SCOAG ENGAGEMENT : FUNDING MODEL

OF THE AUDITOR-GENERAL SOUTH AFRICA

2023-24

#CultureShift 2030

AUDITOR-GENERAL
SOUTH AFRICA

MISSION

The Auditor-General of South Africa has a constitutional mandate and, as the supreme audit institution of South Africa, exists to strengthen our country's democracy by enabling oversight, accountability and governance in the public sector through auditing, thereby building public confidence

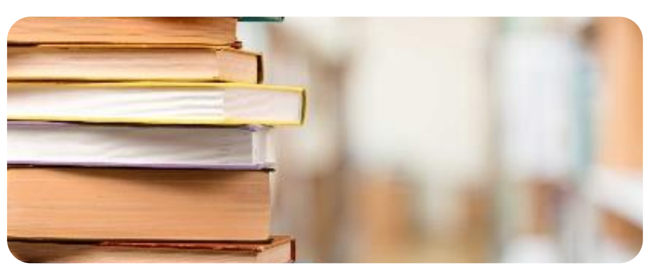
VISION

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

The funding model of AGSA is premised on the organisation being commercially viable and financially independent. We are currently reviewing our funding model in line with #CultureShift strategy and to respond to the current macro economic environment challenges.

We have a backlog of technological investments and to achieve the aspirations of the #Cultureshift strategy, we need to scale up in the implementation of digital transformation programmes and automation of certain processes both in audit and support function. This will require funding.

We intend to utilize the reserves of R4,2 million in our balance sheet to fund the performance audits. Going forward, a portion of the retained surplus will be used to fund some performance audits and the balance to be utilised on capital projects.



Our challenge is that the surpluses are still tied in debtors and have not materialized into cash. Some of these auditees especially state owned entities and municipalities are in financial distress.

Negotiations are currently taking place with National Treasury to fund the implementation of the material irregularities through appropriation. We are also exploring ways of how the MIU can be funded as part of the funding model.

FUNDING MODEL

	Comments
The AGSA as a self-funded organisation, charges fees based on the services performed. The funding of the AGSA are stated in section 36(1) of the PAA. The funds of the Auditor General consist of money—	
• earned as fees for audits or services performed by the Auditor General in terms of this Act or any other legislation;	In practice
• appropriated by Parliament for the purposes of the Auditor General;	In practice
• earned on investments;	In practice
• obtained by the alienation or letting of movable or immovable property;	AGSA does not have property yet
• accruing to the Auditor General from any other source; and	The AGSA does not have any other source of income
• otherwise becoming available to the Auditor General.	N/A
The **Auditor General may accept a donation or bequest, provided that it will not result in a conflict of interest**. All donations or bequests must be disclosed in the annual report of the Auditor General, and all material donations or bequests must be itemised	The funding model has been enhanced to make provision or mechanism for the AGSA to allow donations subject to due diligence and necessary approval

Self funding

Section 36(1)(a) services rendered – we sell time and charge clients

Section 36(1)(b) allows for appropriation of funds e.g. funding of PAA implementation

The AGSA does not receive government grants, to secures its financial & legal independence

Tariffs

Tariffs are based on average direct staff costs per band and interval, mark-up factor per band and recoverable hours per band

(direct staff cost x mark-up factor ÷ recoverable hours)

Recoverable hours are audit hours spent on audit projects and billed to the auditee

Mark-up factor

The mark-up is applied on our internal resources

(direct cost).

No profit on revenue generated on outsourced audits and subsistence and accommodation (S&T)

The mark-up factor is enough to recover the direct cost and to fund the day-to-day operations of the organisation (overheads)

Surplus

Surplus = 1% - 4%

Capital expenditure

(e.g. notebooks, office furniture)

&

Other initiatives

FUNDING MODEL CONSIDERATION

- In line with the culture shift strategy, we are currently reviewing our funding model to consider pricing our services based on the value of insights (messages) we provide to our auditees and other stakeholders, instead of salaries and volume of recovered hours.
- The organisation is driving a strategy to improve operational processes, technology & audit methodology with the aim to improve audit efficiencies i.e. leverage on technology by automating our business processes and audit process,
- The investment in technology will result in a move in cost structure from human aspect to technology. This will not translate into hours and rates as technology will eliminate the mundane tasks that are done by people by automating our processes.
- Whilst our funding model has been financially sound to fund operations and minor capex projects in the past, it has however been unable to fund major capex projects.
- The reviewed funding model will be shared with ScoAG for consideration and approval once it has been finalised.

OVERVIEW OF THE DEBT BOOK

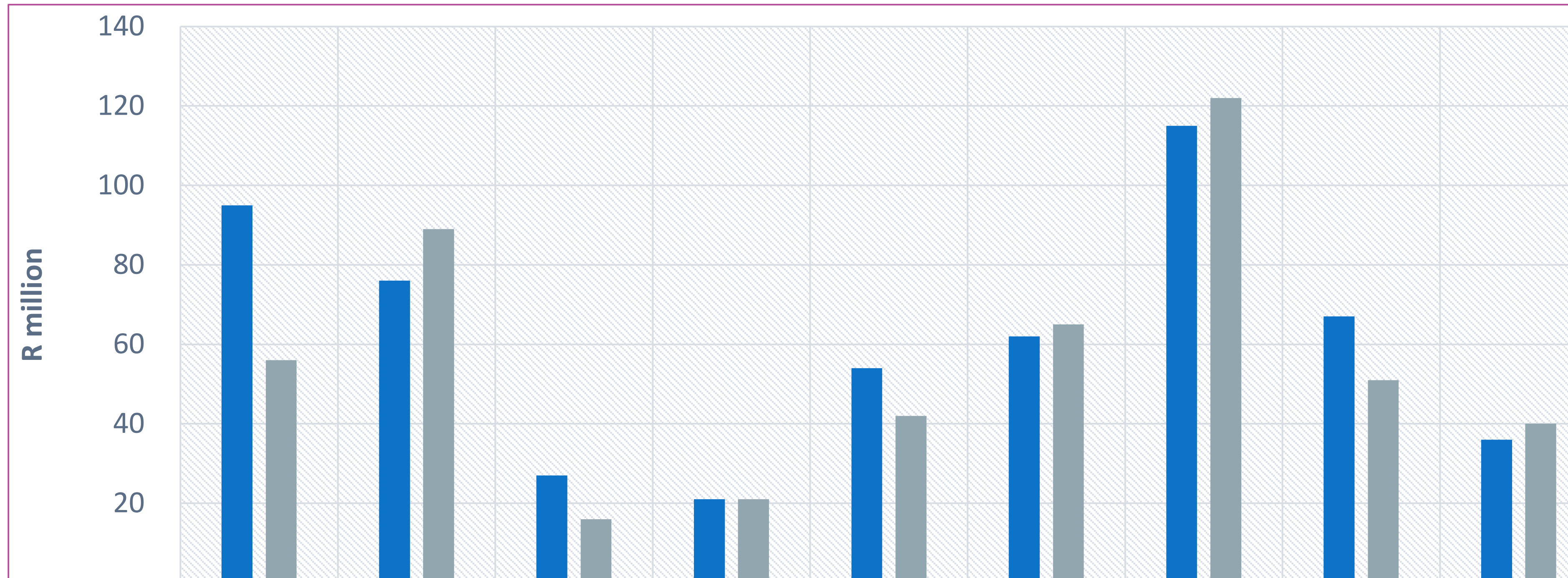
		Current - 30 days	60 days	90 days	120 days	120'+ days	31-Mar-23	31-Mar-22
		R million						
Nationals	7%	76	3	0	0	0	79	71
Provincial	13%	139	3	0	0	5	148	127
Local government	45%	86	28	46	93	249	502	553
Statutory	6%	33	1	0	1	28	64	56
State owned/public entity	29%	157	9	2	3	144	315	292
Total	**100%**	**491**	**44**	**49**	**97**	**426**	**1 107**	**1 098**
% of total		*44%*	*4%*	*4%*	*9%*	*38%*		

- The outstanding debt balance as at 31 March is **R1 107 million (March 2022: R1 098million)**. 45% or R502 million of this debt is owed by the **local government sphere (local and district municipalities)** whilst 29% or R315 million is owed by **schedule 3 & 4 entities (SOCs/entities).** Of the debt book, R523 million or 47% is owed for 120 days or more, mainly by the auditees in financial distress.

- Our auditees are given 30 days to settle their debt through normal collection. In the even that some auditees experience financial challenges, the AGSA offer **settlement arrangements (ring-fencing)** that can be tailor made and suite the need of the organisation as well as the auditee to catch up on their long-outstanding debt. As the last resort, **litigation is used to collect from those delinquent auditees in** line with the PAA.

- The debt owed by state owned entities is **R184 million or 17%** of the debt book. The collection challenges in this category are mainly concentrated from the outstanding debt owed by **Denel group (R70 million), SAPO R30 million and SAA express R16 million**.

- The local government debt is R502 million (March 2022: R553 million) or 45% of the debt book. The collection challenges in this category are mainly concentrated from the outstanding debt owed by Northern Cape, Eastern Cape, Free State ad North West. Majority of the municipalities are in financial distress and based in impoverished locations with low income generation. These four provinces make up R230 million or 45% of the local government debt (2022: R415 million or 81%).
- During the past financial years, the NT has supported the AGSA's financial independence and viability through ad-hoc settlements of outstanding 1% audit fees. In addition, NT provided an additional allocation of R70 million in 2021-22 and R76 million in to settle the cumulative short-falls arising from the prior years.
- It is important to note is that with effect from 1 April 2023, the AGSA will receive a full allocation of the 1% from the National Revenue Fund. The projected amount will increase from an average of R72 million to R123 million per annum. The 100% payment plan comes after numerous engagements between AGSA, National Treasury and the support from SCOAG.
- The above demonstrate the continued respect and support for the mandate and work of the AGSA and is acknowledged with great appreciation.



	BUEC	BUFS	BUGT	BUKZN	BULIM	BUMPL	BUNCP	BUNW	BUWC
2021-22	95	76	27	21	54	62	115	67	36
2022-23	56	89	16	21	42	65	122	51	40

R'million	2020-21	2021-22	2022-23	Projected 2023-24
Opening balance	-	51	30	0
1% invoiced to NT	121	120	118	123
Total invoice + opening balance	***121***	***171***	***148***	***123***
Total collections	***70***	***141***	***148***	***123***
Collection as per NT allocation	*70*	*71*	*72*	123
Additional collection		*70*	*76*	
Outstanding	**51**	**30**	**-**	**-**

OUTSTANDING DEBT OWED BY STATE OWNED ENTITIES

DEBTORS	Total debt	Current - 30 days	60 days	90 days	120 days	120'+ days
		R million				
STATE OWNED COMPANIES/ ENTITIES						
DENEL Group	70	1	1	1	1	66
South African Post Office	30	7	1	0	1	21
Transnet	28	20	5	2	0	1
South African Express Airways SOC Ltd	16	0	0	0	0	16
Pelchem SOC Ltd	8	0	0	0	0	8
PetroSA SOC Ltd	8	3	1	0	0	4
Autopax Passenger Services (Pty) Ltd	4	0	0	0	0	4
Mango Airlines SOC Limited	5	4	0	0	0	1
South African Airways SOC	6	5	1	0	0	0
The South African Nuclear Energy Corpora	1	0	0	0	0	1
Passenger Rail Agency of SA	5	3	2	0	0	0
Eskom Holdings SOC Ltd	0	0	0	0	0	0
DBSA	3	2	1	0	0	0
TOTAL STATE OWNED COMPANIES/ ENTITIES	**184**	**45**	**12**	**3**	**2**	**122**

- The debt owed by state owned entities is R184 million or 58% of the debt owed by public entities (R315 million). Of these auditees, R169 million or 93% is owed by auditees in default as shown in the table.
- The debt owed by state owned entities is R184 million or 58% of the debt owed by public entities (R315 million), Some of the auditees with significant debt are Denel (R70 million), SAPO (R30 million), Transnet (R28 million), South African Express Airways (R16 million), Pelchem (R8 million) and PetroSA (R8 million).
- Attempts to provide these auditees with opportunities to catch up with their payments through ring-fencing arrangements are beginning to yield results even though we have not yet achieved the desired level of collections. Below is the progress thus far:
  - SAPO paid R7,6 million in March 2023 to reduce its debt book. No payment received in April 2023.
  - Denel paid R18 million in March 2023 and R8 million in April 2023 and have committed to pay R8 million per month until the total debt is liquidated.
  - Pelchem is settling their debt through ring-fencing agreement.

WORK ON MATERIAL IRREGULARITIES

	2021-22 Actual	2022-23 Actual	2023-24 Projections	2024-25 Projections
		R million		
Material irregularity unit *(including technical support on MI)*	*77*	82	87	91
Loss of revenue *Portion of the MI work done on audit files which was not billed to auditees*	26	28	30	32
Total PAA cost	***104***	**110**	**117**	**124**

We are exploring options to fund MI process as part of the funding model. We are also relooking at building capacity of the MIU to support the delivery of the MI's.

2021-22 MFMA – MI Impact

2018-19: 9 auditees → 6 MIs
2019-20: 57 auditees → 96 MIs
2020-21: 94 auditees → 185 MIs
2021-22: 170 auditees → 268 MIs

268 MIs on **non-compliance and fraud,** resulting in:

195 Material **financial loss** (estimated R5,19bn)

- **Payments** for goods and services not received
- Unfair, uncompetitive or uneconomical **procurement**
- Ineffective use of financial reporting **consultants**
- **Value for money** not received
- **Revenue** not billed or not recovered
- Interest and penalties **on late or non-payments**
- **Asset and investment** losses

44 Substantial **harm to public sector institutions**

- Repeated **disclaimers**
- **Non-submission** of financial statements

29 Substantial **harm to general public**

- Pollution of water resources
- Poor **landfill site management**

From **INACTION** to **ACTION**

No actions were taken to address **87%** of matters until we issued notifications

MI is resolved only when all possible steps have been taken to:

- Recover financial losses or remove/address harm caused
- Implement consequences
- Prevent any further losses and harm

Status of 182 active and assessed MIs*

29	16%	**Resolved MI**
103	57%	**Appropriate action taken to resolve MI**
50	27%	**No appropriate action taken** – invoked our powers

ACTIONS TAKEN BY **AUDITEES**

- **R150,55m** Financial loss **recovered**
- **R18,85m** Financial loss **prevented** from taking place
- **R310,16m** Financial loss **in process of being recovered**
- **46** **Internal controls improved** to prevent recurrence
- **58** Responsible officials identified and **disciplinary process** completed or in process
- **14** **Fraud/criminal investigations** instituted
- **1** **Supplier contracts stopped** where money is being lost
- **15** **Outstanding financial statements** submitted

Status of 124 active and assessed MIs

- Resolved MI — 14 (11%)
- Appropriate action being taken to resolve MI — 91 (74%)
- No appropriate action taken – invoked our powers — 19 (15%)

FROM INACTION TO ACTION

179 material irregularities on **non-compliance and fraud** resulting in:

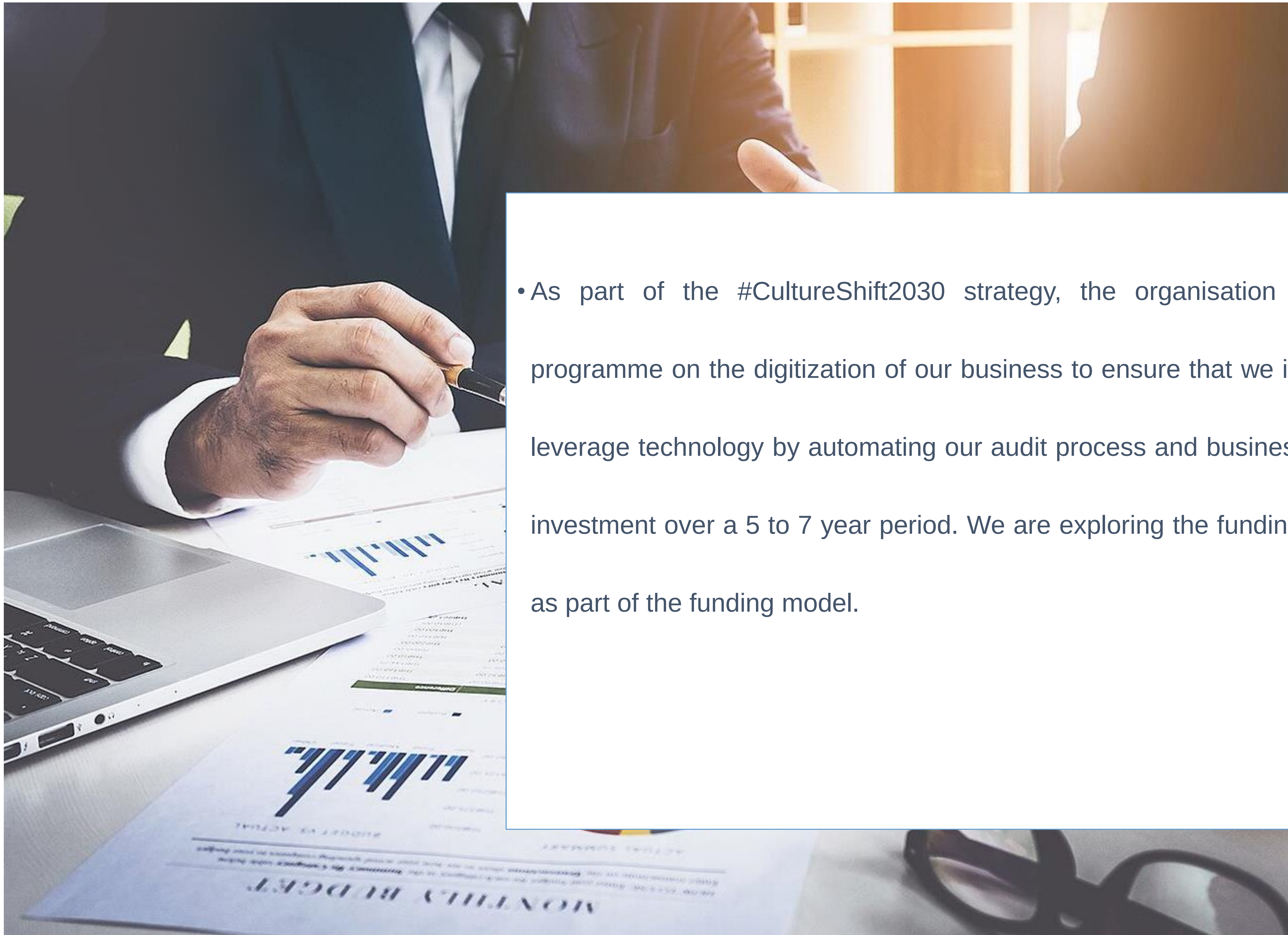
- material **financial loss** (estimated R12 billion) — 169
- substantial **harm to public sector institution** — 9
- **misuse of material public sector resource** — 1

No actions were taken to address 82% of these matters until we issued notifications

2021-22 PFMA – MI Impact

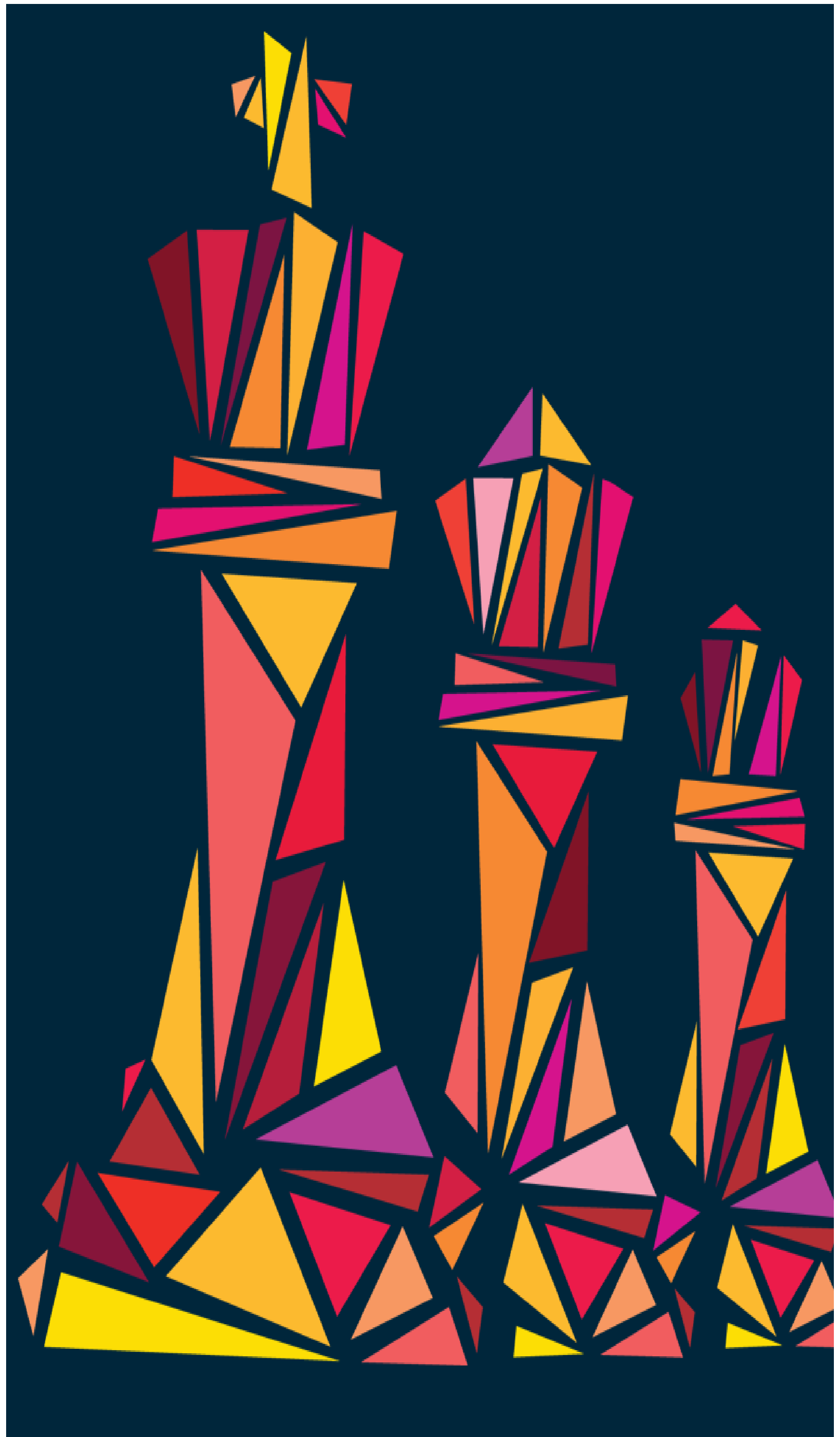
ACTIONS TAKEN BY AUDITEES

R14 m	Financial loss **recovered**
R636 m	**Prevented financial loss** from taking place
R509 m	Financial loss **in process of recovery**
39	**Internal controls improved** to prevent recurrence
36	Responsible officials identified and **disciplinary process** completed or in process
15	**Fraud/criminal investigations** instituted
5	**Stopped supplier contracts** where money is being lost



- As part of the #CultureShift2030 strategy, the organisation will embark on capital investments programme on the digitization of our business to ensure that we improve our operational processes, i.e. leverage technology by automating our audit process and business. This will require significant financial investment over a 5 to 7 year period. We are exploring the funding options for these capital investments as part of the funding model.

SUPPORT REQUESTED FROM SCOAG



Funding Model

- The reviewed funding model will be shared with ScoAG for consideration and approval once it has been finalised.
- The AGSA seek SCoAG to continue to approve for the retention of the surpluses to assist to fund capital investments in the future.

Support with debt collection

- SCOAG to continue to support the AGSA to with debt collection.

Funding support on Real-time audits

- SCOAG to continue to support AGSA to get funding when there is a request for real-time audits.

THANK YOU

Stay in touch with the AGSA

www.agsa.co.za

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Auditor-General of South Africa

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