Report of the Standing Committee on the Auditor-General on the Integrated Annual Report of the Auditor General for The Financial Year 2020/21, Dated 26 November 2021

The Standing Committee on the Auditor-General, having considered the Integrated Annual Report of the Auditor-General 2020/21, referred to it, reports as follows:

1. Introduction

The Public Audit Act (the PAA) requires the Auditor-General (AG) to submit the annual report, the financial statements, and the audit report on those statements within six months after the end of the financial year to which they relate, to the Standing Committee on Auditor-General (SCOAG) through the parliamentary processes.

The AG satisfied the afore-said requirements by submitting the Auditor-General of South Africa's (AGSA) annual report, financial statements, and audit report to the Speaker for tabling in the National Assembly and for referral to the SCOAG.

In exercising its responsibility, the SCOAG invited the AG, her management team, and the Independent Audit Committee to make a presentation on the AGSA's Integrated Annual Report and financial statements, including the Report of Independent Auditors on the Financial Statements and Performance Information for 2020-21. Flowing from that interaction, the SCOAG highlighted and deliberated on some key issues raised in those interactions concerning the tabled Integrated Annual Report of AGSA.

2. Corporate Governance structures of AGSA

The Accounting Officer of AGSA is the Deputy Auditor-General (DAG). The DAG is appointed in terms of Section 31 of the PAA. He is expected to amongst others, take all reasonable steps to ensure that full, true, and effective records of all income and expenditure and all assets, liabilities, and all financial transactions of the AGSA are in place. In the same vein, the AG has to take all reasonable steps to ensure that AGSA has and maintains a system of internal audit under the control and direction of an audit committee. Mr Vhonani Chauke was appointed as the Deputy Auditor-General effective from 1 July 2021.

Another critical governance structure is the Audit Committee (AC) of AGSA. This committee is established in terms of section 40 of the PAA. Members of the Audit Committee (AC) of AGSA are appointed by the AG in compliance with section 40 of the PAA as amended. Further, the PAA provides that those members may not be in the employ of AGSA; and their term of office is not time-bound. The AC of AGSA is responsible for oversight of the financial and non-financial reporting processes, the integrity of the system of internal control, and risk management. Currently, it consists of four (4) members, including its Chairperson, who are independent, knowledgeable, have the requisite business, financial and leadership skills, and do not hold any political office.

The second structure that plays a critical role in assisting to oversee AGSA is its Internal Auditors. The current Internal Auditors were appointed through a tender process which was overseen by the AC of AGSA. The primary role of the internal auditors is to conduct internal audits and advise the AC and AGSA Management on possible areas that need to be strengthened. Currently, Ngubane & Co are employed as the internal auditors of AGSA, replacing SNG-Grant Thornton, whose term came to an end during the 2018/19 financial year. Ngubane & Co are employed on a three-year contract, which started in the 2019/20 financial year.

The existence of external auditors also plays a crucial role to ascertain the prudent financial management of AGSA's resources. The appointment and role of the External Auditors are prescribed in the PAA. Section 39 (1) of the Act, which provides that the oversight mechanism (the SCOAG) must appoint, annually, an independent external auditor to audit the accounts, financial statements and financial management and performance information of the Auditor-General. Whereas section 39 (2) (b) of the Act stipulates that any such person appointed as an external auditor may not be a staff member in the administration of the Auditor-General. The current External Auditors, Crowe Jhb were appointed in December 2017 after the contract of Kwinana ended. The AC has facilitated the appointment of External Auditors through a fair, equitable, transparent, and cost-effective process; and in line with an AGSA's transformation agenda.

3. Financial performance information

The AGSA has generated an actual revenue of R3.4 billion for the 2020/21 financial year, which is less than R3.7 billion generated in the 2019/20 financial year. This represents a decrease of 11, 5 percent when it is compared with the revenue generated in the 2020/21 financial year. Importantly, this is the first decrease in revenue generated since the 2016/17 financial year. This decrease in revenue generated can be attributed to several factors, such as increased unbilled hours, especially during the local government audits, lower collections from auditees, and legislated delays in starting audits. The reporting deadlines for national, provincial, and local government had to be adjusted to allow the auditees to complete their work before the AGSA's audit process could begin. Thus, all these revenue enhancements and efficiencies adopted by AGSA during the 2019/20 financial year, resulted in an increase in AGSA's own revenue to 78 percent and the reductions in the audit work allocated to private audit firms.

For the 2020/21 financial year, the AGSA has achieved a deficit of R293 million. This is in contrast with the good performance which was recorded in the previous financial years. For instance, the AGSA generated a surplus of R190 million generated in 2019/20 financial year R67 million and R71 million for 2017/18 and 2018/19 financial years respectively. Even though the AGSA has recorded a deficit, it managed to contain the deficit through efficient management overhead expenses and cost containment, which was important given the state of the country's economy, and the pressure put on AGSA's revenue due to the Covid-19 pandemic. Further, to curtail the deficit from R318 million recorded in the first quarter to the current closing balance of R293 million, the AGSA streamlined its expenditure by amongst others, not to award salary increases and performance bonuses to employees. In addition to its own revenue, AGSA received an amount of R44 million from National Revenue Fund to fund the implementation of the amended PAA.

In spite of the above, at the end of 2020/21 financial, 2019/20 financial year, AGSA's financial diligence has led to a favourable balance of R576 million, which is lesser than the R674 million recorded in the 2019/20 financial year. Importantly, the decrease in the favourable bank balance is mainly due to lower collections from auditees. This decrease in favourable bank balance can be translated into 1, 8-month cash reserves, compared to three months cash reserves recorded in the previous financial year. Basically, with the current cash reserves, and assuming that no other cash AGSA will receive, it can only take AGSA one month and eight days to operate.

3.1. Outstanding debts

For the 2020/21 financial year, the debt owed to AGSA has increased, overall. At the end of 31 March 2021, AGSA was owed an amount of R1.1 billion which is more than the amount owed in the 2019/20 financial year (R931 million). This shows an increase of 17 percent year- on-year. It is worth noting that the outstanding debts to AGSSA have been increasing since previous financial years. For instance, in the 2017/18 financial year, AGSA's total debts amounted to R650 million. For the 2018/19 and 2019/20 financial years, the outstanding debts recorded an amount of R744 million and R931 million respectively. The aforesaid periods are in contrast with financial years such as the 2016/17 financial year, whereby, outstanding debts to AGSA decreased.

It is further reported that the main contributors to the increase in the recorded outstanding debts to AGSA are local government auditees (municipalities), which accounted for 41 percent of the total outstanding debts (R1.1 billion). For the 2020/21 financial year, the local government's outstanding debts, amounted to R722 million, an increase from R425 million recorded in the previous financial years. In addition, there is a noticeable increase in the outstanding debts from the SOEs, especially those that are being liquidated.

Importantly, historically, AGSA used to experience a challenge of outstanding debts which were mounting annually. In conjunction with the SCOAG, in 2014, AGSA introduced some enhancement collection strategies, which include ring-fencing of the outstanding debts with auditees and litigation of auditees. Following the implementation of those strategies, the challenge of outstanding debts subsided pointing to the effectiveness of these strategies. However, with some financial challenges from municipalities and some SOEs, those strategies may not be so effective going forward.

4. Non- financial information

Under the strategic objective: *Enable operational effectiveness and efficiencies*, the AGSA planned to achieve 80%-90% implementation of 2020/21 ICT projects to implement the ICT strategy. For the 2020/21 financial year, only 77 percent of ICT projects were implemented towards achieving ICT Strategy. Some of the reasons for this non-achievement of this performance target include amongst others, delay in finalisation of IT strategy, retention of ICT employees that resulted in a high turnover of employees in IT infrastructure.

5. Other critical issues emanated from the Integrated Annual Report of AGSA

5.1. Scope of section 4 (3) Audits

Section 4 (3) of the PAA states that the Auditor-General may audit and report on the accounts, financial statements, and financial management of-

(a) Any public entity listed in the Public Finance Management Act; and
(b) Any other institution not mentioned in subsection (1) and which is-
(i) Funded from the National Revenue Fund or Provincial Revenue Fund or by a municipality.
(ii) Authorised in terms of any legislation to receive money for a public purpose

In spite of the above, currently, AGSA directly audits 15 out of 21 public entities listed in Schedule 2 of the PFMA (large and complex SOEs). The number of SOEs under the audit portfolio of AGSA has been increasing in the previous financial years. For the 2021 financial year, AGSA added Transnet as one of the large and complex SOEs under the audit portfolio of AGSA, of which, the process is in place to take over ESKOM.

Significantly, for those SOEs, which are still not yet under the AGSA's audit portfolio, the AG has enhanced their audits oversight by implementing the PAA regulations. This has to ensure that AGSA concurs with the conditions of appointing private auditors to those SOEs. In implementing such enhanced strict audits oversight to those SOEs, which are still yet to become under AGSA's audit Portfolio, AGSA has identified threats of familiarity at some institutions that have been audited by the same private auditors for between five to twenty years. To emphasise, its commitment to good governance for those SOEs, AGSA imposed some conditions, which include amongst others, that those SOEs should appoint new auditors for the 2021/22 financial year. In this regard, AGSA reported that they receive pushbacks from other SOEs.

5.2. Appointment of External Auditors

Section 39 (1) requires the SCOAG to annually appoint an independent external auditor to audit the accounts, financial statements, and financial management and performance information of the AGSA. The Audit Committee of AGSA facilitates the appointment of external auditors through a fair, equitable, transparent, and cost-effective process that is in line with an AGSA's transformation agenda.

During the 2017/18 consideration of the Annual Report of the AGSA, the Audit Committee recommended the appointment of Crowe Jhb to SCOAG. In December 2017, the SCOAG approved the appointment of Crowe Jhb as an external auditor on the condition that they present to SCOAG a transformation plan by 30 June 2018, which they only managed to submit in July 2018. It is worth noting that SCOAG recommended that the Audit Committee should furnish it with the quarterly reports on the implementation of the transformation plan of Crowe Jhb.

In pursuance of the above, for the period under review and the previous financial year, the SCOAG never received any progress report from the Audit Committee.

Currently, the Audit Committee has once again recommended the appointment of Crowie Jhb as the external Auditor of AGSA.

6. The Committee Observations and findings:

The Committee made the following observations:

1. The Committee noted the report in terms of the transformation of the Crowe Jhb, as it was a condition of their appointment. Subsequently, their B-BBEE score has improved from level 7 to level 4 since 2019 and their target as per their transformation plan is B-BBBE Level 3 contributor for the year 2022.

   Importantly, the Committee noted the fact that as part of the appointment terms of Crowe Jhb, the SCOAG had recommended that the Audit Committee should furnish it with progress reports quarterly on the implementation of the transformation plan of Crowe Jhb, of which that

has never happened during the 2020/21 financial year. The Audit Committee has recommended that they should be re-appointed as the External Auditors of AGSA.

2. The Committee noted with slight concern the report that the AGSA had seen an R293 million deficit in the current financial year. It further notes that indeed, the amount would have been much higher had it not been for the new strategies and efforts by the leadership team in leading the organisation during these difficult times. It trusts that the engagements with the Audit Committee will lead to ways and means to reduce this further for the next financial year.

3. The Committee noted that the amount owed to AG has on overall increased during the 2020/21 financial year. For the financial year, the outstanding debt amounted to R1.1 billion, Local government is the main contributor to this debt, while there is a notable growth trend of outstanding debts from SOEs. The Committee noted with concern this new trend, in particular to the fact that most SOEs are becoming financially unsustainable. This can lead to more SOEs defaulting in paying audit fees to AGSA and therefore, adding up to the challenge of outstanding debts.

4. The Committee noted that for the 2020/21 financial year, only 77 percent of ICT projects were implemented towards achieving ICT Strategy. Some of the reasons for this non-achievement of this performance target include amongst others, delay in finalisation of IT strategy, retention of ICT employees that resulted in a high turnover of employees in IT infrastructure.

5. The Committee noted and appreciates that the AGSA continues to expand its audit portfolio of 21 Schedule 2 SEOs, which are big and complex organisation. However, the Committee noted with concerns that these efforts put pressure on AGSA's resources due to a continuous need for intensive training and learning of staff after taking over.

6. The Committee further noted with concerns that AGSA experiences some resistance and pushbacks from some SOEs, when AGSA implements PAA regulations, which requires the concurrence of AG for the conditions of appointing private auditors to those SOEs, which are still not audited by AGSA.

7. The Committee has noted that despite that there were no material findings of the AGSA's audit, but there were some control gaps identified during the audit. Further, some audit findings identified remain unaddressed primarily because of inadequate capacity and capabilities within information technology, which continue to receive leadership attention and support.

7. Committee Recommendations

Flowing from the observations made by the Committee with regard to the 2020/21 Integrated Annual Report of AGSA, the Committee draws the following recommendations:

1. The Committee recommends the further appointment of the current External Auditors, but expresses its dissatisfaction with non-compliance with the request for updates to it (the Committee) on the progress of the institution's transformation plans. The Audit Committee must provide the Committee with update reports on such progress on a quarterly basis.

2. The Committee recommends that AGSA should submit mitigation plans on how it plans to correct the non-achievement of performance target: on the ICT Strategy by 31 January 2022.

3. The Committee welcomed the efforts made by the AGSA to expand its audit portfolio, to include the auditing of large and complex SOEs. In this regard, it recommends that AGSA should communicate any challenges it encounters when increasing auditing the number of large and complex SOEs. Further, the AGSA should keep the Committee abreast on the progress in implementing PAA regulations with regard to concurrence in the appointment of private auditors to those Schedule 2 SOEs, which are not audited by AGSA.

4. The AGSA should consider extending its current collection strategies to SOEs debtors. In this regard, the AG should enter into ring-fencing agreements with SOEs' debtors to ensure that they pay their outstanding debts to AGSA.

5. Given the challenge of outstanding debts to AGSA and the need for financial resources to audit the current 16 Schedule 2 SOEs which are already in AGSA's audit portfolio, it is therefore recommended to review the Funding Model of AGSA by invoking section 36 (1) (b) of the PAA.

6. The Committee recommends that the AGSA should develop an audit action plan to deal with the identified audit findings, and submit it to the Committee for monitoring its implementation.

7. The Standing Committee on the Auditor-General is satisfied with the performance of the AGSA for the 2020/21 financial year and therefore recommends that the National Assembly approves the Integrated Annual Report.

Report to be considered.