



**PFMA
2021-22**

Budgetary review and recommendations report

Portfolio committee on Public Enterprises

October 2022



AUDITOR-GENERAL
SOUTH AFRICA



MISSION

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

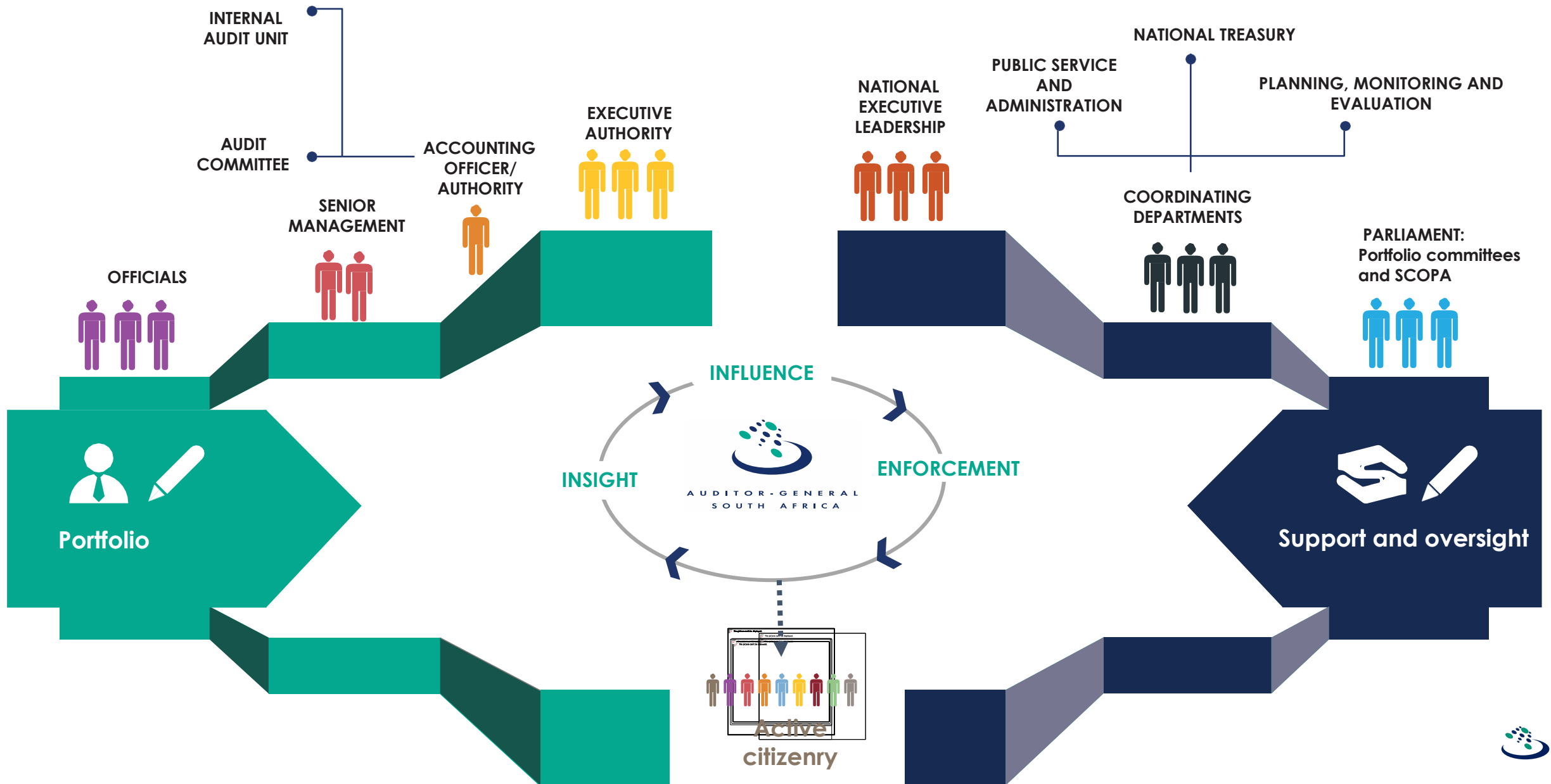


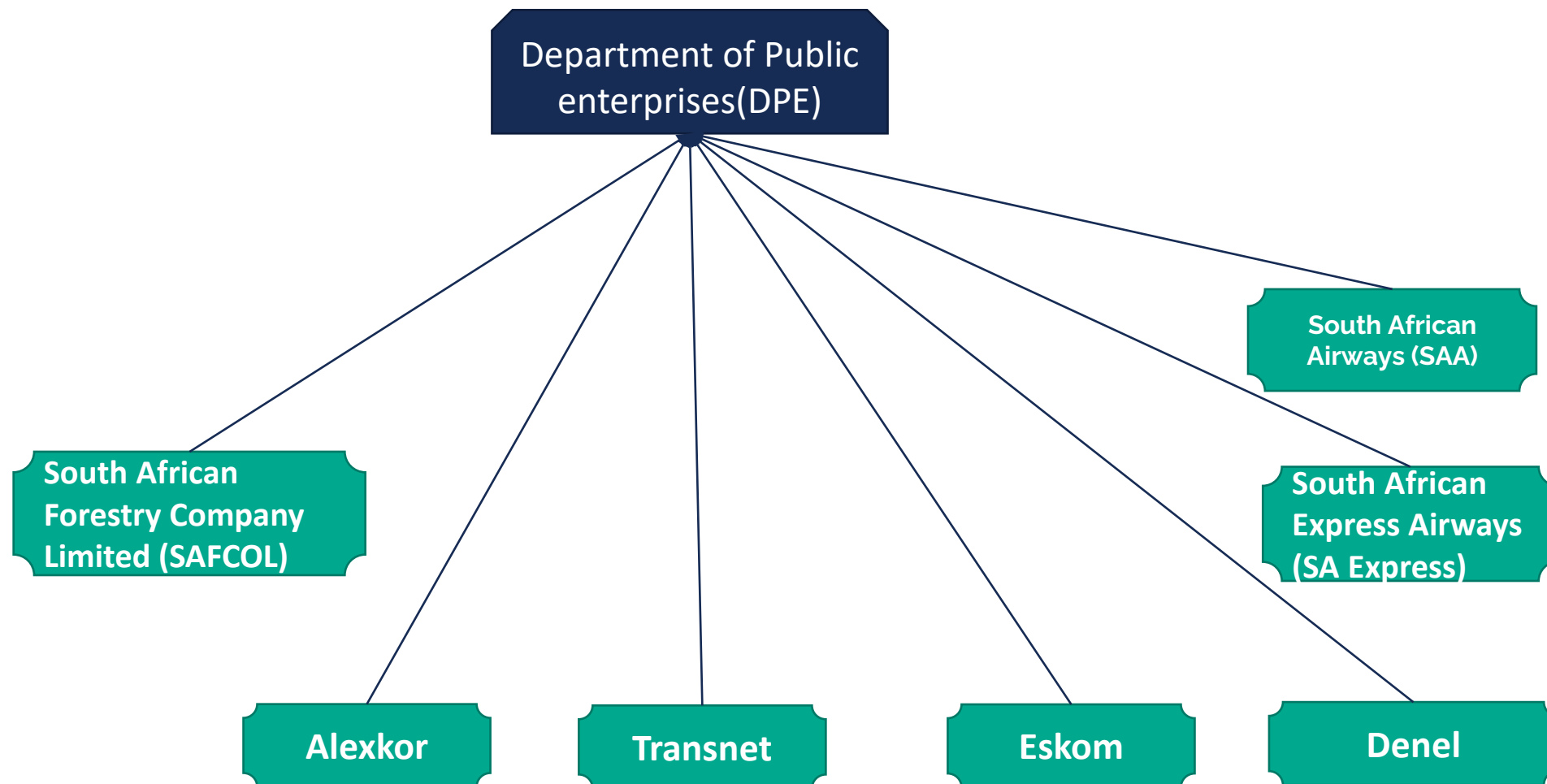
VISION

“To be recognised by all our stakeholders as a relevant Supreme Audit Institution (SAI) that enhances public sector accountability.”

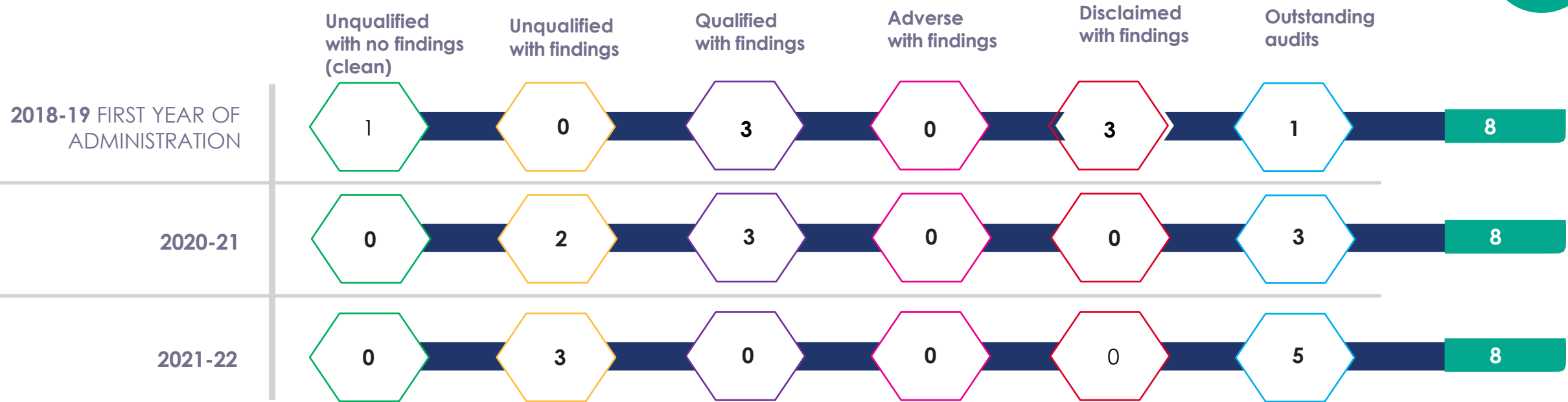


All have role to play in national government accountability eco-system





Movement in audit outcome over administration term



MOVEMENTS FROM PREVIOUS YEAR:
 1 ↑ 0 ↓

FROM FIRST YEAR OF ADMINISTRATION:
 3 ↑ 1 ↓

- 2018-19
- DPE

- 2020-21
- DPE
 - SAFCOL
- 2021-22
- DPE
 - Transnet
 - SAFCOL

- 2018-19
- Transnet
 - SAFCOL
 - Eskom
- 2020-21
- Transnet
 - Eskom
 - Alexkor

None

- 2018-19
- Denel
 - Alexkor
 - SA Express

- 2018-19
- SAA
- 2020-21
- SAA;
 - SA Express
 - Denel
- 2021-22
- SAA
 - SA Express
 - Denel
 - Eskom 21/22
 - Alexkor



South African Airways (SAA):

- The audit of SAA and subsidiaries have been outstanding since 2018-19 due to business rescue proceedings. The AFS for the past four years have been recently submitted and the audits have commenced.

South African Express Airways (SAX):

- AFS not submitted for three financial years, The entity has been liquidated.

Denel:

- AFS for the past two years not submitted due to financial and operational challenges. The entity has committed to submit 2020-21 AFS by 30 November 2022.
- The entity is currently in contravention of the PFMA and the Companies Act having failed to submit financial statements for auditing for two consecutive financial years.

Eskom :

- The audit is delayed as a result of various issues including, late submission of information and adjustments of misstatements identified during the audit.

Alexkor

- Prior year audit was signed-off late in March 2022. There were also delays with the reappointment of the auditors.

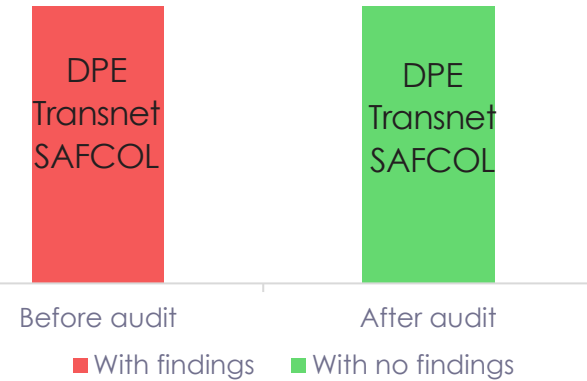


Portfolio performance



Performance against targets

Quality of performance reports before and after audit



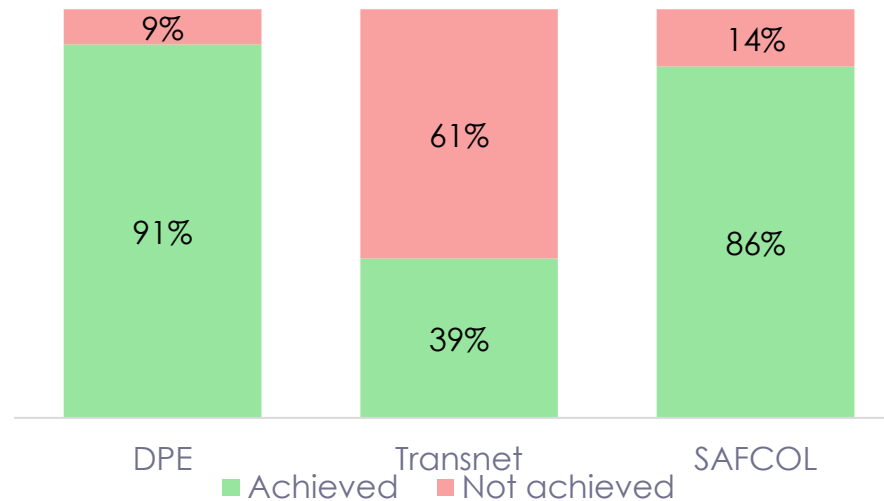
Findings corrected:

Misstatements identified on the APR submitted for auditing were corrected.

Key targets in medium-term strategic framework for DPE portfolio

- 1. Intervention:** Repurpose SOEs, strengthen governance systems and ensure board stability
 - Target: Annual scorecard on the repurposing of SOEs by the end of 2021
 - Target: Main infrastructure SOEs repurposed by March 2022
- 2. Intervention:** Separation and unbundling of Eskom to eliminate cross- subsidisation and improve efficiency
 - Target: transmission company established – Legal separation completed by 2022-23
- 3. Intervention:** Reduce costs for priority sectors by increasing the efficiency of ports –
 - Target: Transnet National Ports Authority Corporatisation completed by March 2022/23.

Achievement of annual targets as reported in annual performance report (all indicators) – 2021-22



Key MTSF targets not achieved:

The DPE performance targets did not include targets relating to the repurposing of SOEs.



Achieving key performance targets – summarised information from performance report

Performance indicator	Target	Actual performance	Reason for non-achievement
Transnet: Total rail volumes	208,83Mt	173,1Mt	<p>Operational challenges that affected Transnet include the increase in security related incidents mainly cable theft and vandalism of rail and pipeline infrastructure, IT security challenges and KZN unrest largely impacted Port and Rail operations, tippler challenges at PE, the availability and reliability of locomotives also the decline in the condition of rail infrastructure</p> <p>The highest number of trains that were planned for the year were cancelled due to security incidents which contributed to over 4000 train cancellations.</p>
SAFCOL: Timbadola Reinvestment project	Approved Execution Plan	Execution plan not approved	<p>The target was not achieved due to the refocus in implementation strategy based on the feasibility.</p> <p>Business case and a Position Paper recommending a feasible implementation option.</p> <p>The new strategy no longer considers a strategic partner that was meant to deliver funding and technical solution together with the Execution Plan. The company will instead seek funding.</p>





DPE

The DPE embarked on a process to sell 51% of its shares to strategic equity partner. While the transaction is not yet finalised, the AGSA reviewed the process followed and the agreement signed with the SEP to determine impact on the DPE financial statements and identify risks facing government.

Overall observation

1. The purchase and sale agreement requires more than R3bn to be paid by DPE to complete implementation of the BR plan. Funds to cover this liability have not been appropriated in the budget.
2. The department did not follow a formal process for the invitation, evaluation and adjudication of proposals from interested parties to identify the success/ preferred strategic equity partner.
 - No public invite for bids or expressions of interests.
 - No evidence that proposals were fairly evaluated based on a pre-determined criteria.
3. The valuation report that was used to determine the transaction value was not timeously provided.

Impact

- The sale is part of the department's strategic goal to resuscitate the SAA. Should the sale transaction not be properly processed, it may result into further losses to the state or delays in making the entity fully operational. It is important to ensure that the transaction are advantageous to the state.

Cause

- There are no clear legislative provisions for the disposal of SOEs, SOE non-core assets or SEP transactions – to ensure that the process & terms are beneficial to the state.
- The DPE does not have a policy that regulates the disposal of shares in SOEs.

Recommendations

There is an urgent need to develop clear regulatory framework for SEP transactions as government has plans to engage in more of these transactions.



Material irregularities



The material irregularity (MI) process was implemented at the following auditees

- Transnet
- SAFCOL

means any **non-compliance** with, or **contravention** of, legislation, fraud, theft or a **breach of a fiduciary duty** identified during an audit performed under the Public Audit 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**



Material irregularities identified



Transnet & SAFCOL

Notified	Type	MI description	Status of MI	Status description
04-August 2021	Transnet: Financial Loss	Contracts for the lease of heavy duty plant and equipment awarded to bidder(s) that did not score the highest points-Non-compliance with section 2(1)(f) of the PPPFA and PPR 11(2)	The accounting authority responded to the MI and appropriate action is being taken	Disciplinary process in progress.
04-August 2021	Transnet: Financial Loss	Contract amounts exceed the tendered prices for the lease of heavy duty plant and equipment-Non-compliance with section 2(1)(f) of the PPPFA and PPR 11(2)	The accounting authority responded to the MI and appropriate action is being taken	Disciplinary process in progress.
18 August 2021	KLF (SAFCOL) Financial loss: Subsidiary	Penalty paid for underestimation of provisional tax	MI under investigation	Investigation report received – currently assessing the outcome of the investigation to determine appropriate steps.

Observations from MI process

- Transnet MIs are taking longer to finalise because some of the implicated employees have disputed the allegations against them and are lodging an appeal on the disciplinary process.

Recommendations for portfolio committee

- The committee may continue to perform oversight over the implementation of commitment made by AO/AA in resolving MI's.

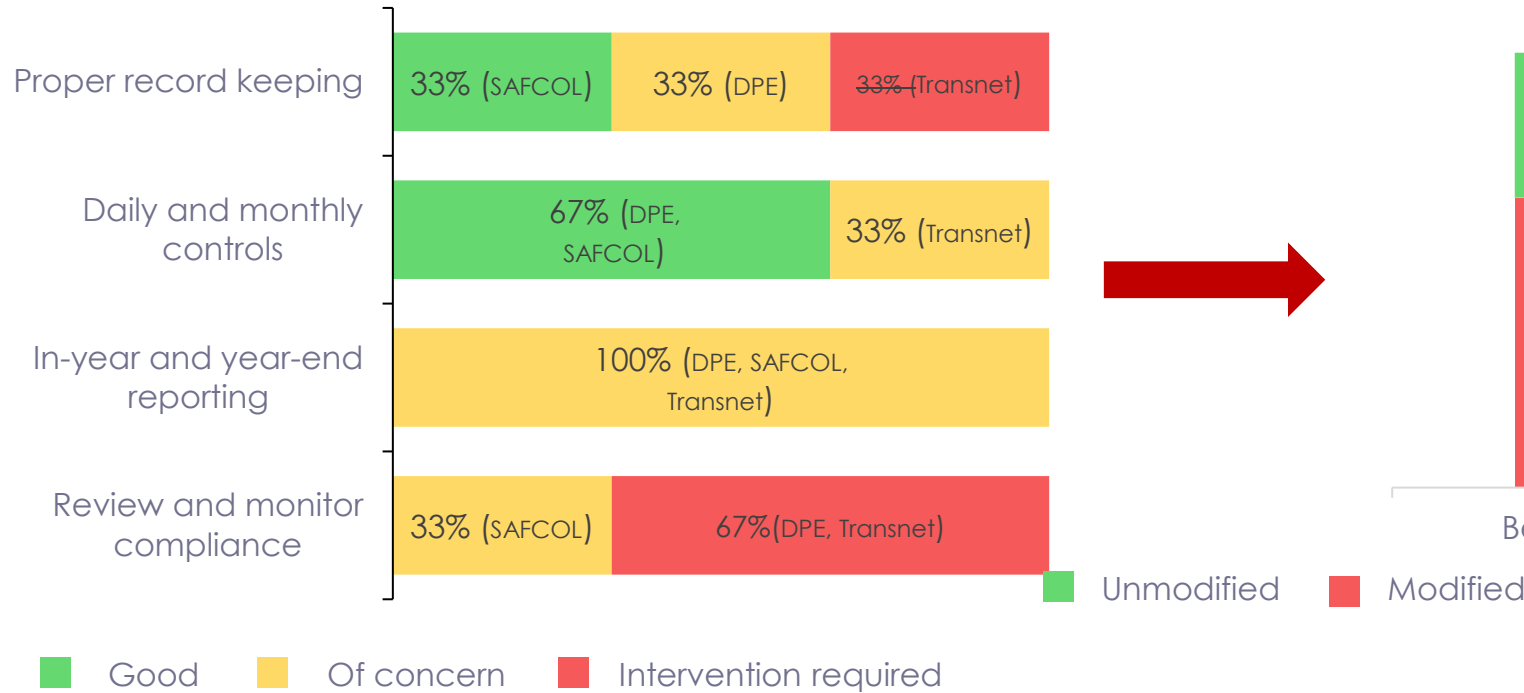




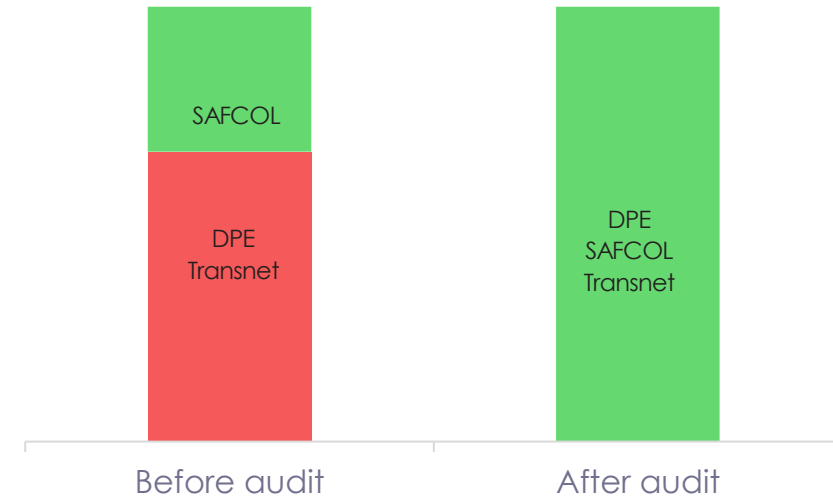
**Financial management
and compliance**



Financial management controls

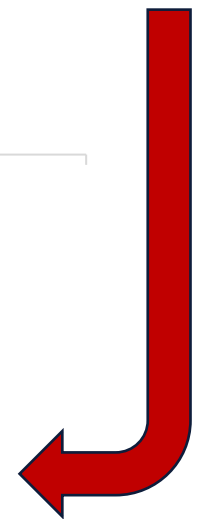


Impact on quality or financial statements submitted for audit



Material adjustments which could lead to a qualification

- Completeness of contingent liabilities (DPE)
- Investment Properties(Fair value adjustments) (Transnet)
- Related Party transactions (Transnet)
- Commitments (Transnet)



Denel

- The DPE has reported that it is working with Denel to implement a long-term turn-around plan which requires restructuring. However, it appears that there are no clear plans to address the immediate liquidity requirements of the entity.
- As a result, Denel faced a number of court challenges during the year from employees and suppliers seeking to recover money owed to them. This is also the root-cause for the R15.2 million unauthorised expenditure incurred by the DPE resulting from an unbudgeted transfer made to Denel to settle claims by suppliers.

SA Express (liquidated)

- The airline was formed to PROMOTE frequency of services on lower-density routes and EXPAND regional air services capability in South Africa,
- Its liquidation left a gap that is yet to be filled in the market it served.

Mango Airlines (a subsidiary of SAA)

- The company is currently grounded and undergoing business rescue. This has left a gap in the low-cost traveller market which is currently under-served.

Government reforms

Government has indicated that the future of state-owned companies is under consideration by the Presidential State-Owned Enterprises Council (PSEC) and their continued existence will be informed by the value they create and whether they can be run as sustainable entities without bailouts from the fiscus.

However, there is slow progress in the implementation of key reforms. e.g. shareholder management Bill, funding criteria for SOE, etc.

This creates policy uncertainty in the SOE environment with SOE struggling to deliver on their mandates (e.g. Denel)





2021-22



● No material findings ● Material findings

Transnet, SAFCOL and DPE



Most common areas of non-compliance

	DPE	TRANSNET	SAFCOL
Procurement and contract management	X	X	
Quality of financial statements	X	X	
Prevention of irregular, unauthorised, and fruitless and wasteful expenditure		X	
Effecting consequences		X	X



Status of compliance with legislation on procurement and contract management

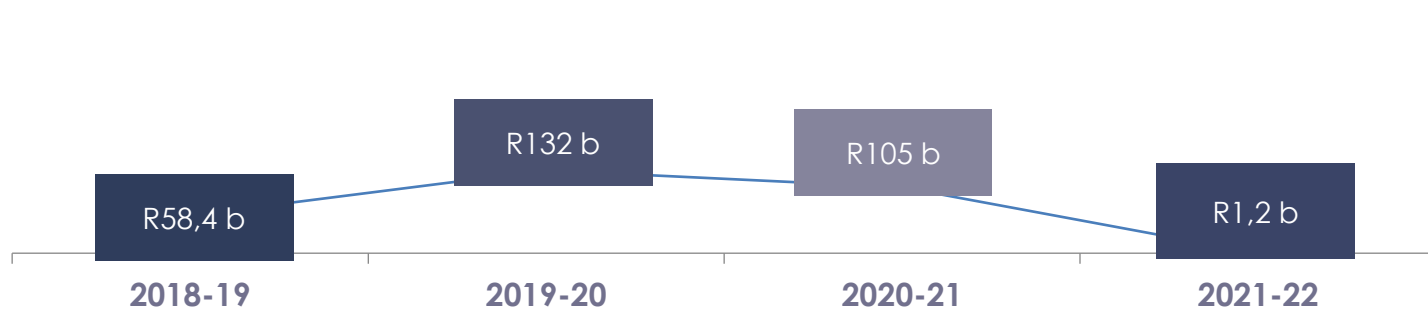


● With no findings
 ● With findings
 ● With material findings

Details of procurement findings	DPE	Transnet	SAFCOL
Uncompetitive and unfair procurement processes	X	X	
Awards to family/partner/associate		R1 m	
Prohibited awards to other state officials			
Limitations on audit of awards selected for testing		R243 m	



Annual irregular expenditure



Top contributors 2021-22



Impact assessment of irregular expenditure incurred

Breach of five pillars of procurement – Equitable, Fairness, Cost effectiveness, Transparency and Competitiveness: (DPE) R2,065m (Deficiencies in the appointment of a service provider)

Other: (DPE) R0,972 m, SAFCOL R59 667 000

*Transnet IE was not disclosed in the AFS due to the exemption from section 55(2)(b)(i)(ii) & (iii) of the PFMA granted by the Minister of Finance to Transnet on 31 March 2022 for a period of three (3) years. This figure was disclosed in the annual report and it is therefore not audited



Conclusions and recommendations



Overall root causes of significant findings in portfolio

- Leadership did not adequately exercise oversight responsibility over financial, performance reporting and compliance with applicable laws and regulations. (DPE)
- Senior management did not prepare regular, accurate and complete financial and performance information, which resulted to the material adjustments on the financial statements and performance report. (DPE and Transnet)(
- Senior management did not adequately review and monitor compliance with applicable legislation, this resulted in the department incurring unauthorised and irregular expenditure. (DPE, Transnet and SAFCOL)

Key recommendations to and commitments by Accounting officers and authorities

- Controls over preparation of financial and performance information at the divisions level needs to be enhanced. The daily and monthly reconciliation review processes need to be emphasised at management division level to ensure errors are detected and corrected .
- Mechanisms to monitor compliance with applicable laws and regulations needs to be revised to ensure their adequacy as non-compliance remain prevalent in the department and state own entities.

Commitments by Executive Authority

- XXXXXX
- XXXXXX
- XXXXXX



Monitor and regularly follow up with the executive authority and accounting officer on:

- There is an urgent need to finalise and implement the SOE reforms that have been announced by government – including the shareholder management Bill and SOE funding criteria.
 - This will ensure policy certainty and empower SOEs to delivery on their developmental mandates.
- The DPE's annual performance plan must be aligned to the MTSF targets of strengthen governance systems and ensure board stability.
 - Key indicators and targets for the department must include outcome/output based indicators which will see improvement of SOCs from year to year.
- Failure to submit financial statements is a contravention of the PFMA and the Companies Act. This further obstruct accountability and oversight processes.
 - Decisive actions be taken against the SOC's that failed to submit Financial statement.



THANK YOU



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