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LEGAL OPINION
[Confidential]

MEMORANDUM

TO: Honourable E Mthetwa, MP
Co-Chairperson: Constitutional Review Committee

AND TO: Honourable Dr M Motshekga, MP
Co-Chairperson: Constitutional Review Committee

COPY: Acting Secretary to Parliament [Ms P N Tyawa]

FROM: Constitutional and Legal Services Office
[Adv Z Adhikarie, Chief Parliamentary Legal Adviser]

DATE: 1 December 2020

REF. NO.: 133/2020

RE: Annual review of the Constitution - Desirability to bolster our Constitution by adding a 10th Chapter 9 institution called the Commission for Internal Auditors

Introduction

1. Our Office was requested to advise the Joint Constitutional Review Committee (“the Committee”) on the proposal received concerning statutory appointment of internal auditors.

Background

2. On 11 May 2020, the Chairpersons of the Committee received a submission proposing that a 10th institution, the Institution of Internal Auditors, be added to the list of Chapter 9 institutions.
3. The proposal, in summary, suggests that by adding the institution of Internal Auditors it would render internal auditors independent of Boards and management.
4. In doing so, it is envisaged that internal auditors’ reports will form part of the organization’s annual reports and once part of annual reports, governments/shareholders and the public will have access to internal auditors’ reports.
5. The upshot of this as proposed, is that Governments/shareholders will be in a positions to retrieve their governance roles that has been abdicated to different organizations and Government will be able to fully govern through the Constitution, based on ongoing feedback by internal auditors.
6. It is submitted that through these comprehensive organizational reports, the public will be in a better position to hold Government accountable.
7. It is further submitted that by creating the additional institution it will allow for internal auditors to focus on preventative controls which will relieve the Auditor-General to focus on detective controls.

Regulatory framework

8. Section 59 (1) of the Constitution provides that the National Assembly must facilitate public involvement in the legislative and other processes of the Assembly and its committees.

9. Section 195 of the Constitution sets out the basic values and principles governing public administration. It stipulates that:

"1. Public administration must be governed by the democratic values and principles enshrined in the Constitution, including the following principles:

a. A high standard of professional ethics must be promoted and maintained.

b. Efficient, economic and effective use of resources must be promoted.

c. Public administration must be development-oriented.

d. Services must be provided impartially, fairly, equitably and without bias.

e. People's needs must be responded to, and the public must be encouraged to participate in policy-making.

f. Public administration must be accountable.

g. Transparency must be fostered by providing the public with timely, accessible and accurate information.

h. Good human-resource management and career-development practices, to maximise human potential, must be cultivated.

i. Public administration must be broadly representative of the South African people, with employment and personnel management practices based on ability, objectivity, fairness, and the need to redress the imbalances of the past to achieve broad representation.

2. The above principles apply to

a. administration in every sphere of government;

b. organs of state; and

c. public enterprises."

10. Rule 227 of the Rules of the National Assembly provides for the functions of portfolio committees in the performance of their oversight function. Rule 227(1)(b) provides that a portfolio committee must maintain oversight of the exercise of national executive authority and any executive organ of state falling within its portfolio, including the implementation of legislation. Rule 227(1)(c) goes on to say that a portfolio committee, “may monitor, investigate, enquire into and make recommendations concerning any such executive organ of state, rationalisation, restructuring, functioning, organisation, structure, staff and policies of such organ of state, institution or other body or institution.
11. Chapter 9 of the Constitution of the Republic of South Africa, 1996 establishes the Auditor-General of South Africa (AGSA) as one of the state institutions supporting constitutional democracy. The Constitution acknowledges the importance and guarantees the independence of the AGSA, stating that the AGSA must be impartial and must exercise its powers and perform its functions without fear, favour or prejudice.
12. Section 181(5) of the Constitution and section 3(d) of the Public Audit Act (PAA) stipulates that the AGSA has to report to the National Assembly on its activities and performance of its functions executed in terms of section 10 of the PAA.
13. Section 188 of the Constitution and the PAA regulate the functions of the AGSA and authorises the AGSA to perform constitutional and other functions. Constitutional functions are those which the AGSA performs to comply with the broader mandate described in the Constitution. Section 4 of the PAA makes a further distinction between mandatory and discretionary audits.
14. Section 188 lists the functions of AGSA. It stipulates that:

“188 (1) The Auditor-General must audit and report on the accounts, financial statements and financial management of—

(a) all national and provincial state departments and administrations;

(b) all municipalities; and

(c) any other institution or accounting entity required by national or provincial legislation to be audited by the Auditor-General.

(2) In addition to the duties prescribed in subsection (1), and subject to any legislation, the Auditor-General may audit and report on the accounts, financial statements and financial management of—

(a) any institution funded from the National Revenue Fund or a Provincial Revenue Fund or by a municipality; or

(b) any institution that is authorised in terms of any law to receive money for a public purpose.

(3) The Auditor-General must submit audit reports to any legislature that has a direct interest in the audit, and to any other authority prescribed by national legislation. All reports must be made public.

(4) The Auditor-General has the additional powers and functions prescribed by national legislation.”

15. The AGSA is accountable to the National Assembly in terms of section 181(5) of the Constitution and section 3(d) of the PAA. It is obligated to report on its activities and performance of its functions in terms of section 10 of the PAA.
16. The primary accountability mechanisms are the AGSA’s annual budget and strategic plan, as well as the annual report, both of which are tabled in the National Assembly. The Standing Committee on the Auditor-General (SCoAG), established in terms of section 10(3) of the PAA, oversees the performance of the AGSA on behalf of the National Assembly.
17. Section 188 stipulates that the AGSA must annually produce audit reports on all government departments, public entities, municipalities and public institutions. In addition to these entity-specific reports, the audit outcomes are also analysed in general reports that cover both the Public Finance Management Act (PFMA) and Municipal Finance Management Act (MFMA) cycles.
18. Over and above this, reports on discretionary audits, performance audits and other special audits are also done. The AGSA tables reports to the legislature, namely Parliament,

provincial legislatures or municipal councils, who all have a direct interest on the audit. These reports are then used in accordance with their own rules and procedures for oversight.

19. An Internal Audit (IA) Framework was developed by National Treasury during the 2003/2004 financial year, which derived its mandate from the Public Finance Management Act, (Act No. 1 of 1999 as amended by Act 29 of 1999) (PFMA), and the Municipal Finance Management Act, (Act No. 56 of 2003) (MFMA). The Framework sought to establish a minimum guideline for internal auditing in the Public Service and it provided a frame of reference and serves as a guidance mechanism on internal auditing in the Public Service.
20. An Audit Committee (AC) is an independent governance structure which provides an oversight role on the internal control systems, risk management, and governance. Section 76(4) (d) of the PFMA stipulates that “the National Treasury may make regulations or issue instructions concerning AC’s, their appointment and their functioning.”
21. The function of the AC is to assist the Accounting Officer (AO) in the effective execution of his/her duties and functions in line with the objectives of the organisation.
22. The PFMA and MFMA both make provision for the establishment of the Internal Audit Activity (IAA) to assist the AO and the AC in the effective discharge of their responsibilities. The IAA provides an independent investigation, evaluations, recommendations, advice and information concerning the activities assessed with a view to enhancing accountability and performance.

Discussion

23. Our understanding of the proposal is that internal auditors are appointed by organizations on an ad hoc basis, unless required by empowering legislation, the Public Finance Management Act, 1999 or the Municipal Finance Management Act, 2003, and many organizations may not have internal auditors in their governing structures.

24. The argument is that internal auditors are the weakest link of the three pillars of audit and governance as they report to management and their reports end internally with management.
25. The AGSA looks at strategic government objectives, programmes and initiatives and reacts to identified risks.
26. Audit reports contribute to a culture of public sector accountability and transparency in Government.
27. The analyses in the AGSA's general report, which are accessible to the public, are aimed at refining the state's overall financial management and improving service delivery reporting.
28. In order to re-establish accountability, the AGSA has introduced preventative control guides that enable oversight structures to determine whether the most important preventive controls are employed by institutions to address their main areas of risks. This assists oversight structures to detect weaknesses in preventative mechanisms and enables these structures to focus their oversight efforts on obtaining assurance from the executive authority and the accounting officer or authority that those defects are being effectively remedied in accordance with their legislated obligations.
29. Internal controls can be categorised as preventative controls, detective controls and corrective controls. Preventative controls are the controls designed and implemented by management to avoid threats to the objectives of the institution materialising. Detective and corrective controls focus more on identifying and correcting failures after they had already occurred.
30. The Public Audit Act has been recently amended to introduce the concept of a material irregularity. Now, when the AGSA performs an audit, the staff on the audit must satisfy themselves, through various tests of transactions of account balances and systems of control, that there has been no flouting or non-compliance of a financial statute and that the entity is not exposed to the risk of fraud which could result in a financial loss, the loss of a public asset or that the organisation is not hindered in the provision certain services due to the financial losses sustained. Once a material irregularity has been identified or is suspected during an audit performed under this Act, the AGSA is authorised to refer any such material irregularity to a relevant public body for investigation, take appropriate legally

binding remedial action and/or issue a certificate of debt where an accounting officer or accounting authority has failed to comply with the remedial action.

Advice

31. It appears that the concerns raised are already addressed and legislated for in existing legislation and the preventative control functions are already executed by the AGSA. The addition may result in a duplication of functions, depending on the mandate of the proposed structure.
32. The addition of a 10th Chapter 9 institution will have financial implications of having to employ additional people to head and work in the institution.
33. The Committee may want to consider addressing correspondence in reply to the proposal advising that the concerns raised are provided for in existing legislation.

SIGNED ELECTRONICALLY



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Chief Parliamentary Legal Adviser