**5. Report of the Standing Committee on the Auditor-General on the Auditor-General of South Africa’s 2018-2021 Draft Strategic Plan and Budget, dated 24 November 2017**

The Standing Committee on the Auditor-General (SCoAG), having considered the 2018-2021 draft Strategic Plan and Budget of the Auditor-General of South Africa on 17 November 2017, reports as follows:

**1. Introduction**

1.1 The Auditor-General of South Africa (AGSA) is established in terms of Chapter 9 of the Constitution, and is a state institute supporting constitutional democracy. The Constitution guarantees the AGSA’s independence, and requires that the office operates in an impartial manner, and performs its functions without fear, favour or prejudice.

1.2 Section 10(3) of the Public Audit Act, No 25 of 2004 (the Act) requires that the National Assembly provides for a mechanism to maintain oversight of the Auditor-General in terms of section 55(2)(b)(ii) of the Constitution. Accordingly, the Rules of the National Assembly provide for the establishment of the Standing Committee on the Auditor General (the Committee). The Committee is charged with assisting and protecting the AGSA in order for the latter to maintain its independence, impartiality, dignity and effectiveness.

1.3 According to section 38(2) of the Act, the Auditor-General must submit its budget and business plan to the oversight mechanism at least six months before the end of the financial year. In terms of section 38(3) the oversight mechanism must within two months of the receipt of the budget and business plan, submit its recommendations to the Speaker and National Treasury.

1.4 This report has been divided into the following four parts:

- Part A, dealing with the Draft Strategic Plan;

- Part B, dealing with the 2018/19 budget;

- Part C, dealing with the audit directives in terms of the Act; and

- Part D, containing SCoAG’s observations and recommendations.

**Part A**

**2. Draft Strategic Plan**

**2.1 Environmental trends**

2.1.1 The AGSA took into consideration the following trends when it reviewed its strategic plan and budget:

- the intensified public awareness and debate around corruption, poor governance and lack of consequences for financial mismanagement;

- increased interest in improving service delivery, and the realisation of national priorities and sustainable development goals;

- the increased concern about the performance of state-owned enterprises;

- resistance to the AGSA from auditees;

- the slow pace of transformation in the professions, and slow skills development; and

- fast pace of technological developments, and the associated risks.

**2.2 Strategic Goals and Objectives**

The AGSA’s commitments for the 2018-2021 period are informed by its four long-term strategic goals. These are outlined below.

*Value-Adding Auditing*

2.2.1 Value-added auditing is aimed at providing audit-derived valuable insights to stakeholders regarding the status of their internal control and performance environment, accompanied by actionable recommendations which, if implemented, should result in visible improvement in public sector administration.

2.2.2 The strategic objectives under this goal are to: demonstrate value-add to stakeholders; and to ensure high quality audits. To this end, the AGSA will,

- remain focussed on auditing areas that matter, and influencing public sector players to improve;

- continue to detect and expose practices that result in the wasting of public funds;

- aim to establish a direct line between detection of breaches to the implementation of consequence management;

- continue to implement various measures to maintain and increase adherence to audit quality standards; and

- support reporting on the achievement of sustainable development goals (SDGs).

2.2.3 The AGSA’s main strategic initiatives in this regard are to:

 - review its audit portfolio annually to ensure its relevance;

- develop models in their new audit methodology for low risk and small-to-medium audits;

- continue intensifying the use of computer assisted auditing techniques (CAATs)’

- continue developing deep knowledge of auditees;

- prepare the organisation for alignment with the amendments of the Act should they be approved and assented to;

- continue strict oversight of the governance of section 4(3) audits; and

- continuously improve the quality of its audits.

*Visibility for Impact*

2.2.4 This objective structures the AGSA’s engagement programmes to encourage and enable the required improvements in the public sector, i.e. to encourage stakeholders to implement its recommendations.

2.2.5 The strategic objectives under this goal are to: achieve impact through visibility programmes; and to engage actively with citizens. To this end, the AGSA will,

- explore better and innovative ways of communicating what matters to stakeholders;

- implement a well-structured status of records and commitments review so as to provide depth to discussions on key controls;

- drive continual improvements in its engagement tools so as to build capacity for meaningful stakeholder interactions; and

- contribute to the advancement of the professionalization of auditors worldwide, specifically on the African continent.

2.2.6 The AGSA’s main strategic initiatives in this regard are to:

- systematically and consistently implement the status of records and commitments reviews programme;

- implement its external through leadership programme

- increase its reach and impact of engagements on the organisation’s mandate and role;

- enhance stakeholders’ awareness and understanding of outcomes; and

- provide effective support to the Organisation of English-speaking African Supreme Audit Institutions (AFROSAI-E) and collaborate with African supreme audit institutions and other members of the International Organisation of Supreme Audit Institutions (INTOSAI).

*Viability*

2.2.7 This objective focusses on the AGSA’s internal workings, and is aimed at ensuring that the organisation had the necessary resources, i.e. an enabling legal framework; independent financial resources; and the required skills, competencies and culture to execute its mandate economically, efficiently and effectively.

2.2.8 The strategic objectives under this goal are to: maintain financial viability and legal independence; attract, develop and retain great talent; create an enabling culture and leadership; and increase operational efficiencies. To this end, the AGSA will,

- engage all relevant stakeholders with the aim of securing full payment of audit fees so as to ensure the organisation’s financial viability;

- pursue even better utilisation and development of its human capital;

- elevate the integrated thinking in the organisation through increased understanding of its resources;

- intensify work on the institutionalising of the desired culture and leadership; and

- manage its physical infrastructure, improve operational processes and maintain information technology to ensure it is best positioned to execute its mandate.

2.2.9 The AGSA’s main strategic initiatives towards maintaining viability and legal independence are to:

- pursue effective debt collection through ring-fencing and litigation, and quantifying and monitoring efficiencies realised from the implementation of the revised audit methodology;

- intensify cost optimisation tactics such as the moratorium on recruitment, and strategic sourcing; and

- regularly review available legal instruments to support the execution of its mandate and to promote consequence management in the public sector.

2.2.10 The AGSA’s main strategic initiatives towards creating an enabling culture and leadership to drive strategic execution are to:

 - develop and implement a culture strategic/plan;

 - continuously enhance its IT solutions and organisational processes; and

 - strengthen information security and information management.

 *Vision and Values Driven*

2.2.11 The AGSA aims to, through its work and behaviour, continually demonstrate that clean administration and transformation are achievable. The AGSA maintained its clean audit in 2016/17. To this end the AGSA will,

 - ensure the highest levels of accountability, ethics and effective governance;

- support South Africa’s transformation objectives by continuously reviewing its procurement policies and practices, and managing people targets at all levels with special attention to employing persons with disabilities;

- **contribute** to the transformation of accounting and auditing profession in South Africa through the distribution of contract audit work in support of black owned firms; its enterprise and supplier development programme; and supporting schools, universities and the Thuthuka graduate programme.

2.2.12 The AGSA’s main strategic initiatives towards adherence to its vision and values are to:

- implement its transformation strategy by growing its people, supporting its suppliers and communities;

- demonstrate quality and transparency of reporting in its accountability instruments;

- cultivate and environment that enables the desired ethical behaviour; and

- continuously enhance the ownership and accountability of business process owners.

**Part B**

**3. 2018/19 Budget**

**3.1 Background/Context**

3.1.1 The AGSA reviewed its funding model in 2008. The current model was accept as the most suitable model for the AGSA’s financial sustainability, and to ensure its independence. Thus, the AGSA’s funding model reviewed process resulted to AGSA having a funding model which was self-sustaining. This funding model differs from that of other Chapter nine institutions as it is not dependent on the fiscus. This funding model has made it possible for the AGSA to, notwithstanding the challenges with regard to collecting ooutstanding fees, generate a surplus over the last five previous financial years.

3.1.2 The difficulties the AGSA has experienced with regard to the collection of outstanding fees has threatened its financial sustainability because it poses cash flow problems to AGSA. This has led to the organisation’s margin of safety, measuring its ability to fund its day-to-day operational costs in the event of lack of cash inflow, declining from 2,5 months in recent years, to 1,8 months at the time of reporting.

3.1.3 To resolve the challenges around collecting outstanding audit fees, the AGSA has implemented debt collection methods which include ring-fencing agreements and litigation strategies. Since the implementation of these collection methods, the AGSA has recorded successes as far as collecting outstanding audit fees. They will therefore continue with these strategies.

**3.2 Summary budget proposal**

The table below summarises the AGSA’s proposed budget for 2018/19 financial year.

|  |  |  |
| --- | --- | --- |
| **(R million)** | **Actual 2016/17** | **Budget** |
| **2017/18** | **2018/19** |
| **Audit income**  | **2 977**  | **3 276**  | **3 382** |
| Own hours  | 2 252  | 2 525  | 2 644 |
| Contract Work  | 725  | 751  | 738 |
| **Direct costs**  | **2 058**  | **2 222**  | **2 255** |
| **Gross profit**  | **919**  | **1 054**  | **1 127** |
| **Other income**  | **72**  | **68**  | **70** |
| **Overhead expenses**  | **1 006**  | **1054**  | **1 121** |
| **Net Surplus**  | **-15**  | **68**  | **42** |

3.2.1 The AGSA’s budget revenue is expected to grow by 3 per cent, below CPIX driven mainly by the organisation’s commitment to affordable fees and the auditees budgetary constraints. The organisation’s revenue will be reduced by R67 million owing to the implementation of the new **IFRS15 standards (International Financial Reporting Standards)** which prohibit recognition revenue that cannot be collected.

3.2.2 Even though the revenue has increased below the expected inflation, the overhead costs are budgeted to increase with inflation. The AGSA reports that although its overheads were projected to grow by 9,6 per cent, but cost containment measures referred to above will result in growth of 6.3 per cent only. Subsequently, the AGSA has projected a net surplus of R68 million and R42 million for the 2017/18 and 2018/19 financial years, respectively.

**Part C**

**4 Audit Directives**

4.1 The AGSA tabled several changes to the audit directive issued in terms of the Public Audit Act. The main purpose of the proposed amendments is to enable the work of AGSA. For instance, the AGSA has previously reported on the difficulties as far as obtaining performance information from auditees. Therefore the AGSA has proposed to add the requirement to submit information for the audit of reported performance information with the annual performance report.

4.2 The AGSA has also proposed minor changes to AGSA’s mode of operations, such as the implementation of a new revised audit methodology.

**Part D**

**5. Observations**

5.1. The Committee notes that although the AGSA has reduced its personnel by 54 employees, it aims to improve productivity and efficiency. Of particular concern is the impact reduction in personnel will have on the AGSA’s capacity to conduct audits of SOEs. The AGSA should ensure that it has the necessary resources to conduct such audits should they be expected to do so in the future.

5.2 The AGSA confirmed that it will not be spending any significant money on capital expenditure projects. Most of its CAPEX expenditure will be on maintaining the significant expenditure for IT infrastructure and IT licences.

5.3 The **Committee noted** the AGSA’s progress in terms of employing persons with disabilities, which far exceeds that of most national departments.

5.4 Technological developments in auditing will impact on recruitment, and the AGSA should ensure that it stays abreast of such developments, so that it is able to adapt as required.

5.5 The Committee notes that the AGSA is proposing a per hour tariff increase of 7 per cent as of thee 2018/19 financial year. The proposed tariff increase is in line with the budget salary increase of 7 per cent. The AGSA’s tariffs are based on the average staff costs per band and interval, mark up factor and recoverable hours per band.

5.6 The Committee notes the AGSA’s budget to generate a net surplus of R42 million for the 2018/19 financial year. This presents a significant improvement on the net deficit recorded by the AGSA in the 2016/17 financial year.

**5.7 On 23 November 2017 the National Assmebly granted the Committee permission to proceed with amendments to the Act. The Committee notes that should the amendments be passed, the AGSA may have to review its strategic plan.**

**6. Recommendations**

6.1 The Committee supports the AGSA’s 2018-2021 strategic plan, and 2018/19 budget.

6.2 The Committee supports the amendments to the audit directives in terms of the Act.

6.3 The Committee supports the proposed tariffs per hour for the 2018/19 financial year.

***Report to be considered***