



AUDITOR - GENERAL
SOUTH AFRICA

Scoag induction session

13 September 2019

Audit

Report

For
Accountability

AGSA

MISSION

The Auditor-General of South Africa has a constitutional mandate and, as the Supreme Audit Institution (SAI) of South Africa, exists to strengthen our country's democracy by enabling oversight, accountability and governance in the public sector through auditing, thereby building public confidence.





AGSA mandate

Mandate of the AGSA

Chapter 9 of the Constitution

○ Section 188:

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

Public Audit Act, No. 25 of 2004

○ Section 20:

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

○ Section 5:

- Discretionary audits (including special audits, investigations and performance audits)



Work of the AGSA



What we do!

Provide assurance that the annual financial statements are free from material misstatements

Report on the usefulness and reliability of the information in the annual performance report

Report on material non-compliance with relevant key legislation

Identify key internal control deficiencies that should be addressed



What don't we do!

Guarantee completeness and accuracy of ALL the information

Provide assurance that service delivery has been achieved

Provide assurance that all applicable laws and regulations have been complied with

Identify fraud



AGSA governance arrangements

The AG's oversight mechanism (Scoag)

- The Constitution requires the AG to account to the National Assembly. The AG accounts to the National Assembly via Scoag.
- Scoag is a committee of the National Assembly established by the Constitution and the PAA to oversee the work of the AG and his/her establishment.
- The strategic role of Scoag is to assist and protect the AG to ensure his/her independence, impartiality, dignity and effectiveness as well as to advise the National Assembly.
- Scoag considers the budget and the business plan of the AGSA and makes recommendations to the National Assembly and the National Treasury.
- Previous interactions with Scoag have been beneficial to the AG with Scoag's input being considered in the budget and strategic plans of the organisation.



Scoag's role in ensuring accountability by the AG

Reporting requirements

- In line with the constitutional value of accountability, each year the AG provides detailed reports on the annual activities of the organisation to Parliament (sections 181(5) and 188 of the Constitution).
- The AG is in full control of and accountable for his/her administration (section 30(2) of the PAA). His/her administration consists of the DAG and a staff establishment necessary for the work of the AG (section 34 of the PAA).
- According to section 10(2) of the PAA, the AG must annually submit to the National Assembly:
 - a) The report on his/her overall control of the AG's administration.
 - b) The annual report, the financial statements and the audit report on those statements, which:
 - fairly present the state of affairs, including business and financial results, financial position and performance against predetermined objectives (section 41 of the PAA)
 - include any material losses or irregular and fruitless and wasteful expenditure and steps to recover such expenditure
 - disclose donations or bequests (section 36(2) of the PAA)
 - must be submitted within 6 months after the end of the financial year to Scoag and the speaker of Parliament



Scoag's role in ensuring accountability by the AG

(continued)

- Section 40(4) requires a disclosure of the membership of the audit committee. As per section 40(6)(a), the audit committee must comment on:
 - the effectiveness of internal control
 - its evaluation of the AG's annual financial statements

Scoag's role

- As per the existing practice, Scoag engages the AG on the annual report and compiles a report containing a recommendation to the speaker regarding the report.
- Scoag annually appoints an independent external auditor to audit the accounts, financial statements, financial management and performance information of the AG (section 39(1)).



Scoag's role in ensuring accountability by the AG

(continued)

Strategic plan and budget

- Section 38 stipulates that the AG must conduct his/her affairs in accordance with a business plan and budget, which includes:
 - Estimates of revenue and expenditure for the relevant financial year
 - Projected revenue and expenditure for the following two years
 - The basis on which audit fees are calculated
- The plan must be submitted at least 6 months before the start of the financial year to Scoag and the National Treasury.

Scoag's role

- Consider the budget and business plan within 2 months of receipt.
- Submit its recommendations to the National Treasury and to the speaker for tabling in the National Assembly.

Retention of surplus

- The AG may after consultation with the National Treasury and by agreement with Scoag, at the end of a financial year, retain for working capital and general reserves, any surplus as reflected in the annual financial statements. The portion not retained must be paid into the National Revenue Fund.



Augmented accountability reporting requirements

Additional reporting requirements have been imposed by the Public Audit Amendment Act:

- Suspected material irregularities referred to public bodies for investigation.
- Any remedial action taken as a result of failure to implement the AG's recommendations made in respect of material irregularities.
- Any certificates of debt issued for failure to adhere to the AG's remedial action.
- The PAA does not prescribe the reporting format. This is currently being developed.



Annual Scoag-AG interactions

The AGSA recommends the following:

- Discussion of the AG's annual report (October), including:
 - The report of the audit committee
 - The retention of any surplus

Note: Proposed date for 2019 is 11 October

- Discussion of the AG's strategic plan and budget (October), including:
 - The AG's annual audit directive
 - Confirmation of the appointment of the external auditor

Note: Proposed date for 2019 is 25 October

- Post-cycle PAA-related interactions

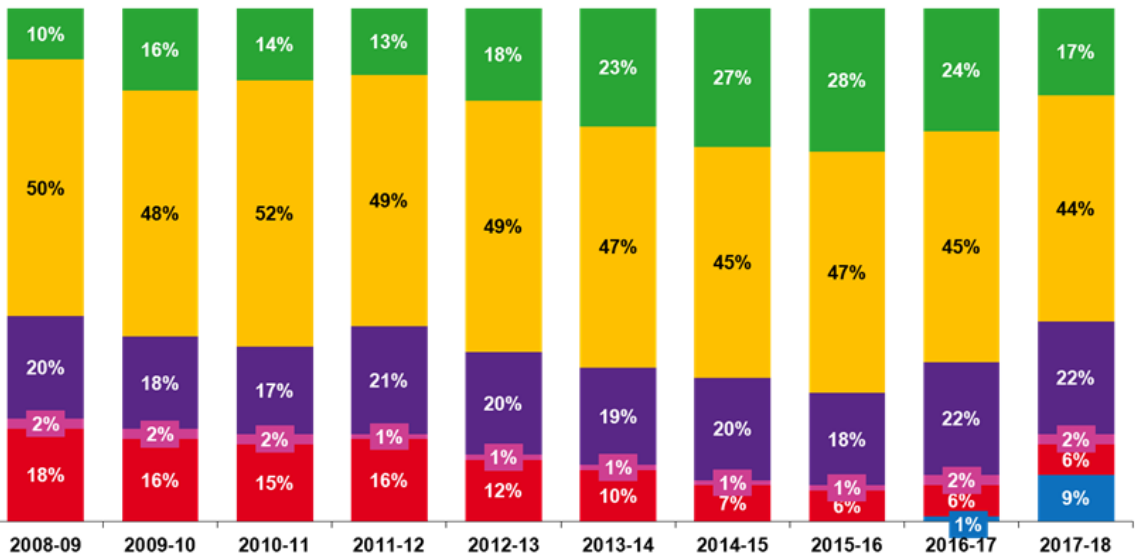




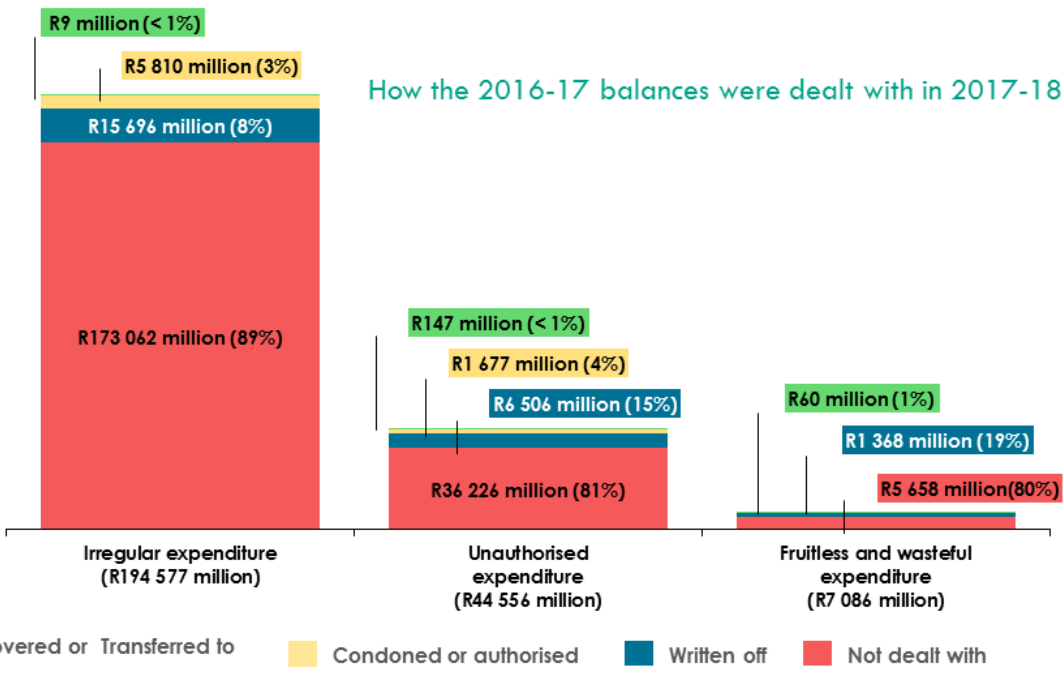
PAA amendments

What gave rise to the amendment of the PAA?

Audit outcomes over the past 10 years - national, provincial and local government



Dealing with unauthorised, irregular and fruitless wasteful expenditure

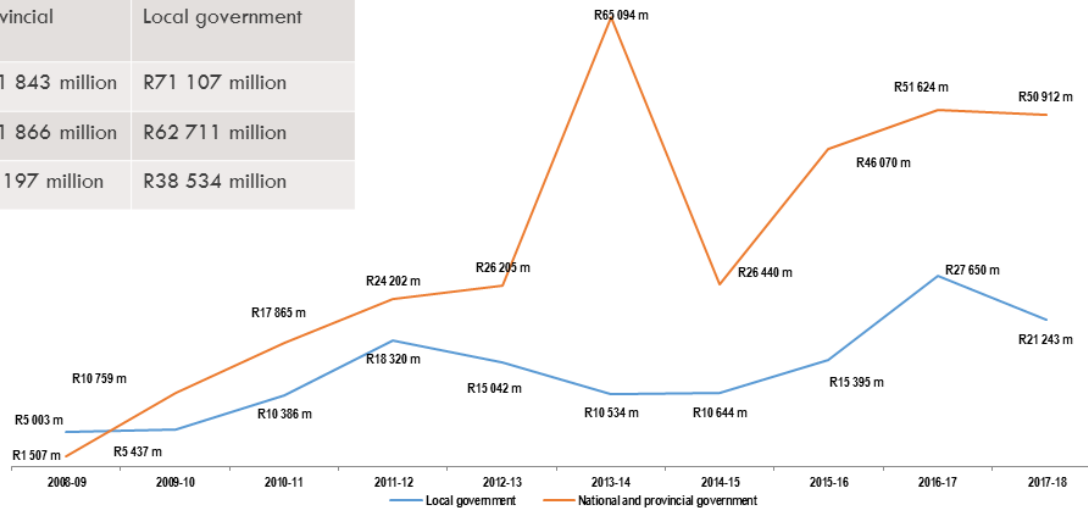


What gave rise to the amendment of the PAA?

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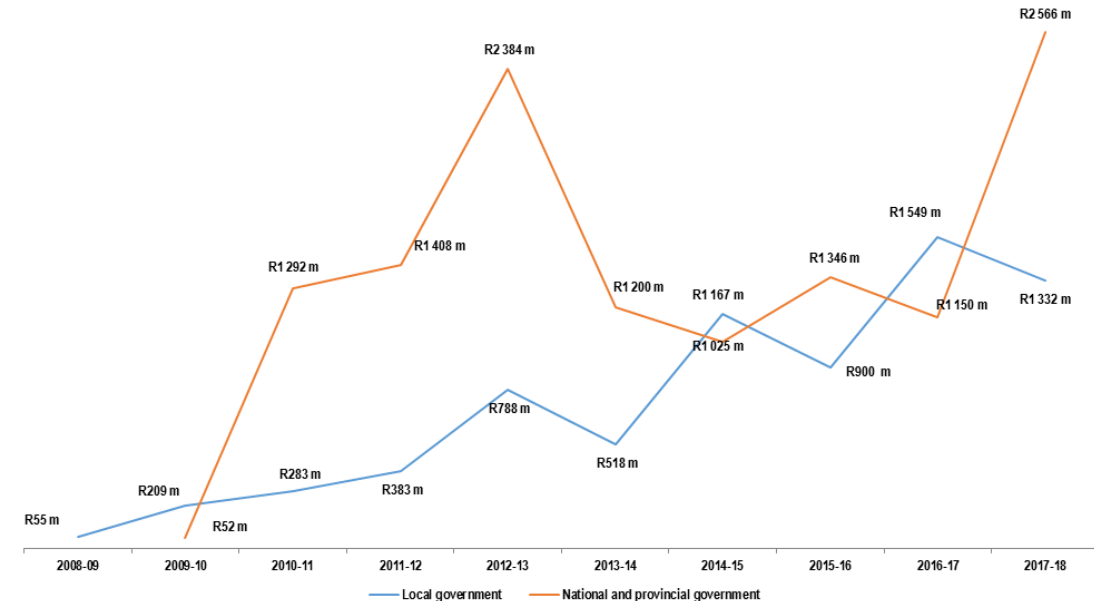
History of irregular expenditure

Balances of irregular expenditure not yet dealt with		
	National and provincial government	Local government
2017-18	R161 843 million	R71 107 million
2016-17	R131 866 million	R62 711 million
2015-16	R95 197 million	R38 534 million



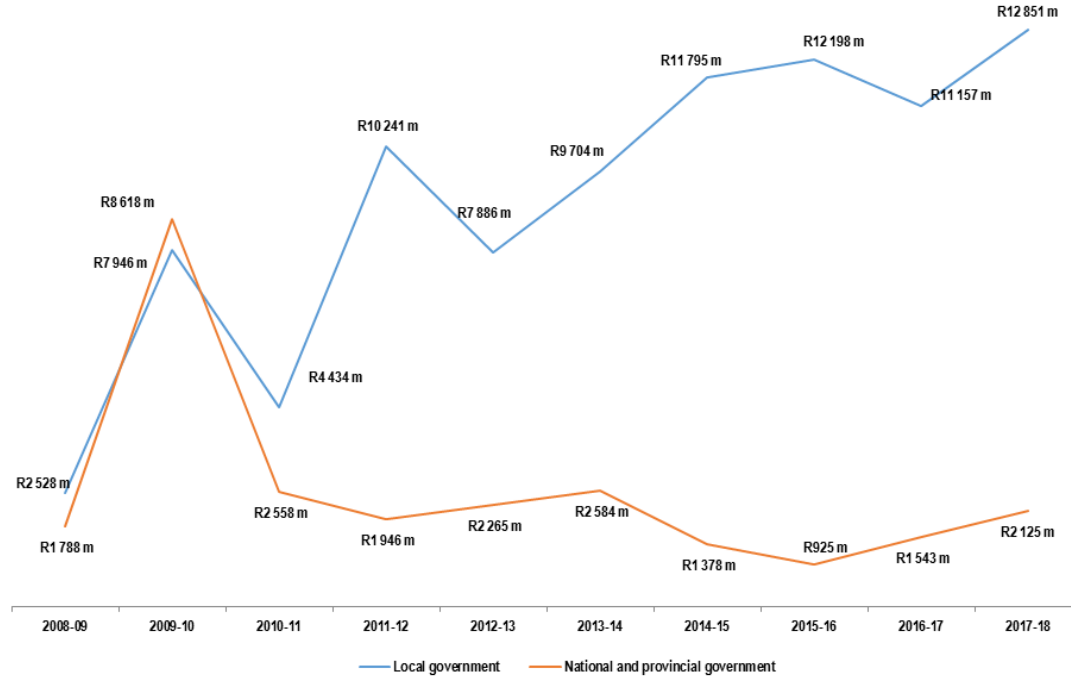
The annual irregular expenditure and the balances as shown is not complete as the disclosure of irregular expenditure is often qualified on completeness thereof – e.g. 74 auditees were qualified in 2017-18

History of fruitless and wasteful expenditure

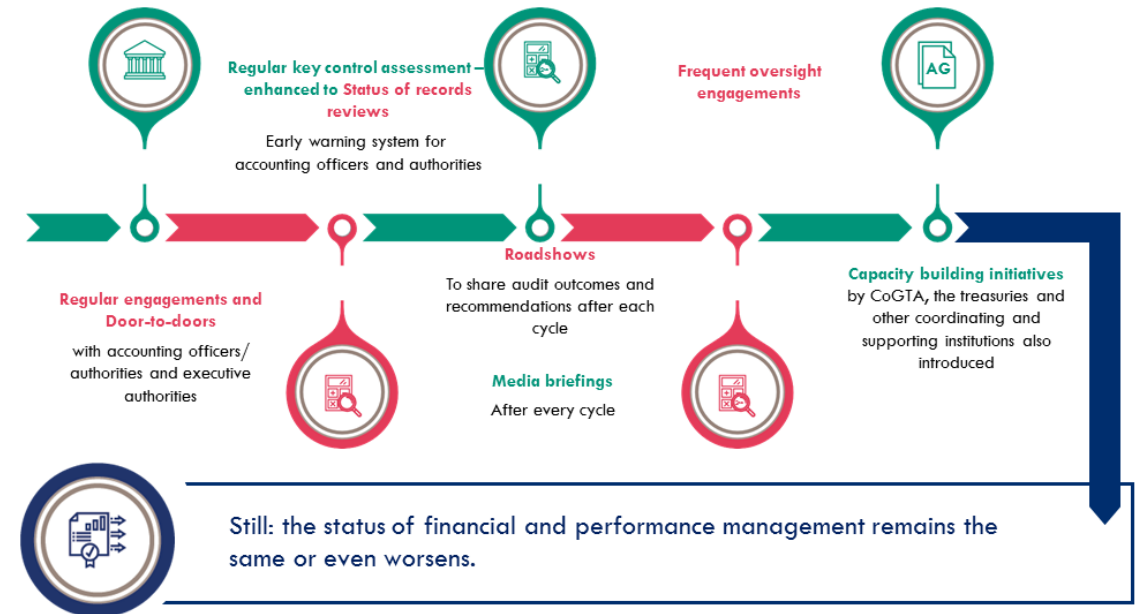


What gave rise to the amendment of the PAA? (continued)

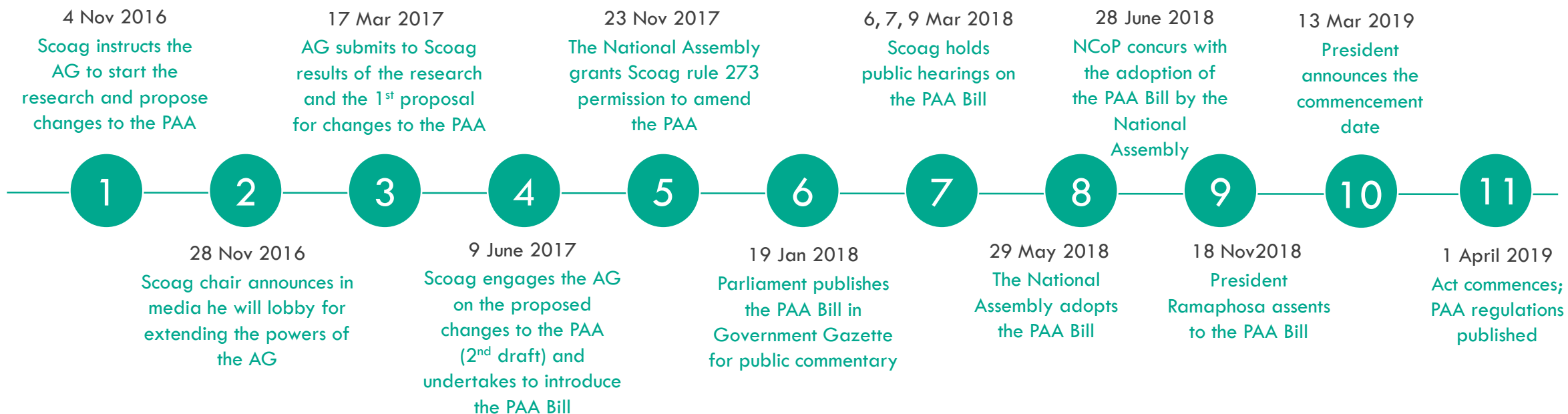
History of unauthorised expenditure



Additional efforts were introduced



PAA amendment road map



17 Jan 2018: PAA project commences to prepare the environment

June - Nov 2018 - Regulations drafting and review process

12 Aug 2018 - Internal stakeholder engagements commence

Jan 2019 - External stakeholder engagements commence

4 March 2019 - Audit teams training

1 June 2019 - PFMA audits commence

To restore the integrity of financial and performance management systems aimed at service delivery and achievement of government's goals





PAA amendments: Legislation

Key definitions

- **Accounting authority** means a body or person defined as an accounting authority in the PFMA, or anybody or person designated as an accounting authority in terms of any other law, as the case may be.
- **Accounting officer** means a person defined as an accounting officer in the PFMA or MFMA, or any person designated as an accounting officer in terms of any other law, as the case may be.
- **Executive authority** means the executive authority as provided for in any relevant legislation applicable to an auditee.
- **Independent Commission** means the Independent Commission for the Remuneration of Public Office-bearers established by section 2 of the Independent Commission for the Remuneration of Public Office-bearers Act, 1997 (Act No. 92 of 1997)



Key definitions *(continued)*

- **Material irregularity** means any non-compliance with, or contravention of, legislation, fraud, theft or a breach of a fiduciary duty identified during an audit performed under this Act that resulted in or is likely to result in a material financial loss, the misuse or loss of a material public resource or substantial harm to a public sector institution or the general public.
- **Prescribed** means prescribed by regulation made in terms of section 52.
- **This Act** includes the regulations.



Amendments on the expansion of the mandate of the office

- **Section 5(1A)** The Auditor-General may, as prescribed, **refer** any suspected MI identified during an audit performed under this Act to a relevant public body for **investigation**.
- **Section 5(1B)(a)** The Auditor-General has the power to take any appropriate **remedial action**. Remedial action can only be taken if the Auditor-General's recommendation in the audit report on how the MI should be addressed hasn't been implemented within the set time-frame.
- **Section 5(1B)(b)** In the event that there is a **failure to implement** the Auditor-General's remedial action the Auditor-General has the power to issue a **certificate of debt**.



Other amendments to the PAA

- **Discretionary audits** – Section 4(3A) requires the Auditor-General to define criteria to opt in or out of discretionary audits. *This criterion has been developed in the Regulations on Audits by Auditors in Private Practice.*
- **Override of conflicting legislation** – Section 4(4) provides that section 4 of the PAA will take preference over any conflicting legislation passed after 1 April 2004.
- **Performance audits** –Section 5(1)(aA) now provides the AG with a clear mandate to conduct standalone performance audits in the public sector.
- **International audits** – Section 5(1)(aB) now provides a clearly articulated mandate to perform international audits. Section 3 of the PAAA now inserts such mandate in section 5 of the PAA, provided that international audits –
 - Will not put undue strain on the AGSA's resources
 - Will not detract the AGSA from the constitutional functions
 - Are properly disclosed to the National Assembly through our accountability reports



Other amendments to the PAA *(continued)*

- **Remuneration committee** – Section 5(2)(bA) provides for the establishment and functions of a remuneration committee.
- **Independent Commission** – Section 7(1A) provides that when considering the remuneration of the Auditor-General, the AGSA's Remuneration Committee and the Minister of Finance must be consulted by the Independent Commission for Remuneration before recommendations to the President pertaining to the remuneration of the AG. Another amendment on remuneration is found in section 34(3) which provides that the AG must consult AGSA's Remuneration Committee on the determination of salaries, allowances and benefits of staff of the AGSA.
- **Accountability reports** – Section 10 of the PAA now provides that the AG reports to the National Assembly yearly on the exercise of the additional powers. Therefore, as from 1 April 2019 our accountability reports will cover the performance and international audits that we perform, as well as information on the matters that we referred for investigation and details on remedial action taken during the course of the reporting cycle as well any certificate of debt issued.
- **1% audit fees** – Section 13(1A) now provides that the AG must consult the National Treasury annually on the frequency, nature and scope of audits to facilitate determination of 1% audit fees.



Other amendments to the PAA *(continued)*

- **Audit fees** – Section 26 (6)&(7) has been amended to provide that the National Treasury contribution towards the 1% audit fees must be defrayed from the National Revenue Fund as a direct charge. The AGSA and National Treasury must agree on annual consultation on audits, criteria to determine financial difficulty, and process to calculate the funds needed for the direct charge.
- **Audit report content** – Section 20 of the PAA has been amended to allow for limited assurance and review engagements, as opposed to reasonable assurance engagements on all our audits. This amendment will allow the freedom to select the most suitable engagement for the size and the risk profile of our auditees. The amendment to this section further provides that the AG may now make any recommendations in the audit report on the annual financial statements, compliance with legislation, and performance information of the auditee.
- **Audit committee** – Section 40 of the PAA now provides that the AG must establish and appoint members of the audit committee.



Other amendments to the PAA *(continued)*

- **Financial reporting framework** – Section 41 has been amended to provide that the annual financial statements must be prepared in accordance with international best practice.
- **Regulations** – Section 52 of the PAA now mandates the AG to make regulations on the following:
 - Criteria for opting in and opting out of discretionary audits
 - The nature and categories of matters in which an investigation or special audit may be carried out
 - The criteria for the referral of a material irregularity for further investigation
 - The process and timeframes for written and oral representations when the AG intends to issue a certificate of debt
 - The form and content of a certificate of debt
- The AG may make further regulations to give effect to any provision in our law and we intend doing so to ensure full implementation of the amendments.



The roles and responsibilities of Scoag as per the amendments

Scoag's role on the remuneration of the AG

- Prior to 1 April 2019, which is the commencement date of the Remuneration Act, 2014 (Act No. 22 of 2014), Scoag had to be consulted on the remuneration of the AG in order for Scoag to make recommendations to the President.
- With the commencement of the Remuneration Act, the Independent Remuneration Committee has assumed the former role of Scoag and now plays the leading role in the process to determine the AG's remuneration.



The roles and responsibilities of Scoag as per the amendments *(continued)*

Scoag's roles and responsibilities on the audit fees amendment

- Section 23(7) provides for an agreement between the AGSA and the National Treasury on annual consultation on audits, criteria to determine financial difficulty, and process to calculate the funds needed for the direct charge.
- In the event that the AGSA and the National Treasury fail to reach the agreement contemplated above within the specified period of time, the responsibility shifts to Scoag after consultation with the AG and the National Treasury to determine the issues that the AG and the National Treasury failed to reach an agreement on.





PAA amendments: MI process

What is a material irregularity?

Irregularity



any **non-compliance** with, or contravention of, legislation, **fraud,**
theft or
a breach of a fiduciary duty

Material
irregularity

identified during an audit performed under this Act
that **resulted in or is likely** to result in ...

Impact



a **material financial loss,**
the **misuse or loss of a material public resource** or
substantial harm to a public sector institution or
the general public.

Examples of material irregularities

Irregularity

Impact



Non-compliance with SCM legislation requiring a competitive bidding process



A material financial loss due to goods being priced above market value



Suspected bribery of an official to approve the payment for services not received



A material financial loss due to no value being received for the money paid



A board of a public entity not exercising its duty with utmost care in investing the funds of the entity



A material loss in the value of the public entity's investments



A repeat disclaimed audit opinion



Substantial harm to the auditee as oversight and accountability are significantly weakened






Neglect in maintaining the infrastructure for sanitation



Substantial harm to the community as a result of contamination of water sources

Material irregularity vs irregular expenditure

What is the	Irregular expenditure	Material irregularity
 Definition	Expenditure incurred in contravention of, or that is not in accordance with, a requirement of any applicable legislation	Non-compliance with, or contravention of, legislation, fraud, theft or a breach of fiduciary duty identified during an audit that resulted in or is likely to result in a material financial loss, the misuse or loss of a material public resource, or substantial harm to a public sector institution or the general public
 Difference: Irregularity	The irregularity is only non-compliance with legislation when incurring expenditure	The irregularity is any non-compliance (not limited to expenditure) as well as fraud, theft or a breach of fiduciary duty
 Difference: Impact	<p>The impact is not specified, as the PFMA requires the accounting officer or authority to determine the impact</p> <p>There can be irregular expenditure that did not result in any losses, misuse or harm</p>	The irregularity must have resulted in, or there must be indicators that it is likely to result in, a material financial loss/misuse or loss of a material public resource or substantial harm to a public sector institution or the general public

Material irregularity vs irregular expenditure

(continued)

What is the

Irregular expenditure

Material irregularity



**Difference:
Value**

The value is the expenditure to date

A material irregularity does not necessarily have a value



Example

A lack of competitive bidding process for the awarding of a contract of R20 million

The irregular expenditure is all the payments made on the contract to date (e.g. R10 million)

A lack of competitive bidding process for the awarding of a contract of R20 million resulting in a material financial loss, as the same service could have been delivered at a lower price (e.g. R18 million)

The financial loss is R2 million (what was lost and what can still be lost)



Legal obligations of an accounting officer / accounting authority to address an irregularity

If an AO/AA is made aware of an irregularity (non-compliance, fraud, theft or a breach of fiduciary duty) the **PFMA, Treasury Regulations and instruction notes typically prescribe** the following steps to be taken:

1. Perform a preliminary investigation to determine the facts and collect information on what caused the transgression, who is responsible, and whether a financial loss was suffered (or will be).

If applicable

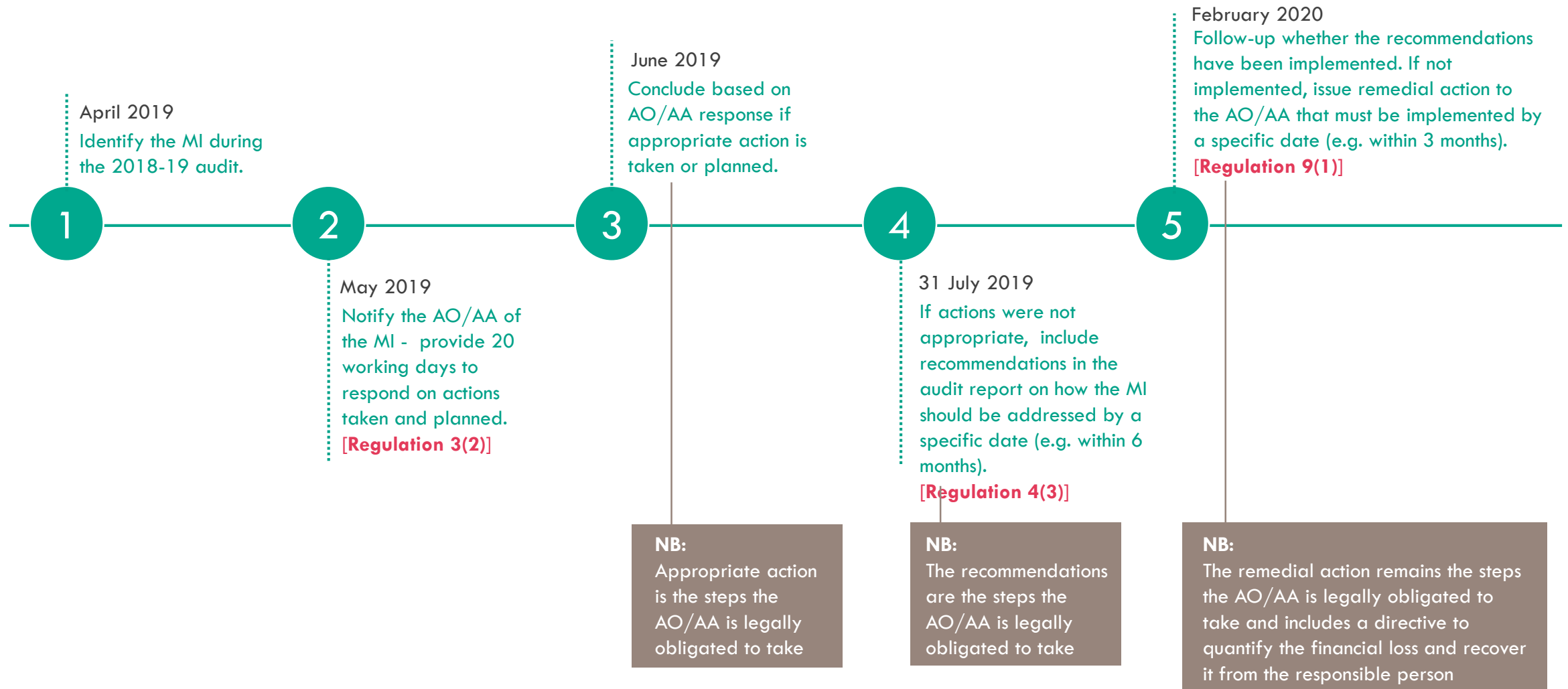
2. Prevent any losses or further losses.
3. Institute a formal investigation if there are indications of fraud, corruption or other criminal conduct. If confirmed, take further action (e.g. report the matter to the SAPS).
4. Recover any financial losses from an external party.
5. Take steps against the responsible official (which can include a financial misconduct investigation).
6. Recover any financial losses from the responsible officials.

The policies and procedures of an auditee typically describe how these steps should be taken and the timing thereof.

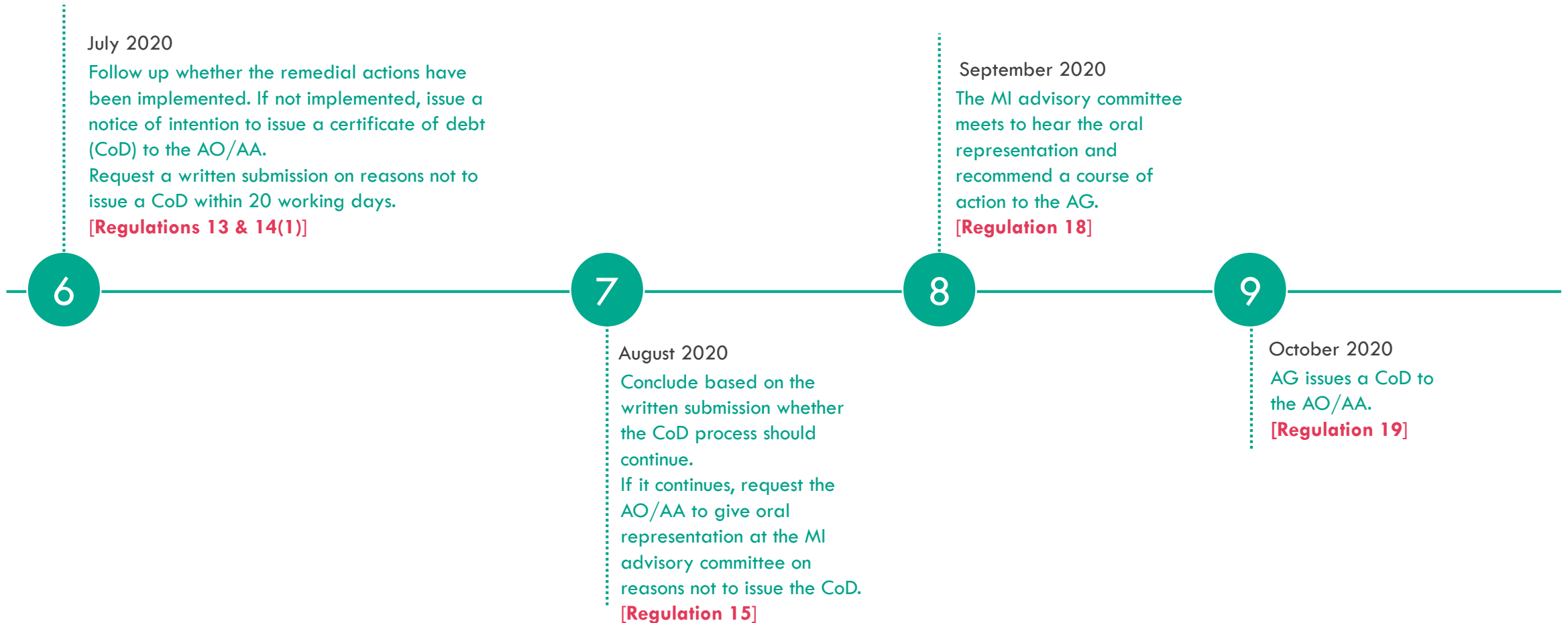
The same steps should be taken if an AO/AA is notified of a material irregularity



Example - MI process for an irregularity that caused a material financial loss (remedial route)



Example - MI process for an irregularity that caused a material financial loss (remedial route) *(continued)*





PAA amendments: Implementation approach

Implementation of expanded mandate



- The AG has the sole discretion to determine the nature, frequency and scope of audits [section 13(1) of the PAA]
- The AG **may** refer material irregularities to public bodies for investigation [section 5(1A) of the PAA]
- The AG **may** make recommendations in the audit report regarding any matter, including material irregularities [section 20(4) of the PAA]
- The AG consulted Scoag on the notion of a phased-in implementation of the material irregularity process

Implementation of expanded mandate *(continued)*



Commencement date 1 April 2019

To allow for establishing capacity and processes, a **phased-in approach** for implementation was agreed with Scoag on the basis of:

1. The type of material irregularity to be identified and reported
2. The auditees where it will be implemented
3. Auditees that are not part of the phased-in approach will be dealt with in terms of the NOCLAR requirements

2018-19 implementation

Type of material irregularity

Type of material irregularity = material non-compliance (which would be reported in the audit report) that resulted in (or is likely to result in) a material financial loss

Selection of auditees

Selection criteria

- Latest audit outcome not clean or unqualified with findings – except if there was a material finding on prevention or follow-up of irregular expenditure
- High irregular expenditure over the last three years
- Sufficient coverage across spheres of government and provinces



Implementation of expanded mandate *(continued)*



The phasing-in of the implementation of the amendments allowed us to:

Responsibly align the organisational resources with the demand placed on us by the PAA

- Develop understanding of the required additional resources to implement the powers
- Reassess the audit methodology and the audit process to accommodate the additional work
- Develop the requisite content and capacitate the audit teams via extensive training
- Develop tools and systems to facilitate the remedial action and referral processes
- Build adequate support capacity
- Ensure that we are able to fund the additional effort
- Develop adequate materiality threshold to ensure value for audit fees
- Enhance the relevant internal processes to ensure adequate accountability reporting

Ensure that our external partners are adequately prepared

- Establish relationships with the identified public bodies

Due to the lack of accountability in the public sector it resulted in the acceleration of the PAA amendments in less than a year, which was unprecedented given the various legal steps to pass any legislation. This meant that the AGSA had to assess and take cautious steps in order to ensure that it had adequate capacity to carry out the new mandate in a responsible manner.



Implementation of expanded mandate *(continued)*



The phasing-in of the implementation of the amendments allowed us to:

Create the required level of awareness of the act and the regulations in the external environment

- Extensive engagement with constitutional stakeholders
 - Accounting officers, accounting authorities, executive authorities and audit committees
 - Oversight – deferred to accommodate the election and post-election processes
- Non-constitutional stakeholders
 - Media
 - Professional bodies
 - Civil society
 - Audit firms

Due to the lack of accountability in the public sector it resulted in the acceleration of the PAA amendments in less than a year, which was unprecedented given the various legal steps to pass any legislation. This meant that the AGSA had to assess and take cautious steps in order to ensure that it had adequate capacity to carry out the new mandate in a responsible manner.



Implementation of expanded mandate

(Phased-in auditees)

PFMA LIST

1. Department of Cooperative Governance
2. Passenger Rail Agency of SA
3. Department of Defence
4. Department of Correctional Services
5. Department of Water and Sanitation
6. Water Trading Entity
7. SAA Technical
8. Department of Basic Education
9. Department of Education (EC)
10. Department of Health (NC)
11. Department of Health (KZN)
12. Department of Human Settlements (FS)
13. Department of Health (GP)
14. Department of Health (MP)
15. Community Safety and Transport Management (NW)
16. Department of Education (LP)

MFMA LIST

1. Nelson Mandela Bay Metropolitan Municipality (EC)
2. Matjhabeng Local Municipality (FS)
3. City of Tshwane Metropolitan Municipality (GP)
4. Ethekewini Metropolitan Municipality (KZN)
5. Mogalakwena Municipality (LP)
6. Dr JS Moroka Municipality (MP)
7. Ga-Segonayana Local Municipality (NC)
8. Ngaka Modiri Molema District Municipality (NW)
9. City of Cape Town Metropolitan Municipality (WC)





Oversight and monitoring

Role of oversight and executive authority

Executive authority

- Insist on credible and frequent **reporting** on state of financial and performance management
- Use reports to **monitor, direct and support accountability**
- **Set the tone** for accountability and consequence management by investigating and dealing with any allegations of financial misconduct and irregularities by accounting officers and authorities
- **Share any knowledge** on possible material irregularities
- Monitor the **implementation of the recommendations** on material irregularities
- **Support referral and remedial processes**, including recovery of debt, if required
- If responsible for **public body – monitor progress of investigations**

Oversight structure

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



Effective oversight in preventing and tracking material irregularities

Oversight and monitoring

Material irregularities	Financial management	Performance management	Procurement and contract management	Compliance management	Information technology management	Human resource management	Oversight report
Progress report on the material irregularities reported	Financial statements (interim and final)	Strategic and annual plans	Contracts and registers Major project register and tracking reports Supply chain management report, including procurement plans	Reports on compliance reports	Information technology governance and management reports	Human resource management information	Risk management reports
Investigation reports	Financial health analysis reports	Annual and quarterly performance reports		Budget reports		Use of consultants information	Internal audit reports
Disciplinary cases reports				Consequences reports			Audit committee reports
Progress reports on matters referred to the public bodies				UIFW reports			
Recovery reports on financial loss suffered				Management revenue and expenditure reports			
				Grant management reports (compliance)			



Threats and intimidation against auditors

Threats and intimidation: background

There is concern regarding sporadic instances of threats and intimidation against our auditors during their course of duty. However, this risk has not reached out-of-control levels. The following are examples of incidents reported since May 2018:

- Gauteng: **Emfuleni Municipality (October 2018)** – One team member was shot at a guesthouse.
- Gauteng: **City of Tshwane (October 2018)** – Audit team members were held hostage by a contractor who was demanding payment from the municipality.
- North West: **Moretele Municipality (October 2018)** – A staff member of the auditee narrated a story of an auditor who was killed because he had raised a finding.
- KZN: **eThekweni Metropolitan Municipality (May 2018)** – One team member received a telephone call threatening him and his family. The latest incident at **eThekweni (April 2019)** was that eavesdropping devices were found at the auditee's premises.



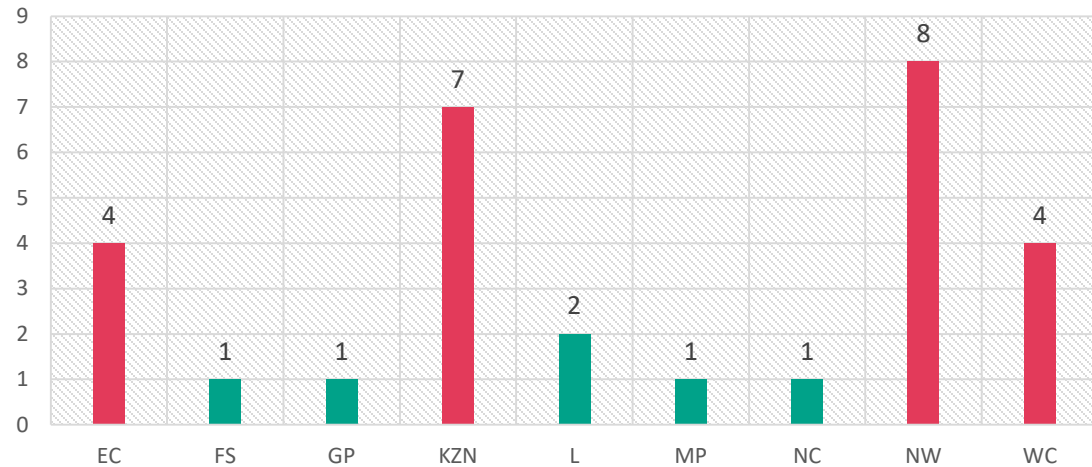
Threats and intimidation: background *(continued)*

- The organisation **acted immediately to remove the teams from the auditees**, institute investigations and provide appropriate security support where necessary to mitigate the risks.
- With the increased powers of the AG due to the amendments to the PAA, we foresee that the threats and intimidation risk may increase.

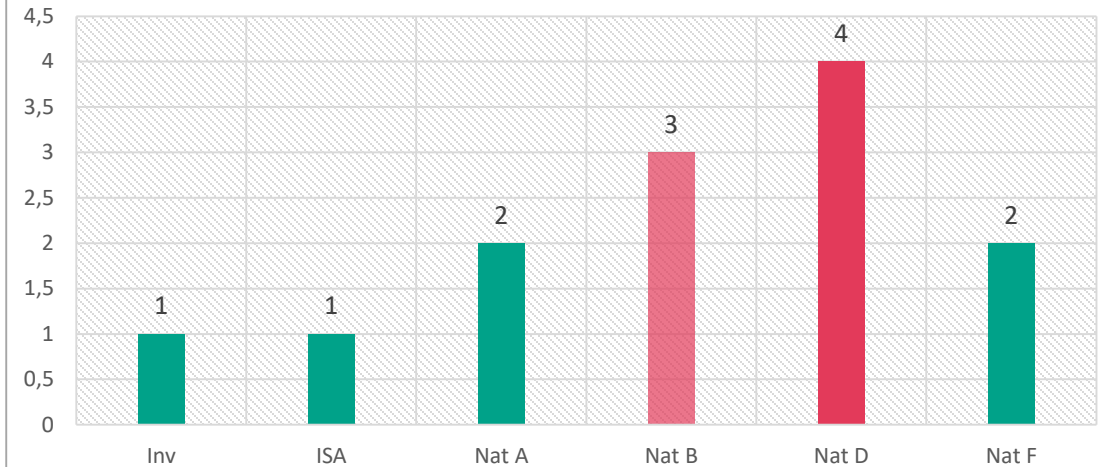


Summary of incidents

Intimidation or threat - provincial BUs

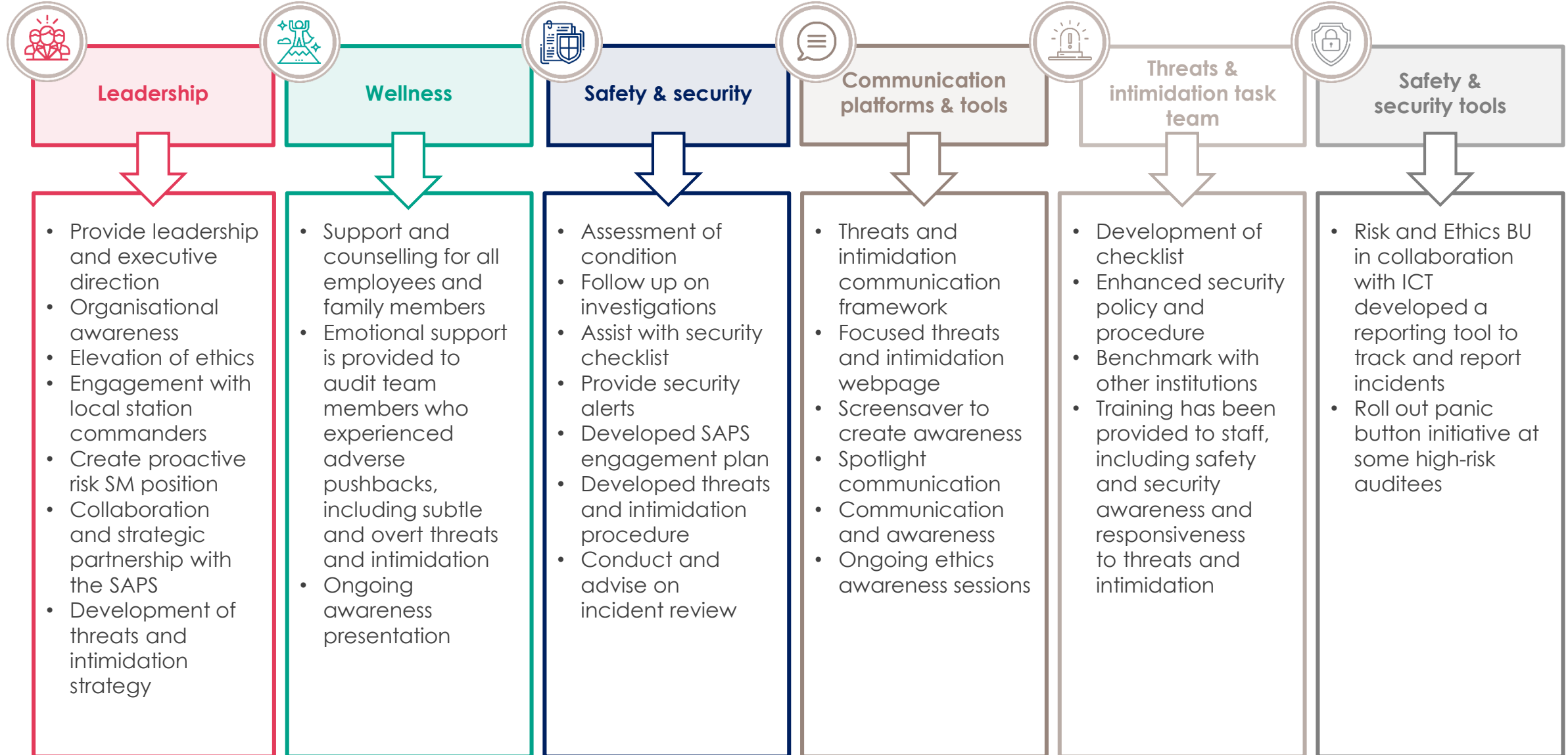


Intimidation or threat - national BUs & SAS



- All (42) reported incidents were attended to by the threat and intimidation task team. 29 (or 69%) of these incidents occurred at the provincial BUs and the rest were at national BUs, including Specialised Audit Services. The AGSA also escalated these cases to the accounting officers where appropriate for further intervention and there was a positive response to address the incidents.
- Six of the above incidents were reported to the SAPS: two of these are still under investigation and four have been closed due to a lack of evidence.

Initiatives to support auditors



Thank you



www.agsa.co.za



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