AUDITOR-GENERAL
SOUTH AFRICA

Briefing to SCOPA
SAA

4 May 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

Mandate for the AGSA and SCOPA

AGSA mandate

Constitution section 188

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

PAA section 20(2)

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

Section 5(1B)

- Auditor-General has the power :
  - to take an appropriate remedial action
  - where an accounting officer/authority has failed to comply with remedial action, to issue a certificate of debt, as prescribed.

Standing Committee on Public Accounts (Rule 243)

Must consider…

- the financial statements of all executive organs of state and constitutional institutions or other public bodies when those statements are submitted to Parliament,
- any audit reports issued on those statements,
- any reports issued by the AG on the affairs of any executive organ of state
- any reports reviewing expenditure of public funds by any executive organ of state and constitutional institution or other public body
- any other financial statements or reports referred to the committee in terms of these rules

The committee may….

- report on any of those financial statements or reports to the Assembly
- **may initiate any investigation in its area of competence**

Background and overall message

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Background

The objective of this presentation is to brief the SCoPA on audit outcome of SAA for 17/18 and to provide an update on the outstanding audits.

In 2019, SAA financial difficulties resulted in then board requesting suspension of the audit as they wanted to focus on finding solutions to address liquidity and solvency challenges. At the time of withdrawing the audit team, **the audit for 2017-18 was incomplete as we were waiting final board approved financial statements**.

The board then adopted a resolution to place SAA under **business rescue on 5 December 2019**, as per section 129 of Companies Act. SAA exited business rescue on **30 April 2021** when the practitioners filed a notice of substantial implementation of the BR plan.

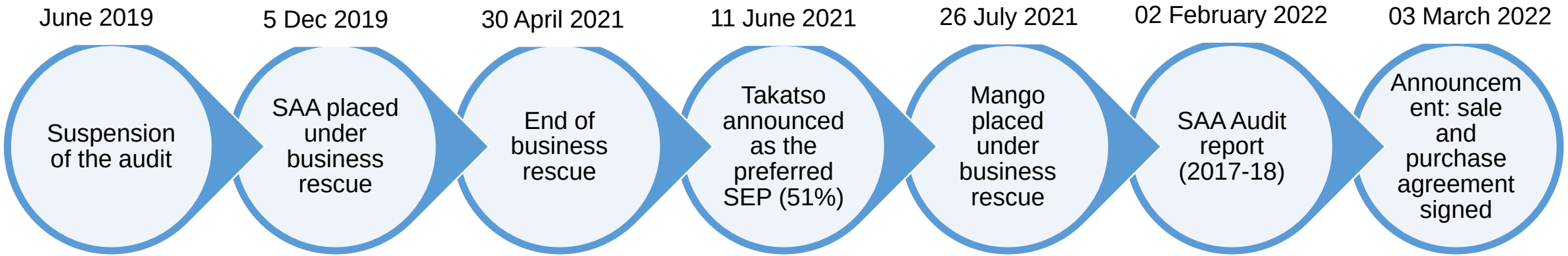
Subsequent to this, we engaged management and the board and finalized outstanding audit for 2017/18 on **2 February 2022**. The audit opinion was qualified and outcomes are summarized in this presentation.

We are busy engaging SAA as well as other stakeholders to start the remaining audits for the financial years **2018-19, 2019-20, 2020-21 and 2021-22**.

Once the sale of 51% controlling stake of SAA is finalised and the sale agreement is shared, we will be able to understand the partnership between government and the controlling shareholders (Takatso Consortium) as well as:

- the **type of entity** from being 100% state-owned to privately controlled entity;
- the **role of government** (the DPE) in managing and overseeing the 49% minority stake;
- the **role of the AGSA**; and
- The oversight **role of parliament**.

Timeline of key events and the future of SAA



Strategic Equity partnership: 51% stake sold to Takatso Consortium

- Sale and purchase agreement has been signed. The only outstanding steps are the regulatory approvals.
- Once the transaction is finalised, SAA will cease to be a majority state-owned entity.
- Government will only have a minority stake – therefore, will not be treated like a public entity in the context of the PFMA.
- The sale transaction includes all subsidiaries except Mango. This means that from the transaction date, Mango will no longer be a subsidiary of SAA and will be a stand-alone entity.
- Mango is also going through a process of identifying a strategic equity private partner that will own a controlling stake.

Material irregularities, State Capture Commission report and consequence management

SAA group has been earmarked for implementation of the AGSA expanded mandate in relation to MIs

However, as the audits are still outstanding – no matter has been identified for material irregularity yet.

The report by the state capture commission of enquiry highlighted a number of irregularities which require further actions by the board of SAA and law enforcement agencies.

This further highlighted the importance of consequence management to ensure appropriate accountability for irregularities that took place when the entity was under the control of the state.

In this regard, the approach to consequence management will need to take into account the following implications of the sale of the controlling stake:

- The PFMA will no longer apply to SAA;
- Irregular expenditure and fruitless and wasteful expenditure will no longer need to be disclosed;

Therefore, our approach of material irregularity and any recommendation for consequence management will need to be done in a manner that will capacitate those charged with governance to ensure continued consequence management even when the company is no longer under the control of the state.

SAA audit outcomes

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AGSA audit outcomes

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

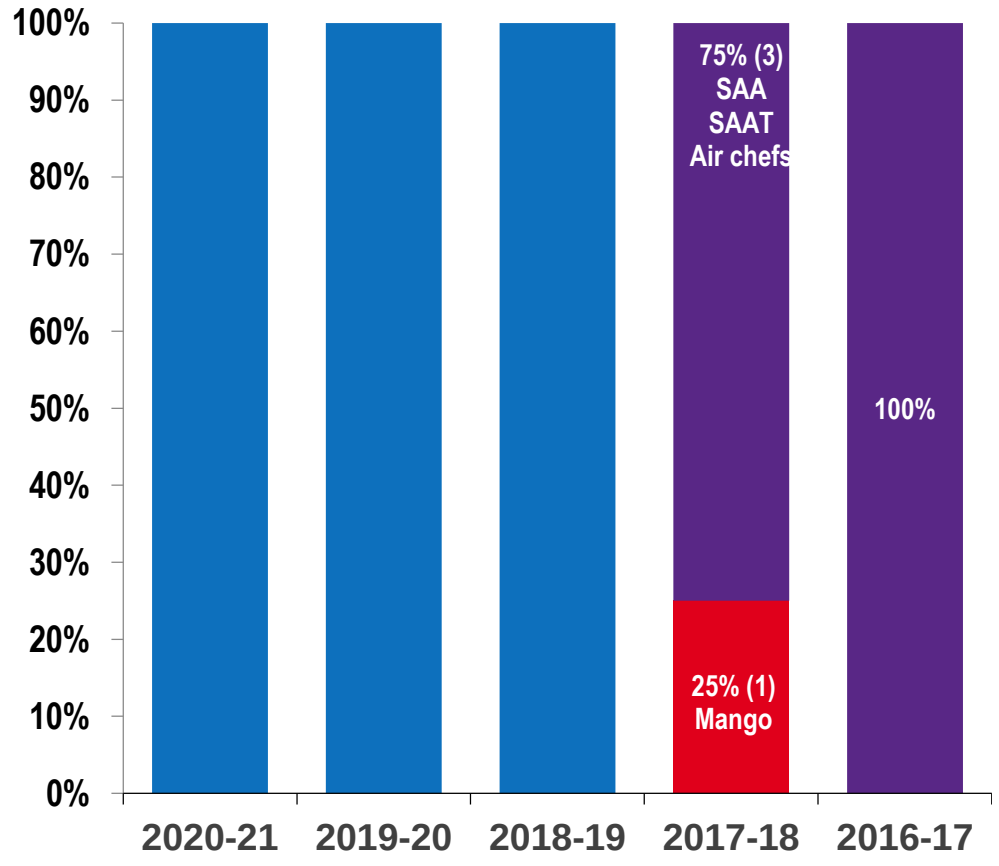
The AG's annual audits examine:

1. Fair presentation and absence of significant misstatements in **financial statements**
2. Reliable and credible **performance information** for predetermined objectives
3. **Compliance with laws and regulations** governing financial matters

Movement over the previous year is depicted as follows:

- ▲ Improved
- ▶ Unchanged
- ▼ Regressed

Audit outcomes for 2017/18 financial year



These audit outcome are for the period up to 31 March 2018. The audits for 2018-19, 2019-20 and 2020-21 are outstanding due to non-submission of AFS.

- The overall audit outcome of South African Airways SOC Ltd (SAA) remained stagnant with a qualified audit opinion with findings on predetermined objectives and compliance with legislation. Mango airline regressed to a disclaimer due to the lack of evidence to support the going concern assumptions.

- SAA was audited by the AGSA for the first time in 2016-17 and the 2017-18 financial year was our second year performing the audit. There was an increase in significant findings raised on the financial statements, compliance with legislation as well as in areas of supply chain management (SCM).

For the outstanding audits:

- We are engaging with SAA management to agree on key actions and deliverables in support of the audit process, including commitment on the submission of financial statements for all outstanding years.

Audit outcomes are depicted as follows:	Unqualified with no findings	Unqualified with findings	Qualified with findings	Adverse with findings	Disclaimed with findings	Outstanding audits

Areas of qualification and non-compliance with legislation

The areas of qualification are as follows:

- **Property, plant and equipment**: Review of the useful lives and residual values of property, plant and equipment at each reporting date in accordance with IAS 16.
- Completeness of **irregular expenditure**;
- Completeness of **fruitless and wasteful expenditure**;
- Limitation of scope on **trade and other payables**;
- Limitation of scope on **inventory**;
- Limitation of scope on **maintenance costs**;
- Limitation of scope on **intangible assets**;
- Understatement and incorrect valuation of **trade and other receivables**;
- Limitation of scope on **taxation and deferred tax**;
- Limitation of scope on **related parties**;
- Indequate assessment for impairment of **investment in subsidiaries**;
- Limitation of scope on commitments.

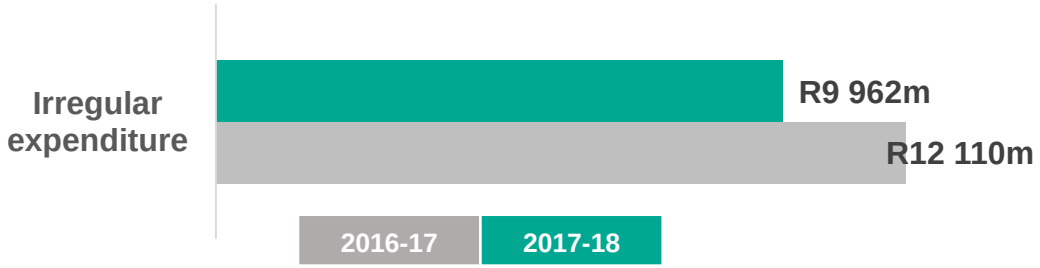
The areas of material non-compliance reported are:

- Late submission of financial statements for auditing;
- Material misstatements identified in financial statements submitted for auditing;
- Proper control systems to safeguard and maintain assets were not implemented;
- Financial assistance to its subsidiaries in contravention of s45 of the Co. Act;
- Quarterly reports were not submitted to the executive authority;
- Ineffective steps to prevent irregular expenditure;
- Ineffective steps to prevent fruitless and wasteful expenditure
- Uncompetitive and unfair procurement processes;
- Inadequate consequence management.

Irregular expenditure and Fruitless and wasteful 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 SAA



Closing balance at 31/3/18 = R22bn

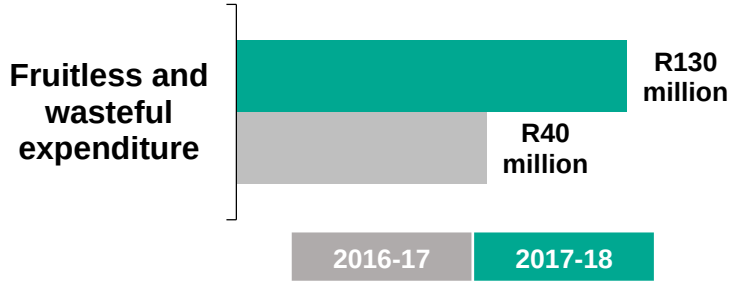
The 2016-17 AFS disclosed irregular expenditure incurred of R126 million. This figure was restated by an increase of R11.9 billion. This was as a result of the audit process identifying more historical irregular expenditure.

The majority of the irregular spend incurred to date was due to expired contracts or no contracts in place, as well as procuring without complying with the Supply Chain Management policy

*As per the qualification paragraph, **this figure is incomplete** and the true extent of the irregular expenditure has not been determined by management.*

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 SAA



Closing balance at 31/3/18 = R24.8m

*As per the qualification paragraph, **this figure is incomplete** and the true extent of the fruitless and wasteful expenditure has not been determined by management.*

Consequence management: R12,9 million of historical expenditure was recovered from responsible persons (employees and service providers).

Root causes and recommendations

Key root causes in internal control environment

- Instability and vacancies in key positions within SAA and in particular at executive management level contributed to the weak control environment.
- Inadequate controls to prevent non-compliance with procurement legislation and related weaknesses in consequence management.
- Management did not effectively develop and monitor implementation of remedial action plans
- Inadequate basic financial management disciplines and adherence to good controls exacerbated by instability in system used to collate financial information.
- Lack of review of annual financial statements and performance reports to ensure that they are reliable and supported by sufficient and appropriate information.
- Lack of timely submission of information for audit purposes.

Recommendations:

- A lot has changed in the entity since the 2017-18 financial year. The board and management should assess this outcome and determine the areas of concern (in the context of the current circumstances), ensure an effective action plan is developed to ensure it addresses root causes
- In preparing the outstanding financial statements for the financial years 2018-19 to 2021-22, the accounting authority and management should take note of the weaknesses highlighted in the 2017-18 report and strengthen controls to ensure credible financial statements are submitted for auditing.
- A more realistic action plan must be developed which takes into account the extent of work required to address prior year material misstatements in the financial statements.

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