

TRANSNET – SCOPA PRESENTATION

November 2017 PFMA IMPROVEMENT REPORT





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Context

- Transnet is committed to complying with the provisions of the PFMA and handling alleged governance breaches in a firm and expeditious manner.
- Accordingly the company implemented a number of preventative initiatives over the past few years and these are yielding positive results.
- Media allegations was noted with concern and are dealt with on page 3.
- Net PFMA transgressions, after condonations and potential recoveries, amounted to R305,7 million for the year ended 31 March 2017
- The previous year's foreign vendor potential PFMA violation of R230 million was also condoned by National Treasury.

Improvement initiatives

- PFMA control improvements and consequent management across Transnet are been monitored on a project management basis.
- Critical Financial Reporting Control (CFRC) Step-Up Project is in place to cover all financial related processes end to end.
- Operational Controls are also being Stepped-Up which will see the top priority processes undergoing improvements.
- Initiatives are underway to bring data analytics in-house for regular monitoring and reporting to support External Audit processes.
- AOPO and Compliance activities have been brought forward to be conducted during quarterly Audit Reviews to proactively manage emerging risks.
- The Group PFMA Forum was re-instated during Quarter 1 of the 2017/18 FY.

TRANSNET MEDIA ALLEGATIONS



- Transnet has noted with concern recent reports casting aspersions on the integrity of the company's governance processes, especially relating to procurement. The allegations of payments between our suppliers and third parties under the pretext of winning business with Transnet are of grave concern to us. Recent media reports make reference to Transnet in a number of allegations related to procurement irregularities.
- The Group Chief Executive has commissioned a preliminary internal forensic investigation on the media allegations relating to kickbacks on Transnet contracts. The results of the investigation will be communicated once the investigation is completed.
- We have requested the affected companies to indicate to us if any past or current employees of Transnet requested that they pay any kickbacks to themselves or any third parties. Some companies have denied any involvement in such activities while others are still investigating and will make their findings available to us.
- The special oversight committee comprises three non-executive directors who are members of the Transnet's Board Audit Committee and have engaged the services of Werksmans Attorneys and forensic specialists to conduct an independent investigation on locomotives.

PFMA CONTEXT AND TREND ANALYSIS



Overall statistics (FY 2016/17)

PFMA contextualised:

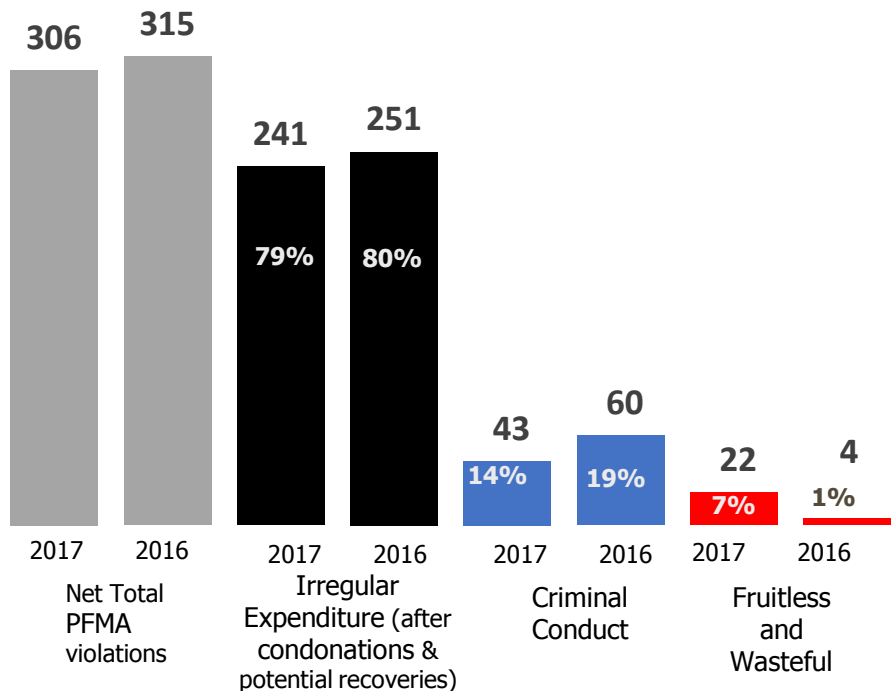
% of Revenue

0.47%

% of Expenditure

0,8%

* Amounts are in Rm



Where were the PFMA transgressions picked up?

78%

PFMA transgressions were identified by management where existing controls are in place

22%

Highlighted either by Internal or External Audit

Are we able to quantify which parts of irregular expenditure we obtained value?

Irregular expenditure typically involves expenditure incurred by Transnet for goods or services that were required, delivered and value received, however an internal policy or processes was not followed correctly.

79%

PFMA transgressions relate to Irregular Expenditure

REPORTABLE PFMA ITEMS - 16/17



The Shareholder Representative determined that the materiality limit for reporting in terms of section 55(2)(b)(i), (ii) and (iii) of the PFMA, relating to losses and expenditure through criminal conduct, fruitless and wasteful and irregular expenditure, is R25 million per transaction. There are 7 reportable items exceeding R25m which have been reported as Irregular Expenditure as at Quarter 4 of the 2016/17 financial year.

Category of reportable items	2016/17				2015/16	
	Rm Spend Prior Years	Rm Spend in 2016/17	Rm Total	Number of finalised disciplinary/ criminal cases	Rm	Number of finalised disciplinary/ criminal cases
Fruitless and wasteful expenditure	15	7	22	40/13	4	35/3
Losses through criminal conduct	0	43	43	0/885	60	12/1029
Irregular expenditure	550	143	693	10/10	21+230	10/0
Gross PFMA Transgressions	565	193	758	50/909	315	
Less: Irregular expenditure condoned by National Treasury			+230-230			
Less: Irregular expenditure condoned by Transnet	-241	-52	-293	6/0		
Less: Amounts recoverable (not condoned)	-49	-110	-159	0/1		
Net PFMA Transgressions	R275m	R31m	R306m		R315m	

*There were 40 * criminal conduct items, 41* Fruitless and Wasteful items and 62* Irregular items reported by operating divisions across Transnet.*

- The table above reflects the number of finalised disciplinary cases instituted against employees for non-compliance to PFMA. There are other cases that are still pending finalisation, and is reported through Transnet's reporting structures on a regular basis.*
- 909 criminal cases have also been lodged with SAPS to date, and mostly relate to losses through criminal conduct.*
- The company enhanced its reporting systems for irregular expenditure, which resulted in additional violations, relating mainly to prior years, being identified and reported in the current year. Consequently, of the total, 75% relates to irregular expenditure relating to contractual spent in prior years*

HUMAN CAPITAL - CONTROL IMPROVEMENTS ON PFMA DISCIPLINARY PROCESSES



- Communique from Human Resources published on 30 June 2017 reinforcing PFMA and associated Treasury Regulations, read together with the Transnet Disciplinary Code and Procedure when dealing with disciplinary matters involving PFMA violations.
- PFMA violations are investigated swiftly and there is an arrangement with Group Forensics to expedite investigations relating to misconduct involving PFMA violations.
- Disciplinary action is initiated against any employee implicated in an investigation and every effort is made to complete the hearings as soon as possible.
- Where an employee resigns in the face of disciplinary action, Transnet continues with any investigation and disciplinary action during the notice period.
- Wherever possible any financial losses suffered by Transnet are recovered from the Transnet Pension Fund.
- Monthly statistics are provided to Group Employee Relations and tabled at Operating Division committees to ensure ongoing oversight and control of investigations and disciplinary matters involving PFMA violations.
- Disciplinary sanctions are determined based on the nature of misconduct and the loss suffered by Transnet. Transnet rules are well communicated and employee's are aware of the consequences of transgressing these rules. Every effort is made to ensure consistency of sanction by presenting argument to the presiding officers hearing the disciplinary cases.

TRANSNET AND ITS REGULATORY UNIVERSE REGARDING PROCUREMENT



- Transnet is an organ of state as defined under section 239 of the Constitution of the Republic of South Africa ('the Constitution') as well as section 1 of the Public Finance Management Act, 1 of 1999 ('PFMA'). In terms of section 217 (1) of the Constitution and section 51 (1) (a) (iii) of the PFMA, Transnet has to have a procurement and provisioning system that is fair, equitable, transparent, cost-effective and competitive. In terms of the Promotion of Just Administrative Action Act, 3 of 2000, which was issued in terms of section 33 of the Constitution, Transnet has to ensure that its administrative actions, i.e. a decision to award a tender, is lawful, reasonable and procedurally fair.
- Transnet's procurement processes are regulated through administrative law, because Transnet is an organ of state as mentioned above. Therefore, over and above the pieces of legislation that mentioned above, Transnet also has to comply with other acts of parliament and regulations during its procurement process. Some of these acts and regulations are as follows:
 - The Construction Industry Development Board Act 38 of 2000 ('CIDB Act') and the regulations ('CIDB regulations') thereto;
 - The Promotion of Access to Information Act, 2 of 2000 ('PAIA')
 - The Preferential Procurement Policy Framework Act, 5 of 2000 ('PPPFA') and the regulations thereto ('PPPFA regulations')
 - National Treasury ('NT'), also issues Instruction Notes which regulate Transnet's procurement processes.
- Transnet's internal processes are as follows:

Transnet Delegation of Authority:

- The approved Transnet DOA sets out the various activities related to procurement and provides the various levels of approvals, Ministerial, Board, Board Sub-committee, GCE and further down

SCM Policy:

- The SCM Policy (SCMP) sets out the principles that need to be considered during every procurement event. The SCMP communicates the spirit of various pieces of legislation, regulations, government policies and Instruction Notes.

Procurement Procedures Manual:

- The Procurement Procedures Manual (PPM) details various procurement rules, procedures and processes for the entire end to end procurement business process

Infrastructure Procurement and Delivery Management Framework:

- Regulates infrastructure related procurement and related delivery management.

SCM Contract Management Procedures Manual:

- Regulates contract management with SCM. The Procedure manual is based on Transnet's Contract Management Policy

Procurement Control Frameworks:

- The Procurement Control Frameworks list Business Critical Activities (BCA's) and Business Critical Controls (BCC's). BCAs are activities which have to be undertaken for a process to be compliant. The BCCs are controls that ensure that activities are conducted in a manner consistent with applicable, laws, policies and procedures. The Control Frameworks, are used during audits by internal audit and External audit. Transnet also develops a Fraud Risk management framework to ensure controls are developed to combat fraud in procurement.

High Value Tender process:

- The High Value Tender Process (HVT), performed by the Internal Audit process, provides real-time compliance assurance that a procurement process has complied with all the governance requirements

Acquisitions and Disposal Committee (ADC) Terms of Reference:

- Terms of reference ('ToR') set out the roles and responsibilities of the committee as it relates to procurement and include the Board approved DOA's.

Acquisition Council Terms of Reference:

- The Acquisition Council ('AC') terms of reference ('ToR') set out the roles and responsibilities of the members of the ACs when they perform their adjudication role.

Procurement Ombudsman:

- Transnet has a Procurement Ombudsman processes which considers complaints from aggrieved or interested suppliers. Transnet uses the services of external legal firms to investigate complaints, in order to maintain the independence of the ombudsman function. The Procurement Ombudsman has the power to recommend that a tender award be set aside. The ToR of the Procurement Ombudsman were approved by the ADC.

INTERNAL CONTROLS INITIATIVES: TRANSNET KEY BUSINESS PROCESSES 'STEP UP PROGRAMME'



Maintaining a world class risk and internal control environment

The Company is committed to complying with the provisions of the PFMA and handling alleged governance breaches in a firm and expeditious manner. Accordingly the company has implemented a number of preventative initiatives. The specific root causes on the irregular expenditure relating to the current and prior year have been assessed and mitigating controls, as tabulated below have been developed.

INITIATIVES

- Financial processes 'Step Up'.
- Key business processes 'Step Up'.
- PFMA Control 'Step Up'.
- Operating Divisions Assurance Sub-committee.
- Continuous monitoring and improvement.
- SMART analytics.

PURPOSE

- Programme to aimed to improve the key financial processes that impact on critical financial reporting controls.
- Programme to improve the key business (operational) processes impacting on Transnet achieving its objectives.
- Improvement of PFMA control environment and alignment of the PFMA legislation to all applicable Transnet processes, ensuring controls are implemented and are adequate.
- Reviews and assesses the integrity and effectiveness of the accounting, financial, compliance and other control systems, as well as evaluate internal control frameworks within Transnet. Sub-committee also reviews internal and external reports.
- Perform Audit Of Performance Objectives and compliance audit quarterly as opposed to annually, as well as external audit's computer audit assisted testing (CAATS) monthly, to ensure control weaknesses and exceptions are addressed timeously, and that there is continuous monitoring and improvement.
- Improvement on automated controls and exceptions reporting dashboards as well as implementation and monitoring of documented processes via exception reporting to enable management. This will reduce manual process, facilitate quicker identification of areas that require management's attention for better decision making and to resolve exceptions.

THANK YOU

