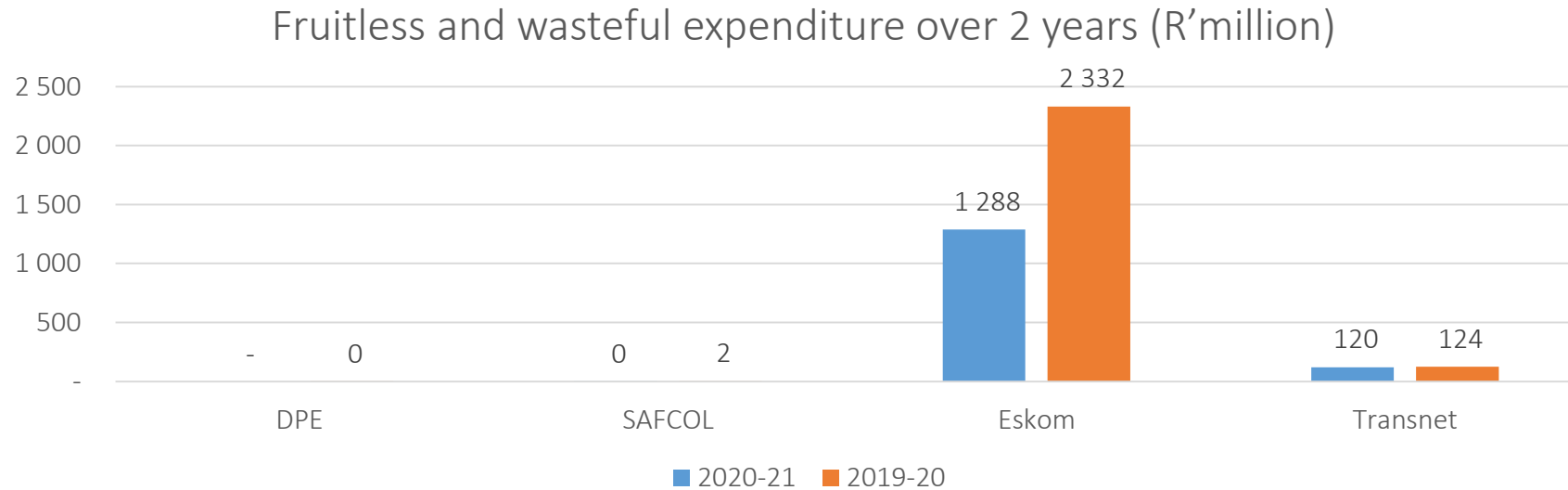
Irregular expenditure over 2 years (R'million)



## Irregular expenditure

- Total irregular expenditure identified – R25.9 billion. This is a reduction of R8 bn (24%) from the R33 bn incurred in prior year.
- Major contributors to the irregular expenditure are Transnet with R14 bn and **ESKOM** with R11.6 bn. Procurement and contract management irregularities remain the cause of irregular spending at these entities.

# Fruitless and wasteful expenditure



- Majority of the fruitless and wasteful expenditure was incurred by Eskom, which mainly relates to poor procurement and contract management overpayments of R1 280 million relating to a fuel oil contract.
- 9% was incurred by Transnet and it relates to poor procurement and contract management, inappropriate delegation of authority, redundant assets and stock fines and penalties.
- There is a notable reduction in irregular expenditure from R2.4bn in 2019-20 to R1.3 bn in 2020-21

# Compliance with legislation

## Consequence management

Consequence management remains a challenge at **Eskom** and **TRANSNET**, while **DPE** and **SAFCOL** did not have material non-compliance findings on consequence management.

At **Transnet** and **Eskom**, we noted that the respective boards and management developed action plans as part of strengthening accountability and consequence management. As the implementation of these action plans is still in progress, we identified instances of non-compliance with applicable legislation and related internal controls that resulted in the lack of effective consequence management practices. The following non-compliance was noted:

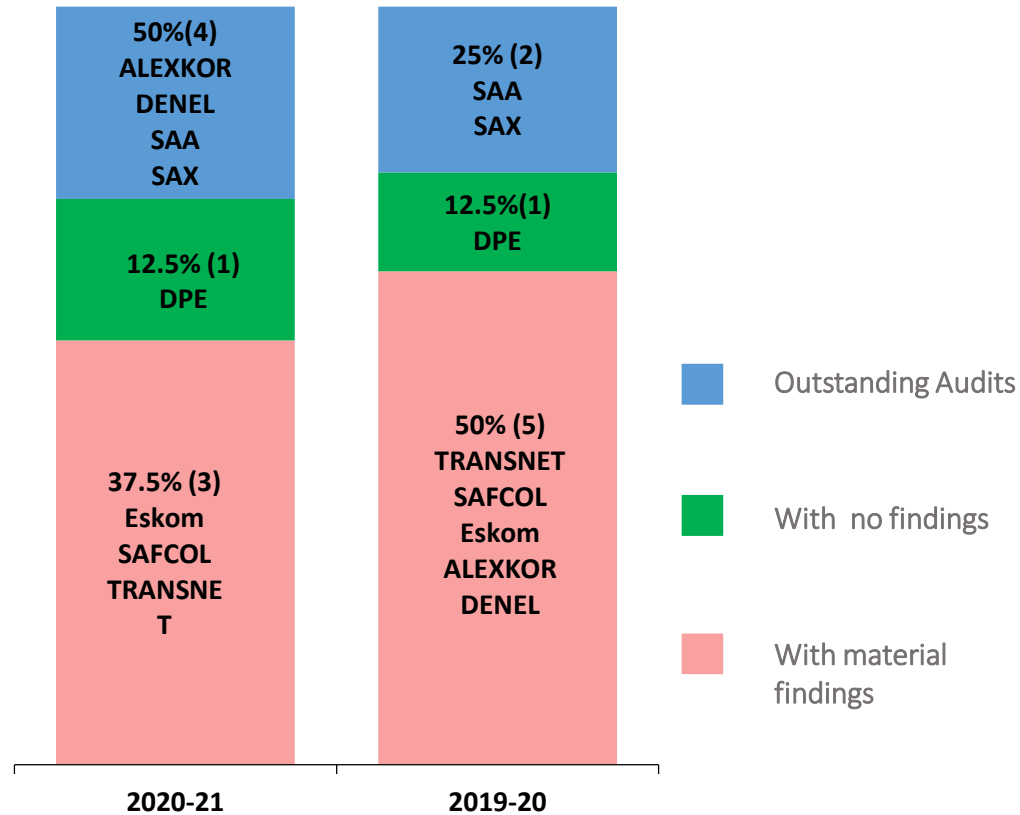
- Lack of evidence supporting disciplinary steps taken against some officials responsible for Irregular and Fruitless and Wasteful Expenditure. (**Transnet, Eskom**)
- Disciplinary steps not taken against some of the officials who incurred IFWE (**Transnet**)
- Lack of evidence on investigations that were conducted into some allegations of financial misconduct by officials (**Transnet, Eskom**)
- No disciplinary hearings held for some confirmed cases of financial misconduct (**Transnet**)
- Lack of evidence that allegations of fraud exceeding R100 000 were reported to SAPS. (**Eskom**)

## Recommendations

- Improvement of record management system to enable availability of information relating to consequence management is a matter that requires attention at both Eskom and Transnet.
- Strong internal control system in procurement and contract management is needed to bring board's effort to drive a culture of accountability to fruition.
- Officials must be held accountable for missing documents. Missing documents effectively mean that management and board do not have a full view on the extent of the irregularities that took place within the entity.
- Management should consider continuing to seek guidance of National Treasury in dealing with historical irregular expenditure.

# Supply chain management (SCM)

Overall regression in SCM compliance  
All SCM findings should be investigated



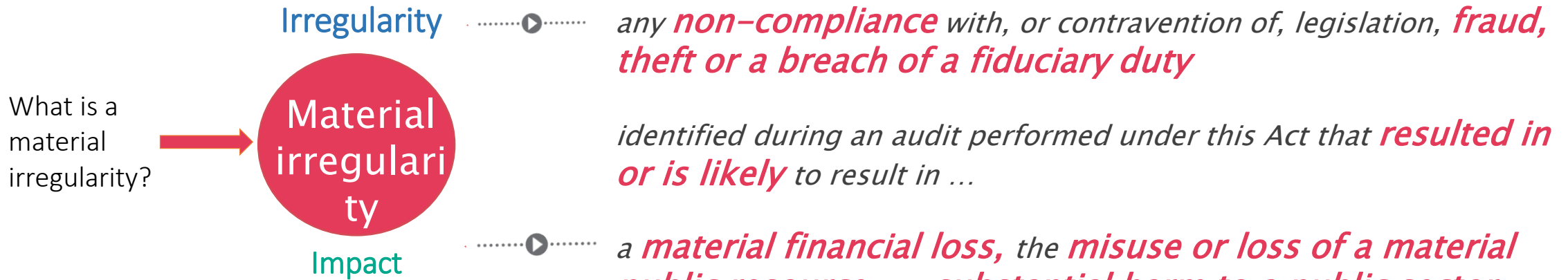
## Most common findings on SCM

- Procurement process that was not fair, equitable, transparent and competitive. (Both)
- Preference point system not applied (Eskom)
- Procurement from suppliers without SARS Clearance certificate (Transnet)
- Criteria applied in evaluation differed from specification (Transnet)
- Highest scoring supplier was not selected without justification (Transnet)
- Awards made to contractors not registered with CIDB (Both)
- Limitation on compliance testing (Both)

## Recommendations

- SCM trainings and refresher courses should be attended by to ensure understanding and application of legislation
- Procurement officials must be held accountable for lack of records supporting procurement activities.

# At the center of the PAA amendments – material irregularity



## Type of material irregularity

### Selection criteria

Any non-compliance in line with the definition stated above.

The MI process is implemented at selected auditees audited by the AGSA that represent a **significant portion of the expenditure budget and the irregular expenditure** of national, provincial and local government, including state-owned entities. The selection is also focused on auditees that are key contributors to **government priorities**.

To allow for establishing capacity and processes, we will follow a phased-in approach for identifying MIs in 2020-21 based on:

1. the type of material irregularity to be identified and reported
2. the auditees where it will be implemented

# Implementation of expanded mandate in 2020-21



## Status of MIs in progress

Entity	Material irregularities identified	Status
Transnet	Contracts for the lease of heavy duty plant and equipment awarded to bidder(s) that did not score the highest points	Accounting authority instituted a forensic investigation.
Transnet	Contract amounts exceed the tendered prices for the lease of heavy duty plant and equipment	Accounting authority instituted a forensic investigation.

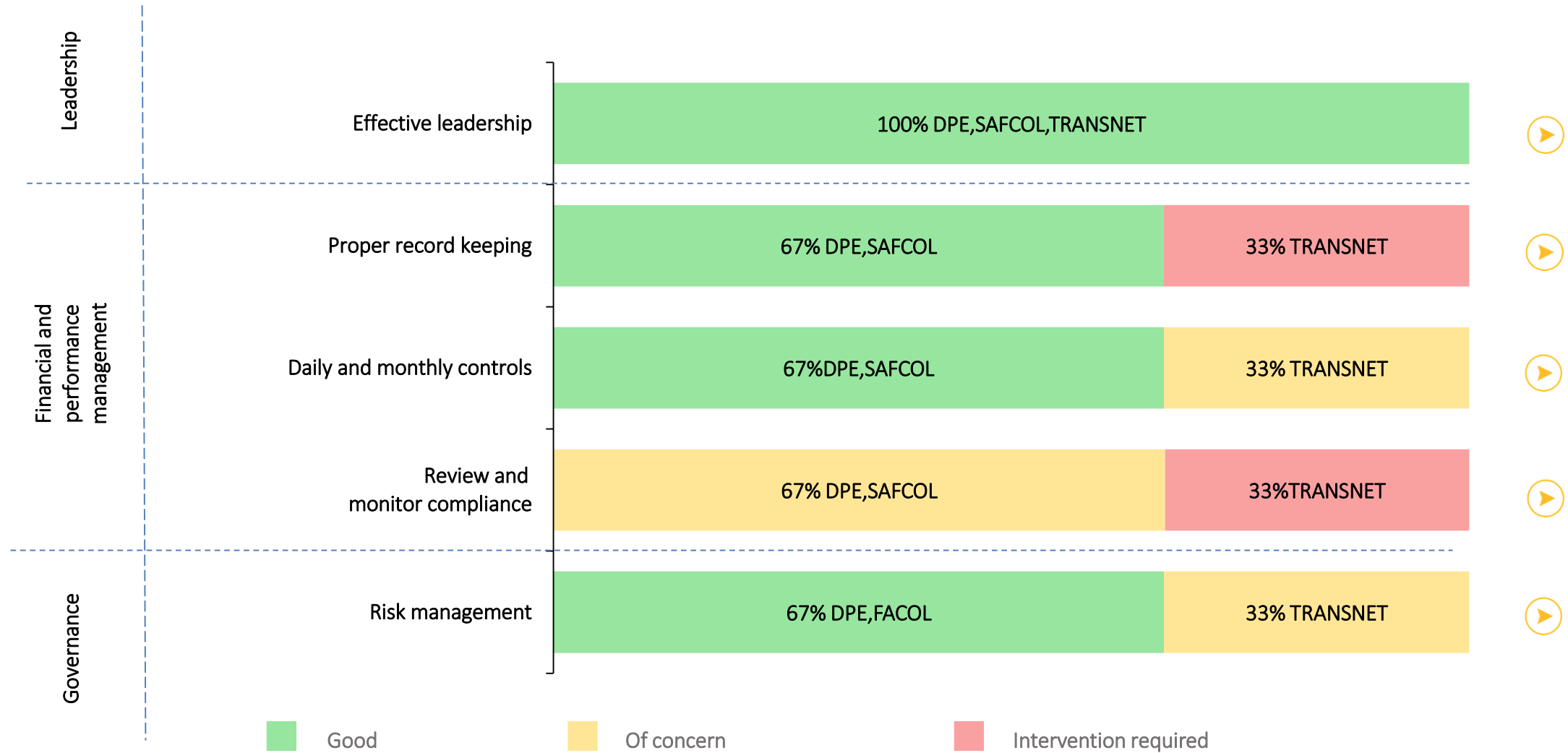


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# Governance and internal controls



# Status of internal control



- Eskom is not included in assessment of internal controls
- The movement excludes Transnet as it was not assessed in the previous year.



# Status of information technology (IT) environment

- **IT governance** – there to ensure IT is effectively and efficiently used to enable entity to achieve its mandate by specifying decision rights and accountability framework to encourage desirable behavior in using IT
- **IT system controls** – there to ensure entity’s IT operates as intended to achieve its mandate
- Effective IT governance and system controls will help ensure entities are not vulnerable to cyberattacks and business continuity concerns



Good      Of concern      Intervention required



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# Portfolio snapshot



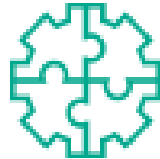
# Portfolio snapshot 2020-21



Clean audits: 0  
(2019 - 20: 0)



Financially unqualified financial statements: 2  
(2019-20: 2)



No findings on performance reports: 2  
(2019-20: 2)



No findings on compliance with legislation: 0  
(2019-20: 0)



Irregular expenditure: R25.9b  
(2019-20: R23b)

## Summary of key root causes

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Internal controls implemented were inadequate to prevent non-compliance with procurement legislation.



Management did not implement adequate review and monitoring controls over preparation of financial statements and annual performance reports.



Management was not effective in ensuring adherence to the action plans developed audit action plans as there were repeat findings in AFS Compliance as well as IT.



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# Recommendations



# Recommendations for entities within the portfolio



Accounting officers/ authorities should strengthen preventative controls to identify non-compliance



Accounting officers/ authorities must thoroughly review developed action plans to ensure they address root cause



Accounting officers/authorities must continue to do their work through audit committees to ensure management implements and enhances review processes for AFS



There must be timely consequences for officials who do not implement actions plans or neglect their duties

# THANK YOU

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