



AUDITOR-GENERAL
SOUTH AFRICA

Briefing to Portfolio Committee of Employment and Labour on the Compensation Fund

23 February 2022



Our mission and vision



OUR MISSION

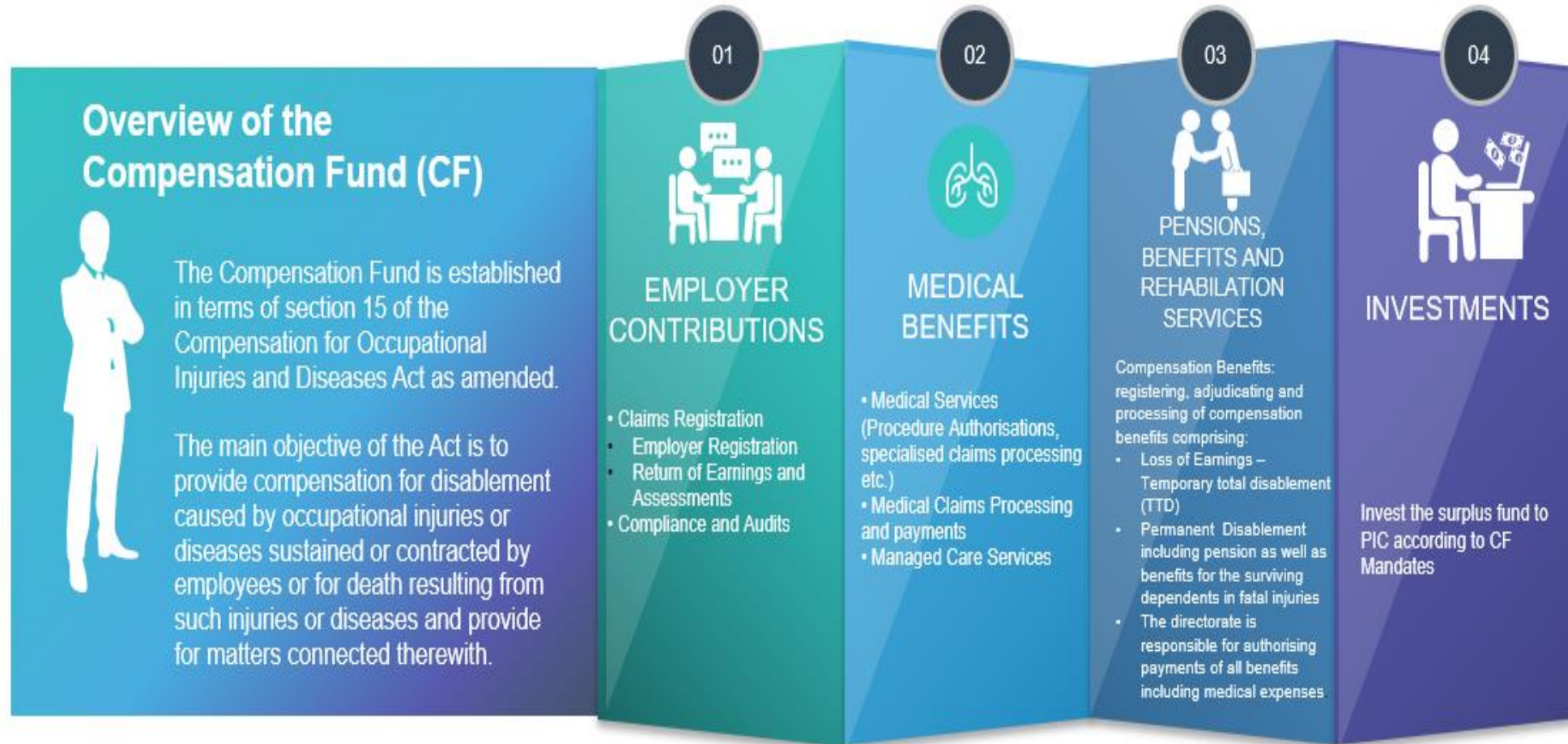
We have a constitutional mandate and, as the supreme audit institution of South Africa, exist to strengthen our country's democracy by enabling oversight, accountability and governance in the public sector through auditing, thereby building public confidence.



OUR VISION

To be recognised by all our stakeholders as a relevant supreme audit institution that enhances public sector accountability

Overview of the operations of Compensation Fund





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Audit outcomes

The AGSA expresses the following different audit opinions

Unqualified opinion with no findings (clean audit)



Auditee:

- produced credible and reliable financial statements that are free of material misstatements
- reported in a useful and reliable manner on performance as measured against predetermined objectives in the annual performance plan (APP)
- complied with key legislation in conducting their day-to-day operations to achieve their mandate

Financially unqualified opinion with findings



Auditee produced

financial statements without material misstatements or could correct the material misstatements, but struggled in one or more area to:

- align performance reports to the predetermined objectives they committed to in APPs
- set clear performance indicators and targets to measure their performance against their predetermined objectives
- report reliably on whether they achieved their performance targets
- determine the legislation that they should comply with and implement the required policies, procedures and controls to ensure compliance

Qualified opinion



Auditee:

- had the same challenges as those with unqualified opinions with findings but, in addition, they could not produce credible and reliable financial statements
- had material misstatements on specific areas in their financial statements, which could not be corrected before the financial statements were published.

Adverse opinion



Auditee:

- had the same challenges as those with qualified opinions but, in addition, they had so many material misstatements in their financial statements that we disagreed with almost all the amounts and disclosures in the financial statements

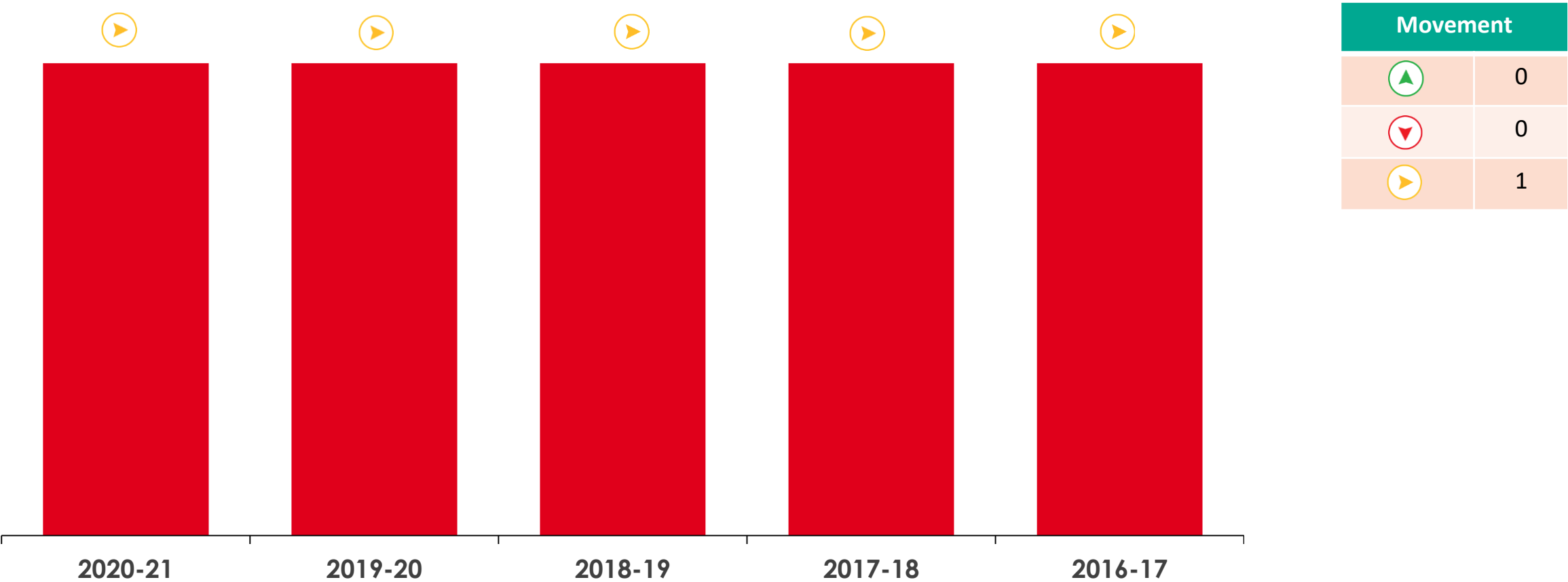
Disclaimed opinion



Auditee:

- had the same challenges as those with qualified opinions but, in addition, they could not provide us with evidence for most of the amounts and disclosures reported in the financial statements, and we were unable to conclude or express an opinion on the credibility of their financial statements

Audit outcomes of the portfolio



Audit outcomes are depicted as follows:

- Unqualified with no findings
- Unqualified with findings
- Unqualified with findings
- Adverse with findings
- Disclaimed with findings
- Outstanding audits

Compensation Fund disclaimer journey



Key qualification areas (Explanations)

REVENUE FROM NON-EXCHANGE TRANSACTIONS AND STATUTORY RECEIVABLES



The fund had inadequate process in place to ensure that employers were accurately assessed. Furthermore, the fund did not ensure that all the employers that met the criteria were assessed.

The fund incorrectly accounted for revenue from non-exchange relating to the prior year in the current year.

BENEFITS



Management did not keep adequate records to substantiate the figures recorded in the AFS.

IRREGULAR EXPENDITURE AND FRUITLESS AND WASTEFUL EXPENDITURE



Completeness of the amounts disclosed could not be confirmed due to the limitation of experience during the audit.

Sufficient and appropriate audit evidence was not provided to support the figures reported.

PAYABLES FROM NON-EXCHANGE TRANSACTIONS



Management did not maintain adequate records to support the amounts in the AFS.

PROVISION FOR OUTSTANDING CLAIMS AND CAPITALISED VALUE OF PENSION

Effective system of internal control to maintain proper accounting records and relating provision were not implemented

Compensation Fund key qualification areas

Revenue from non-exchange transactions and statutory receivables

The public entity did not correctly account for revenue from non-exchange transactions in accordance with GRAP 23, revenue from non-exchange transactions. The public entity incorrectly reversed revenue recognised in the prior year against the current year revenue from non-exchange transactions without verifying the employers who submitted returns on earnings in the current year. Furthermore, the public entity did not raise the revenue estimate for all the employers who met the criteria to be assessed in the current year. I was unable to determine the full extent of the understatement of revenue from non-exchange transactions and statutory receivables as it was impracticable to do so. Additionally, there was an impact on the surplus for the period and on the accumulated surplus.

I was also unable to obtain sufficient appropriate audit evidence for revenue from non-exchange transactions and statutory receivables for the current and prior year as the public entity had inadequate processes in place to ensure that employers were accurately assessed in terms of the Compensation for Occupational Injuries and Diseases Act of South Africa, 130 of 1993 (Coida). Management also did not maintain proper accounting records and adequate controls over revenue assessment from non-exchange transactions and statutory receivables. I was unable to confirm revenue from non-exchange transactions and statutory receivables by alternative means as the public entity's records did not permit.

1. The fund was unable to provide the underlying supporting documentation to prove that the employers that submitted returns on earnings were assessed at the correct rate and class. As the employers information submitted was insufficient to enable verification of the calculation performed by the fund.
2. The fund did not implement adequate and appropriate controls to address the completeness and accuracy of employer contributions from the employers, as some of these employers' returns of earnings (ROE's) were not assessed. The deficiencies identified included :
 - Inadequate assessment of the accuracy of information submitted by the employers.
 - Inadequate processes to ensure all employers are registered and assessed at the correct rate and class.
 - Inadequate enforcement of the act for employers not complying with the COIDA Act.
3. Furthermore, the fund did not correctly account for the revenue earned in the prior year as that revenue was incorrectly included in the current year revenue, which was in contradiction with the GRAP 23.

Compensation Fund key qualification areas (Cont...)

Benefits (related accounts – Provision for outstanding claims and the Capitalised value of pension)

I was unable to obtain sufficient appropriate audit evidence that benefits had been adequately accounted for relating to all claims in the current and prior year. Management did not keep adequate records to substantiate the figures recorded in the financial statements. I was unable to confirm benefits paid by alternative means, as the public entity's records did not permit.

1. The fund could not provide the auditors with claim data listings that agrees with the financial figures recorded in the Annual Financial Statement (AFS). This was due to inadequate records to confirm the figures reported in the financial statements.
2. Included in the benefits expenditure is the provision for outstanding claims and the capitalised value of pension. These figures are to be incorrect due to the inaccuracies in the data used to calculate the provision for the capitalised value of pension and outstanding claim. Furthermore, the actuarial experts indicated that the data provided by the fund was not suitable for the calculations performed.

Payable from non-exchange transactions

I was unable to obtain sufficient appropriate audit evidence for payables from non-exchange transactions for the current and prior year as management did not maintain adequate records to support the figures disclosed. I was unable to confirm payables from non-exchange transactions by alternative means as the public entity's records did not permit.

1. The fund could not provide supporting documents for debtors that have credit balances. Therefore, the validity of the credit balances could not be verified, and consequently, the accuracy and completeness of the related revenue cannot be verified.

Compensation Fund key qualification areas (Cont...)

Investment in associates, Investments in financial assets and associates

I was unable to obtain sufficient appropriate audit evidence for the investments in associates for the current and prior year, as management did not implement adequate internal control systems to maintain proper accounting records and supporting information. I was unable to confirm investments in associates by alternative means as the public entity's records did not permit.

1. The fund invests in various financial instruments, including investments in associates and unlisted loans. Some of the companies in which the fund invests are listed, and others are unlisted. The deficiencies below were identified in the internal control environment over the management of the unlisted investments.
 - There was insufficient and inappropriate audit evidence to validate the data used to perform the valuations of unlisted investments for the prior year.
 - Valuation reports for unlisted investments were prepared using a different accounting framework to the fund, and no adjustments were performed to ensure alignment to the funds accounting framework.
 - The fund does not have the processes in place to verify the information from associates.
 - In instances where financial information was received, the fund had still not implemented the necessary controls to ensure that the information received from the investees is accurate, complete and valid and can be relied upon for financial reporting purposes. The fund did not implement effective internal control systems to determine the accuracy, validity and completeness of the financial position, financial performance and cash flows of the investees for inclusion in the financial statements, including alignment between the applicable accounting frameworks/policies.

Compensation Fund key qualification areas (Cont...)

Prior period error

The public entity did not disclose various prior period errors in note 32 to the financial statements, as required by GRAP 3, Accounting policies, estimates and errors. Furthermore, the nature of the correction for each financial statement item affected some prior period errors, and the amount of the correction at the beginning of the earliest prior period was not disclosed. I was unable to determine the impact on the prior period errors disclosure note as it was impracticable to do so.

1. The fund did not implement adequate and appropriate controls to address the issue of non-submission, as the supporting information was not provided to verify the accuracy and completeness of the prior period error disclosure. In some instances, the fund did not correct most of the misstatements identified by the auditor in the previous years to ensure that the financial statements were correct and complete.

Contingencies

I was unable to obtain sufficient appropriate audit evidence for contingent assets, as the public entity did not implement adequate internal controls to maintain accounting records. I was unable to confirm contingent assets by alternative means as the public entity's records did not permit. Consequently, I was unable to determine whether any adjustments were necessary to contingent assets as disclosed in note 30 to the financial statements.

1. Adequate records regarding contingencies relating to securities held/ceded and notices of motions and summons were not adequately maintained. Some contingencies should have been recorded as liabilities; however, there were no processes in place for the fund to adequately identify the completeness and accuracy of the contingency balance disclosed in the annual financial statements.

Compensation Fund key qualification areas (Cont...)

Irregular and Fruitless and wasteful expenditure

I was unable to obtain sufficient appropriate audit evidence to confirm whether all irregular, fruitless, and wasteful expenditure for the prior years had been recorded, impacting the closing balance for the current year. I was unable to confirm irregular expenditure by alternative means as the public entity's records did not permit.

1. The fund did not submit supportive evidence to enable the confirmation of irregular expenditure and fruitless and wasteful expenditure resulting in limitations.
2. Furthermore, the fund did not record all instances of fruitless and wasteful expenditure identified through the investigation performed.

Cash flow statements

The public entity did not correctly prepare and disclose the net cash flows from investing activities as required by GRAP 2, Cash flow statements. This was due to multiple errors in determining cash flows from investing activities. I was not able to determine the full extent of the errors in the net cash flows from investing activities as it was impracticable to do so.

1. The fund did not accurately disclose the amounts in the cashflow statement. Differences were noted in the calculation. The cashflow statement included amounts which could not be verified as cash items. The reviews and monitoring to ensure that correct amounts, including the re-performing of the cash flow statements, were not adequately performed, resulting in these inaccuracies.

Compensation Fund key qualification areas (Cont...)

Risk Management

The public entity did not disclose risk management in accordance with GRAP 104, Financial instruments. The public entity did not disclose the asset allocations per class under the concentration risk descriptions, and the sensitivity analysis amounts and credit risk in note 34 to the financial statements were incorrectly accounted for. As a result, the risk management components were overstated.

1. The fund did not correctly allocate the asset allocation per class under risk description and sensitivity risk as required by the GRAP 104. As a result, this resulted in the misstatement on the risk management note. Furthermore, the fund did not have proper processes in place (e.g. reviewing and monitoring) to ensure that the information captured on the financial statements is accurate and complete.

Principal-Agent Relationship

The public entity did not disclose the relationship with the public investment corporation as a principal-agent relationship, as required by GRAP 109, Accounting by principal and agents. Consequently, the financial statements are not in line with the accounting standard with regard to principal-agent relationships. I have not included the omitted information in the audit report as it was impracticable to do so.

1. The fund did have adequate systems to account for the principal-Agent relationship, as disclosure notes in the financial statements. The omission of this note resulted in the financial statements being incomplete.

Related parties

I was unable to obtain sufficient appropriate evidence for the amounts disclosed as related-party balances and transactions, as the public entity did not maintain adequate records. I was unable to confirm the related-party balances and transactions by alternative means as the public entity's record did not permit. Consequently, I was unable to determine whether any adjustments were necessary to related-party balances and transactions disclosed in note 31 of the financial statements.

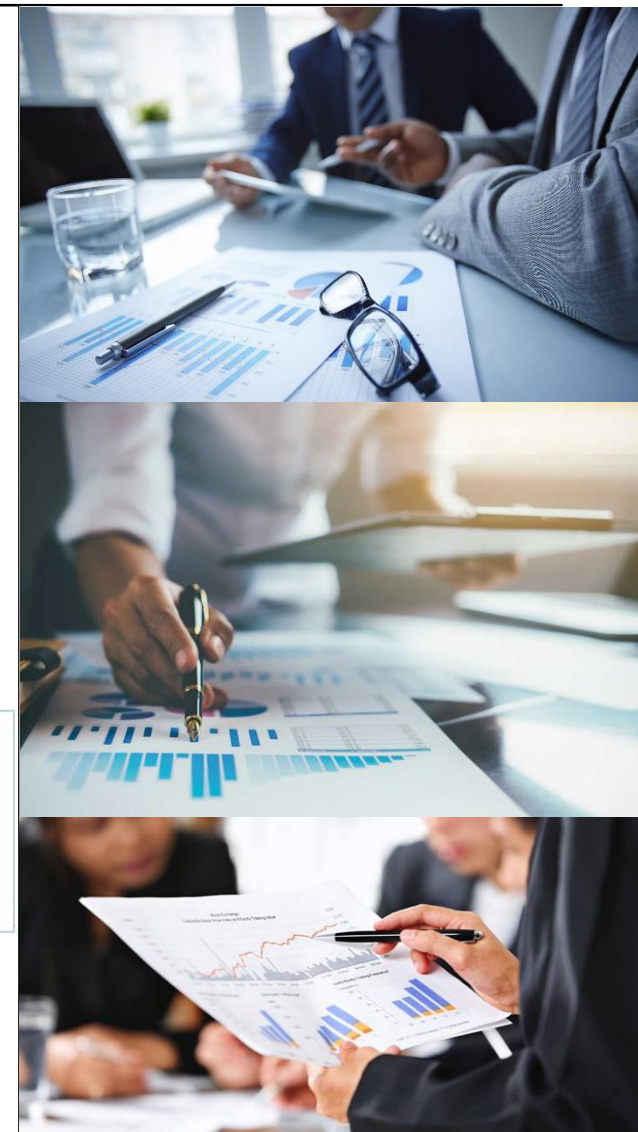
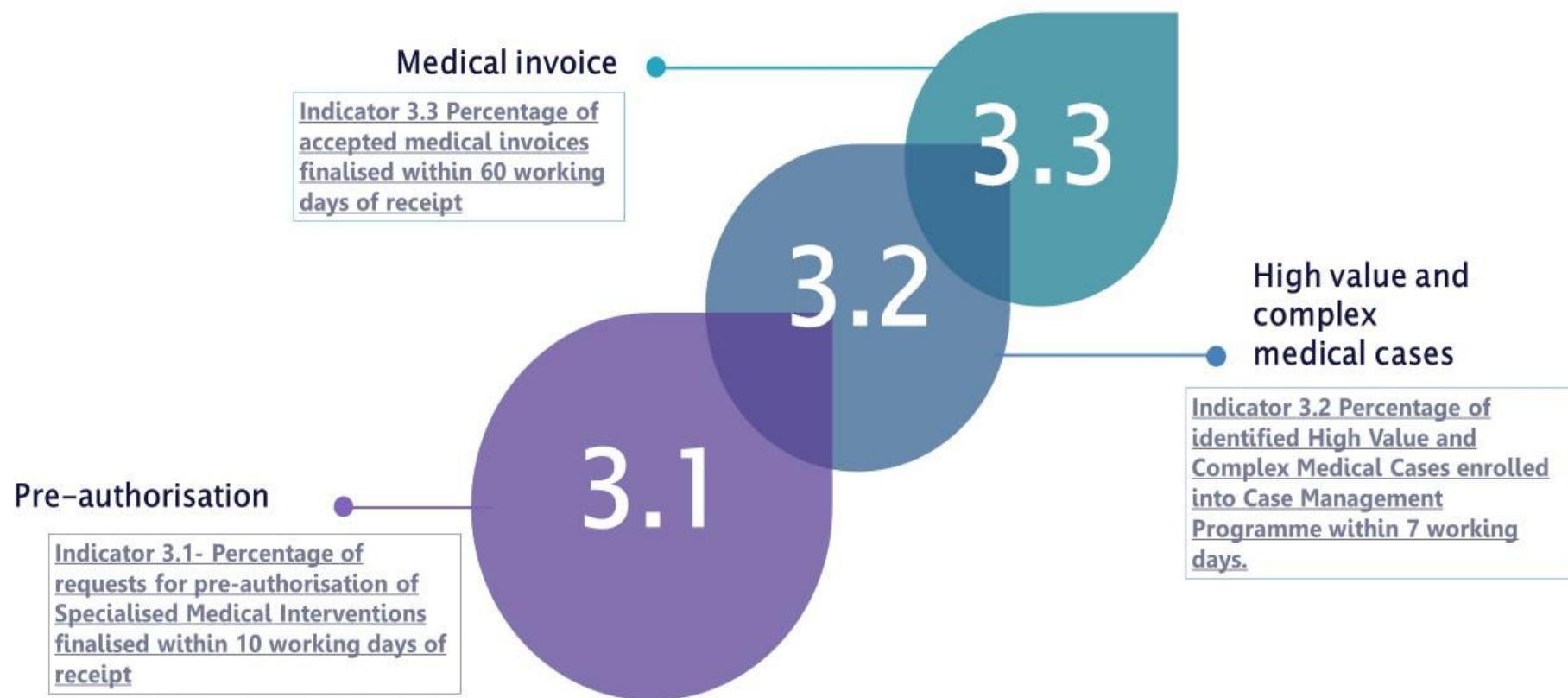
1. The fund did have adequate systems to identify and disclose all related party transactions, for example transactions with the Department of employment and labour.



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Quality of performance reporting

INDICATORS SELECTED FOR AUDIT UNDER PROGRAMME 3



Credible performance reporting (cont...)



Performance report



CF remained with uncorrected misstatements after the audit process. The findings identified on programme 3: Medical Invoice are recurring. Usefulness: The fund was able to correct the finding relating to usefulness of the submitted annual performance report.

Material findings on reliability of programme 3:

- The Fund had material uncorrected misstatements on the annual performance report due to lack of supporting documentation to support the reported achievement as well as inappropriate recording of the performance achievement, management could not correct the misstatements.
- Medical benefits were as a result of a lack of supporting evidence and accurate listing that support the performance achievement reported in the annual performance report and recording of the previous years' achievement in the current year.
- In some instances, the performance achievement was not correctly calculated, and some listing included the performance achievement related to the previous period.

Root cause analysis	Recommendations
<div><p>There is poor record keeping within the fund, not all role players are ensuring that they keep supporting documentation in order to support the targets achieved.</p></div> <div><p>Key role players, are not reviewing the reported achievements adequately to ensure that schedules are supported by evidence.</p></div>	<div><ul style="list-style-type: none">• An alignment of the reporting processes to support the reporting processes in the APR.• Management should enhance the review controls to ensure that misstatements are prevented or detected and corrected.</div> <div><ul style="list-style-type: none">• Effective performance management processes that ensures all role players attend to their duties adequately.</div>



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Compliance with legislation

Compliance with legislation

In the current year there has been a stagnation in compliance with legislation for Compensation Fund. In most instances, the non-compliance identified is similar to that reported in the prior year and the nature is as follows:



Annual financial statements: The financial statements submitted for auditing were not prepared in accordance with the prescribed financial reporting framework and supported by full and proper records. Material misstatements were identified on various accounts as detailed in section 2.1 of this briefing, and in some instances supporting evidence was not provided.



Expenditure management:
Effective and appropriate steps were not taken to prevent irregular expenditure, as required by section 51(1)(b)(ii) of the PFMA. The irregular expenditure disclosed in the financial statements was mainly caused by non-compliance with various National Treasury procurement requirements.
Effective steps were not taken to prevent fruitless and wasteful expenditure, as required by section 51(1)(b)(ii) of the PFMA. The fruitless and wasteful expenditure disclosed in the financial statements was mainly caused by interest on late payments, sheriff costs and legal costs.



Resources of the public entity were not utilised economically, as required by section 57(b) of the PFMA.
The fund incurred interest on the late payment of medical invoices, which could be avoided as such; there is non-compliance with the requirements of section 57(b) of the PFMA with regard to the economic use of resources by the public entity.



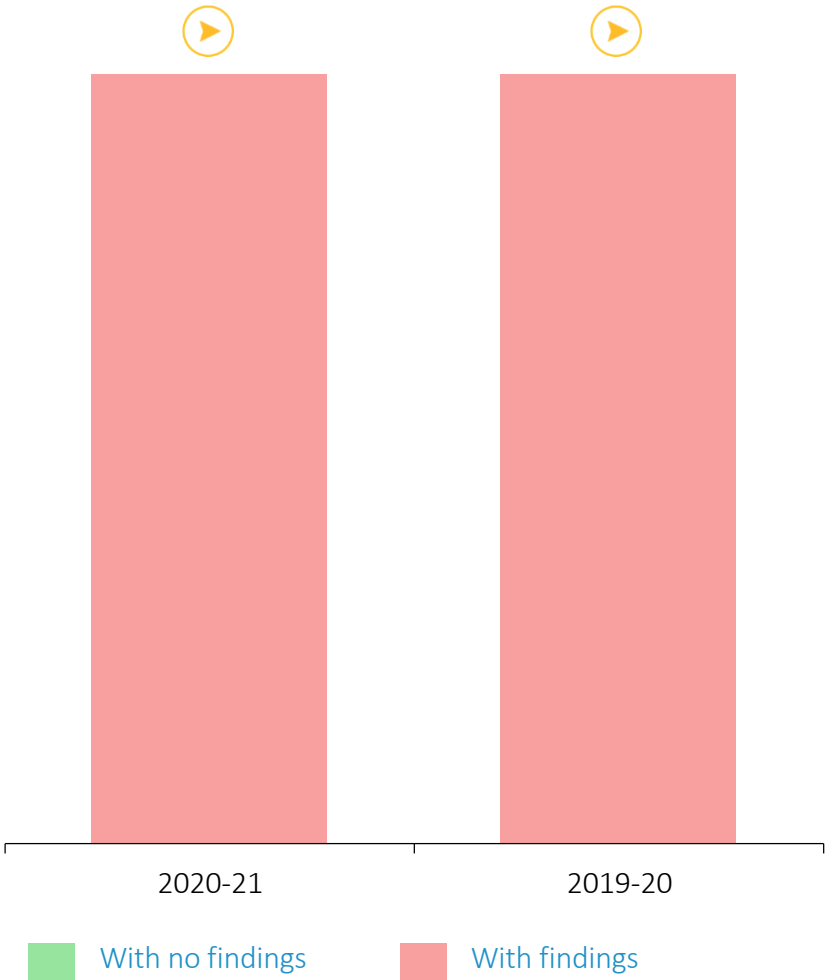
Consequence management: We could not confirm that disciplinary steps were taken for individual who permitted the irregular, fruitless and wasteful expenditure due to lack of complete and proper records to support investigations.



Revenue management: Effective and appropriate steps not taken to collect all money due and interest not charged at the approved rates.

Compensation Fund did not implement effective action plans to address significant internal control deficiencies relating compliance with legislation

Findings on compliance with key legislation

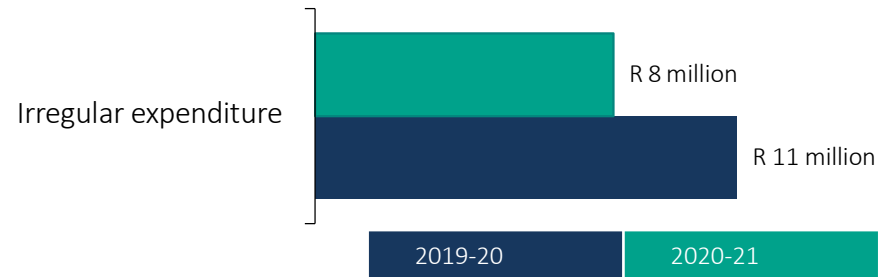


Irregular expenditure over 2 years

Definition

Expenditure incurred in contravention of key legislation; goods may have been delivered but prescribed processes not followed

Irregular expenditure incurred by the fund



- R3 million – non-compliance in 2011-12
- R5 million – non-compliance in 2020-21

Nature of irregular expenditure

Highest contributors to irregular expenditure related mainly to the non-adherence to SCM prescript and the effective monitoring thereof:



Payments exceeding the contract value were made on three [3] contracts. The total amount paid was R3 million.



R5 million relates to expenditure incurred on contract that was cancelled due to the delivery air-conditions that did not meet the requirement of the specification.

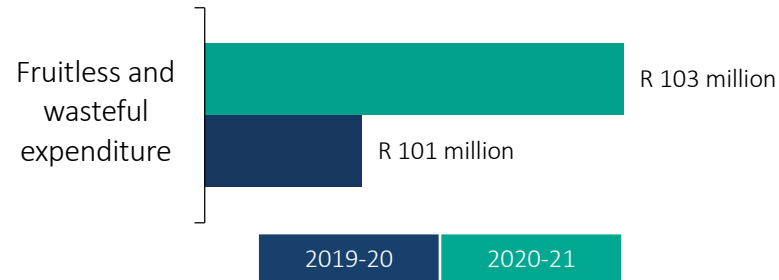
Note: We could not confirm the completeness of the Irregular expenditure, which forms part of the basis of modified opinions, furthermore Two contracts were extended without approval by the appropriate official.

Fruitless and wasteful expenditure over 2 years

Definition

Expenditure incurred in vain and that could have been avoided if reasonable steps had been taken – no value for money!

Fruitless and wasteful expenditure incurred by fund



Nature of fruitless and wasteful expenditure



The majority of the fruitless and wasteful expenditure relates interest incurred due to the Fund fail to pay the medical invoices within the stipulated timeframes.



Intercepted payments resulting in payments being made to incorrect beneficiaries.

Note: We could not confirm the completeness of the fruitless and wasteful expenditure, which forms part of the basis of modified opinions.

Consequence management



Consequence management

Overall, Compensation Fund does have processes in place to investigate and follow up on irregular expenditure and fruitless and wasteful expenditure.

However, we could not confirm whether disciplinary steps were taken at the following auditees due to lack of complete and proper records to support actions.

Below is a summary of findings we identified:

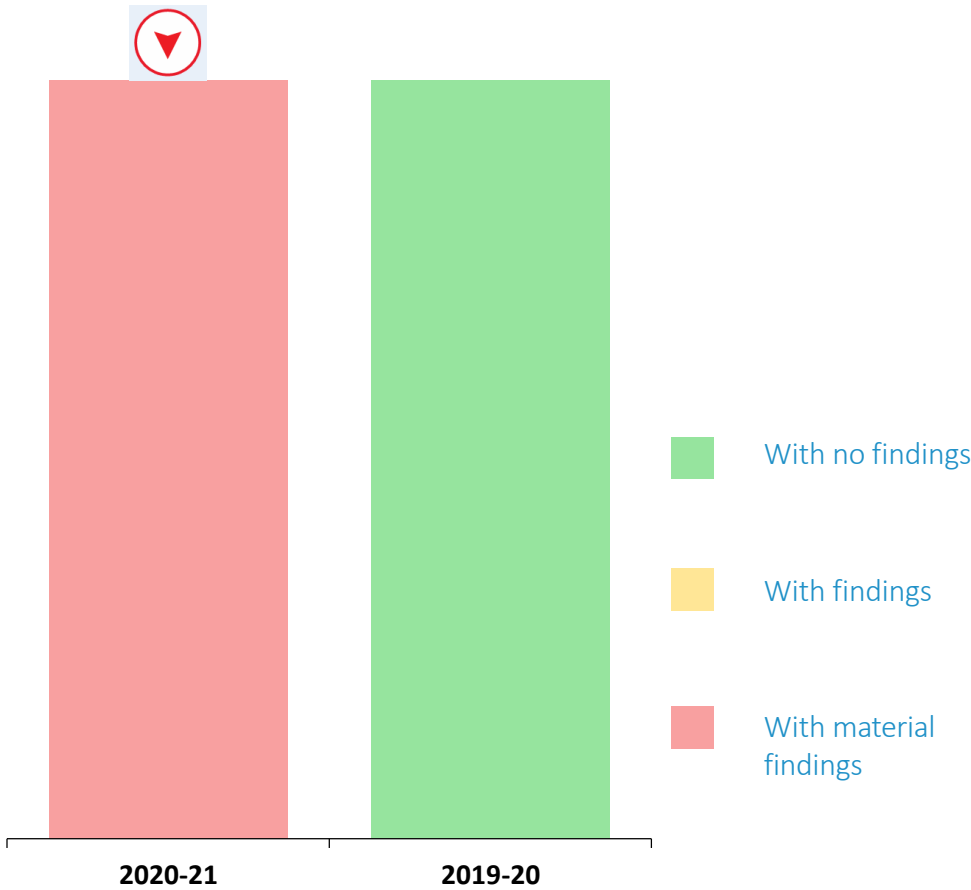
- ✓ The fund had investigations that have not been allocated to an investigator, some of which were reported more than 12 months.
- ✓ Where investigations were taking place, evidence could not be provided to substantiate the progress thereof and the outcomes.
- ✓ The fund has 31 fraud related investigations that have not been finalised as at year-end.

Recommendations

- The accounting authority must follow up on the progress made on investigations, where the process is weakened , actions must be taken to ensure that these weaknesses are remedied.
- The accounting authority must ensure that complete and proper records are kept to support the investigations that have been conducted.
- The accounting authority must ensure that appropriate action is taken, by reviewing the outcomes of these investigations against the policies of the fund.
- All the records surrounding disciplinary actions must be kept to ensure that these steps are supported.

Supply chain management

Overall regression in SCM compliance
All SCM findings should be investigated



Most common findings on supply chain management

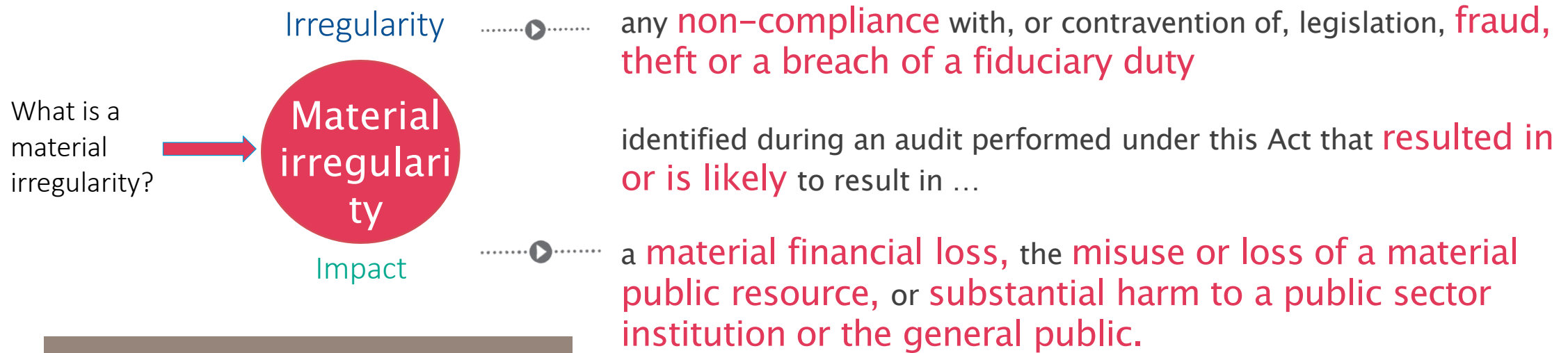
Uncompetitive or unfair procurement processes followed:

- Extension of contracts without proper approval

Recommendations

- Adequate project management must be in place, to ensure that where there are delays/or increases in costs appropriate steps are take to ensure compliance with legislation.

At the center of the PAA amendments – material irregularity



To allow for establishing capacity and processes, we followed a phased-in approach for identifying MIs in 2020-21 based on:

1. the type of material irregularity to be identified and reported
2. the auditees where it will be implemented

Selection criteria

The MI process is implemented at selected auditees audited by the AGSA that represent a significant portion of the expenditure budget and the irregular expenditure of national, provincial and local government, including state-owned entities. The selection is also focused on auditees that are key contributors to government priorities. For 2021, the Compensation Fund was selected for MI implementation in the portfolio.

MATERIAL IRREGULARITIES

NUMBER	DESCRIPTION	STATUS
<u>COMPENSATION FUND</u>		
1	<p><u>Interest, legal fees and sheriff fees charged due to the Fund not complying with the court order relating to payment of invoices submitted by a service provider.</u></p> <p>The fund failed to make payment of the medical invoices within the 75 days, as per order of the court. Consequently, CompSol instituted further legal action against the Fund in an attempt to obtain settlement of its medial invoices. As a result the Fund incurred additional costs in the form of interest on late payments of the medical invoices</p> <p>The Fund did not comply with section 51(a)(i) of the PFMA as it states that an accounting authority for a public entity must ensure that that public entity has and maintains effective, efficient and transparent systems of financial and risk management and internal control.</p>	<p>The accounting authority committed to ensuring that the investigation is finalised by the end of the financial year 31 March 2022.</p> <p>We will follow up on the implementation of the actions during the next audit cycle.</p>
2	<p><u>Duplicate payment made to medical claims beneficiaries.</u></p> <p>Overpayments were made to a medical service provider through Umehluko system due to ineffective (inadequate) internal controls. The Fund did not comply with Section 51(1)(a)(i) of the PFMA that states an accounting authority for a public entity must ensure that that public entity has and maintains effective, efficient and transparent systems of financial and risk management and internal control.</p>	



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Governance and internal controls



Internal control deficiencies



The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the audit opinion as well as the material findings on performance information and compliance with legislation.

Leadership responsibility over financial and performance reporting

- The leadership did not ensure that effective preventative and detective controls were in place to enable reliable reporting and compliance with legislation.*
- Preventative controls such as ensuring that there are efficient and effective processes in place to prepare financial statements and performance reports appropriately.*

Action plans to address internal control deficiencies

- Action plans to improve audit outcomes were not adequately implemented and monitored to ensure effective implementation of the corrective. As a result, there were recurring findings.*
- In some instances, these action plans were not addressing the root causes.*

Proper record-keeping

- The leadership did not implement adequate proper record keeping to ensure that complete, relevant and accurate information was accessible and available in a timely manner to support financial and performance reporting.*



Internal control deficiencies (continued)

Regular, accurate and complete financial and performance reports

- *Management did not prepare regular, accurate, and complete financial statements supported by reliable and credible information due to inadequate review of the financial statements, performance reporting, and compliance with legislation. This resulted in material misstatement being identified during the audit.*

Daily and monthly processing and reconciling of transactions

- *Management did not implement adequate controls relating to daily and monthly processing and reconciliation. The controls that management put in place to ensure regular, accurate, and complete financial reports did not always prevent and/or detect material misstatements in annual financial statements and annual performance reports.*

Compliance monitoring

- *The leadership did not adequately review and monitor compliance with applicable laws and regulations, which resulted in instances of non-compliance being identified during the audit.*

Internal audit and audit committee

- *The audit committee and internal audit functions have not been effective, as the funds management often submitted the information required late or not at all. Furthermore, there was no audit committee for a part of the financial year.*





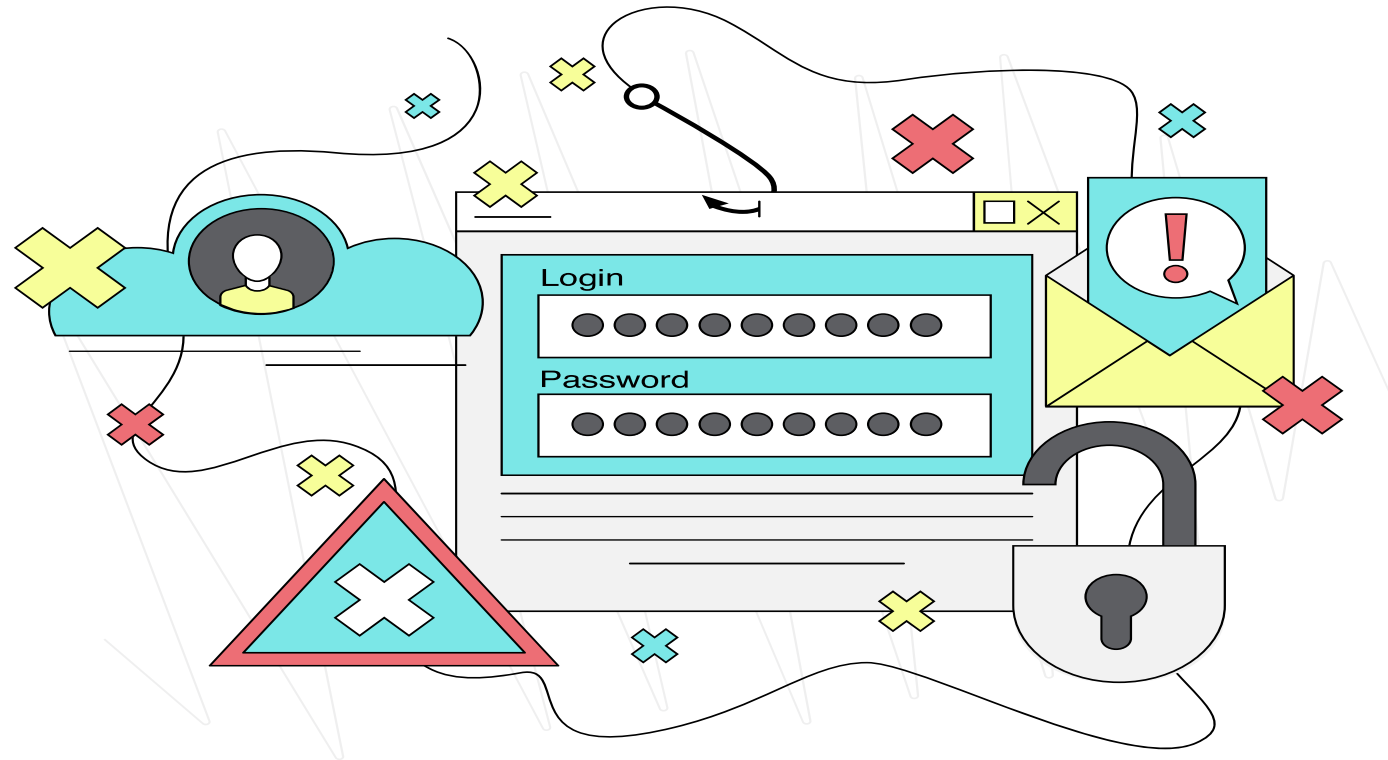
Status of information technology (IT) environment

IT Governance

- Project Objectives as per Business Case still has outstanding deliverables.
- CompEasy User Acceptance Testing Sign-off not completed.

IT service continuity (ITSC)

Lack of disaster recovery plan at DEL, impacting disaster recovery plans and efforts for both the department and its entities.



Recommendations

- Management should develop the disaster recovery plan in line with the overall Business Continuity Plan for the Department and its Entities.
- System administration management should not grant users and consultants, not part of the authorisation function, any of the above transactions and access revoke where inappropriately assigned.
- Management should implement measures that ensure that access to these critical functionalities is restricted.
- Management should investigate the list of users whose activities are not segregated and implement appropriate measures to resolve this discrepancy.
- Management should monitor and track access to the user accounts and ensure access is appropriately restricted and controlled.

Security Management

Some weaknesses were identified over security management.

- SAP S4i and ECC6 basis and related functionality assigned to users who are not part of the basis team.
- Significant network security weaknesses at DEL and the entities.

User Account Management

Some weaknesses were identified over user account management. Eg,

- Segregation of duties and conflicts on the SAP ECC6 system.
- Users with access to sensitive transactions in the SAP S4i system must be controlled and reviewed.

Program change management

- There were users with inappropriate with access to insert codes into queries in SAP ECC6 production.
- Users inappropriately assigned development related functions in SAP S4i production.
- There were no user acceptance testing sign-off and change advisory board approval for some changes implemented in SAP S4i.



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Recommendations



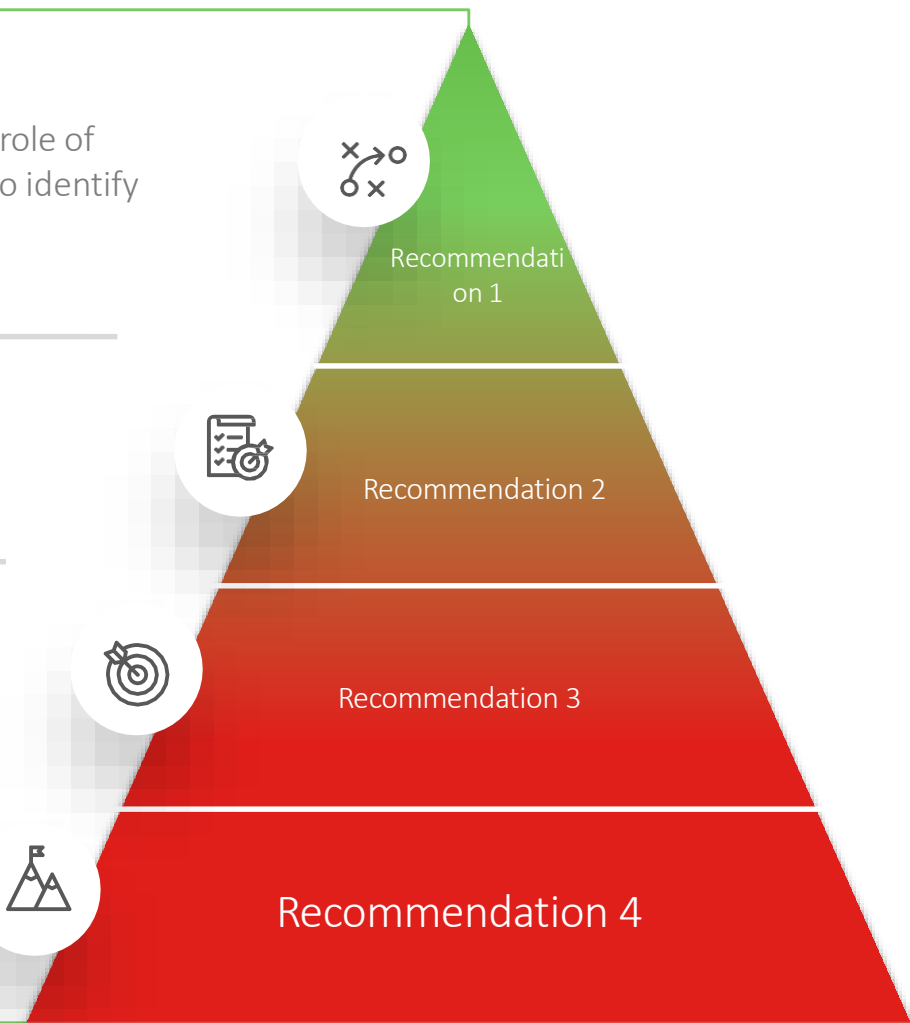
Recommendations to the Compensation Fund

There is **still an urgent need to review the control environment** of the fund including the role of management and subsequently strengthen the preventative and monitoring controls, to identify deficiencies early and react appropriately.

Monitoring of the **adherence to controls** must be enforced proactively and where there is transgressions actions must be taken and the root causes identified must be responded to timeously.

Implement **regular and adequate review controls** over financial and performance reporting to ensure that errors are timeously detected and corrected.

Consequence management should be implemented and monitored on transgressions.



Recommendation to the committee

Recommendation to the committee

Obtain a report detailing the progress made by the Compensation fund on the review of the control environment of the fund.

The committee should obtain all the investigation reports from the fund and confirm that:

- ❖ The investigations have been adequately conducted,
- ❖ The root causes are addressed,
- ❖ Employees that caused the irregularities are identified and action is taken against them.

Recommendation to the committee

Where the fund has incurred a financial loss that loss is recovered

Monitor that consequence management is implemented to transgressors.

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