



General report on the provincial audit outcomes of the **FREE STATE**



AUDITOR-GENERAL  
SOUTH AFRICA



# General report on audit outcomes

## FREE STATE PFMA 2013-14

### Our reputation promise/mission

"The Auditor-General of South Africa has a constitutional mandate and, as the Supreme Audit Institution (SAI) 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."



The information and insights presented in this flagship publication of my office are aimed at empowering oversight structures and executive leaders to focus on those issues that will result in reliable financial statements, credible reporting on service delivery and compliance with laws and regulations.

This publication also captures the commitments that leaders have made to improve audit outcomes.

I wish to thank the audit teams from my office and the audit firms that assisted with the auditing of provincial government for their diligent efforts towards fulfilling our constitutional mandate and the manner in which they continue to strengthen cooperation with the leadership of the province.

*Auditor-General*

Kimi Makwetu  
Auditor-General



AUDITOR - GENERAL  
SOUTH AFRICA

# OVERVIEW



Four auditees achieved clean audits

Slight improvement in audit outcomes

The departments of education and health need the most attention

78% of auditees received financially unqualified audit opinions



Qualified opinions avoided by eight auditees through correcting material misstatements identified during audit process

Slight improvement in the quality of financial statements submitted for audit

Slight improvement toward improving reliability and usefulness of annual performance report

Slight improvement in the quality of performance reports submitted for audit



Audit findings avoided by two auditees through correcting material misstatements identified during audit process

Material non-compliance with legislation by 78% of auditees

Increased levels of unauthorised, irregular as well as fruitless and wasteful expenditure



Uncompetitive and unfair procurement processes/  
inadequate contract management/  
conflicts of interest not declared

Regression in supply chain management

Financial health regressed at some departments and public entities



Financial statement analyses show continuing risks that affect auditees' financial health

Vacancies and instability in key positions are affecting audit outcomes

No improvement in HR management controls

Confidentiality, integrity and availability of information at risk

No progress in addressing root causes of poor audit outcomes



Key role players did not provide adequate assurance to improve controls

Slight improvement in the ICT controls

Implementation and impact of commitments and initiatives of role players limited



Audit outcomes of portfolios of MECs and commitments made for improvement

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# FREE STATE CLEAN AUDITS 2013-14



## DEPARTMENT

Provincial treasury  
Free State legislature  
Department of Sport, Arts, Culture and Recreation



## PUBLIC ENTITY

Fleet Management Trading Entity



# EXECUTIVE SUMMARY

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## Executive summary

This general report summarises the audit outcomes of the Free State provincial government for the financial year ended 31 March 2014.

The total adjusted budgeted expenditure of the province was R27,7 billion in 2013-14. The budget figure only includes voted departmental funds (i.e. public entities are not included). The following were the main areas of expenditure:

- Employee cost R15,9 billion
- Goods and services R4,6 billion
- Transfer payments R2,9 billion
- Capital expenditure R4,3 billion

We audited every department and eight of the public entities in the province, also called 'auditees' in this report.

It is important to note that our annual audits have once again focused on the following three areas:

1. Fair presentation and whether the financial statements are free from material misstatements.
2. Reliable and credible performance information for purposes of reporting on predetermined objectives.
3. Compliance with all laws and regulations governing financial matters.

### Overall audit outcomes

There has been a slight year-on-year improvement in the overall audit outcomes when compared to previous years; however, the number of clean audit opinions remained unchanged. The audit outcomes of five auditees improved, while two auditees regressed. Where improvements were noted, the progress is attributed to the members of the executive council enhancing oversight and management responding timeously, whereas regressions and stagnations were the result of a slow response by management to address prior year matters at 78% of auditees.

This progress towards better outcomes has been slowed down by the lack of improvement in basic key internal controls in day-to-day operations, which casts doubt upon the sustainability of the progress made. Based on the key control assessments over the past few years, management does not take ownership of the process as limited or no improvements are seen in internal controls from year to year.

Notwithstanding a commitment made in the previous year to address the skills challenge in departments and entities that had not achieved clean audit opinions, significant vacancies and/or instability in key positions (head of department, chief financial officer, head of supply chain management and the manager responsible for reporting on predetermined objectives, as well as direct reports to all of them) were noted at 67% of auditees. Another concern was that certain officials appointed in these key positions lacked appropriate competencies at 67% of the auditees.

Only six auditees (33%) submitted financial statements that did not require material adjustments to avoid qualification.

### Financially unqualified with no findings

Four auditees (21%) received a **financially unqualified opinion with no findings** (depicted in green in this report) as they have passed the audit test in each of the above-mentioned aspects. This is commonly referred to as a 'clean audit'. Provincial treasury, the department of Sports, Arts, Culture and Recreation as well as the Fleet Management Trading Entity managed to retain clean audit opinions. The provincial legislature reclaimed its clean audit status (unqualified with findings audit opinion), while the department of the Premier regressed from a clean audit opinion to a qualified audit opinion.

### Financially unqualified with findings

Ten auditees (53%) received **financially unqualified audit opinions with findings** on their performance information, compliance with legislation, or both these aspects (depicted in yellow in this report). These are auditees that have passed the critical test of fair presentation of financial statements, which means that they have accounted accurately for their financial transactions.

Four auditees (21%) were able to improve from a qualified opinion to an unqualified opinion on the financial statements, namely Economic Development, Tourism and Environmental Affairs, Public Works, Free State Development Corporation and Free State Tourism Authority. This was due to a concerted effort by management to address prior year qualification areas. It is commendable that the department of Public Works, as custodian of all immovable assets in the province, is one of the auditees that were able to improve their asset management processes.

The majority of auditees managed to obtain unqualified audit opinions with findings. This is the audit outcome that showed most improvement, but it is also where most auditees stagnate after they managed to improve to an unqualified audit opinion with findings. This is an indication that there is a greater focus by

auditees to obtain an unqualified audit opinion, but not the same drive to address findings on the annual performance report and compliance with legislation. The significant irregular expenditure incurred in the province caused by non-compliance with supply chain management requirements is one of the main reasons why auditees are unable to move to clean audit outcomes. Another reason is that findings on the quality of financial statements and annual performance reports are not addressed due to a lack of competencies and systems to support the collation and reporting of financial and performance information.

### **Qualified audit opinion**

Four auditees (21%) received a **qualified audit opinion** (depicted in purple in this report), which means that they were unable to adequately and accurately account for all the financial effects of the transactions and activities they conducted. In this regard, the financial statements they presented were unreliable in certain areas.

Of concern are the departments of the Premier and Education, whose audit outcomes of the previous two years were not sustained as they regressed from unqualified to qualified audit opinions. This was mainly due to slow response by management to address concerns raised by the auditors regarding the quality of the submitted financial information.

The departments of Human Settlements and Health did not manage to address all their qualifications and findings on performance information and compliance with laws and regulations during the past three years as their basic daily and monthly controls are not yet all functioning effectively.

### **Other significant audit observations**

#### ***Annual performance reports***

Auditees are required to measure their actual service delivery against the performance indicators and targets set for each of their predetermined performance objectives and to report on this in their annual performance reports.

The province made progress in the area of reporting on predetermined objectives to ensure transparent reporting on the status of implementing undertakings made to the public. However, 53% of auditees made material adjustments to their performance reports during the audit process. Auditees are still relying on the audit process to identify and correct misstatements in the performance information. Effective oversight should be exercised of district offices. There should be a consistent format for the collection of performance information from district offices. The information received from the district offices by head office should also be reviewed against support on a monthly basis. Furthermore, annual and cyclical targets should be monitored throughout the year and reported on, not only at year-end.

Auditees need to adopt the best practices in the province which relate to the implementation of systems, with related internal controls established and

monitored on an ongoing basis. In addition, the auditees need to continue implementing the recommendations arising from the performance audit of the readiness of auditees to report on their performance.

### ***Non-compliance with laws and regulations***

Non-compliance with laws and regulations is of high concern and was evident at 14 auditees (78%), with no improvement since the prior year. Despite this, 56% of auditees had taken no steps to implement consequences for poor performance or non-compliance with legislation. The main areas of non-compliance related to the quality of the financial statements submitted for auditing, the prevention and follow-up of unauthorised, irregular and fruitless and wasteful expenditure, as well as inadequate procurement processes being followed by auditees. The value of these controls cannot be emphasised enough as they are an important mechanism to narrow the space for widespread abuse of the public resources that are required to provide services to citizens.

### ***Irregular expenditure***

As a result of a breakdown in controls and the lack of proper systems to prevent, detect and record irregular expenditure, auditees entered into transactions that were not concluded in accordance with regulations and other prescripts. Irregular expenditure of R2,429 billion was incurred by 17 auditees (94%) for the period under review. The major contributors responsible for 92% of the total irregular expenditure were the departments of Health, Human Settlements and Education. This is of concern as the departments of Health and Education received the largest portion of the budget allocation (67%) in the province.

Of the R2,429 billion in irregular expenditure incurred in 2013-14, most was as a result of non-compliance with supply chain management legislation amounting to R1,978 billion (81%). We have determined through our normal audits that R936 million of this amount represents goods and services that were received despite the normal processes governing procurement not being followed. For the remainder of the amount (R1 042 million) of irregular expenditure relating to supply chain management we could not specifically confirm that goods and services were not received. However, no material risks were identified for goods and services paid but not received.

The main reason for incurring irregular expenditure is that credible procurement plans are not developed, which then filters through to project plans. Therefore auditees do not follow adequate procurement processes, which results in crisis management, e.g. invalid deviations to utilise all funds before year-end in a bid to avoid surrendering unspent funds. As a result, there was a lack of transparency during procurement processes which hampered the competitiveness thereof.

There is an increasing trend where auditees employ the strategy of delegating their functions to another entity, appointing them as implementing agents. Fair, equitable and transparent procurement processes are not always followed to appoint these implementing agents. Furthermore, once payments are made no

further monitoring is done by auditees to ensure that fair, equitable and transparent procurement processes are followed by the implementing agents to ensure the best price is paid when they spend money on behalf of the auditee. The use of implementing agents is especially of concern in light of the poor financial health of the province since the best prices are not always paid for goods and services. In addition, management fees have to be paid although more than half (57%) of the provincial budget is already spent on employee cost while it is expected that government employees should perform the duties delegated to implementing agents.

The high occurrence of irregular expenditure year-on-year results from a general lack of consequences for officials responsible for incurring such expenditure. At 56% of auditees no steps were taken to implement consequences for poor performance or non-compliance with legislation. Leadership should give serious attention to investigating irregular expenditure already incurred and to preventing further irregular expenditure. The significant irregular expenditure incurred in the province caused by non-compliance with supply chain management requirements is one of the main reasons why auditees are unable to improve towards clean audit outcomes. There is also an ongoing need for oversight role players to ensure that accounting officers and senior management are held accountable for providing the desired level of assurance that will maintain the momentum towards improved audit outcomes.

### **Unauthorised expenditure**

Unauthorised expenditure refers expenditure that was not incurred in accordance with the approved budget. Unauthorised expenditure of R470 million incurred in 2013-14 was due to overspending of the budget. There was a significant year-on-year upward trend in unauthorised expenditure, which increased by 87% in the current year compared to the previous year. The departments of Health and Education were responsible for 98% of the unauthorised expenditure. Daily and monthly disciplines need to be implemented and monitored to ensure that effective cash flow and budget management can occur to prevent unauthorised expenditure.

### **Financial health**

The financial health of the province has deteriorated since the previous years. Due to inadequate budgetary controls, nine auditees (50%) encountered serious concerns relating to financial sustainability.

The financial sustainability of departments and public entities is an area of grave concern due to, inter alia, the following:

- At 31 March 2014, the bank balances for departments as disclosed in the financial statements were in overdraft to an amount of R23 million.
- At 31 March 2014, funds to be surrendered amounted to R606 million.

- Accruals older than 30 days amounted to R976 million. Of the amount of R976 million, R856 million (88%) relates to accruals of the departments of Education and Health.
- Taking into account the overdraft, funds to be surrendered and long-outstanding accruals, the province requires R1,6 billion to clear the backlog.
- The total provincial budget for 2014-15 is R27,7 billion. Of this, R18 billion (65%) is for salaries. Therefore only R9,7 billion remains for goods and services and other service delivery such as capital expenditure.
- Since R1,6 billion of the remaining budget will need to be used to fund the backlog, only R8 billion (29%) of the budget will be available for service delivery in the 2014-15 year.

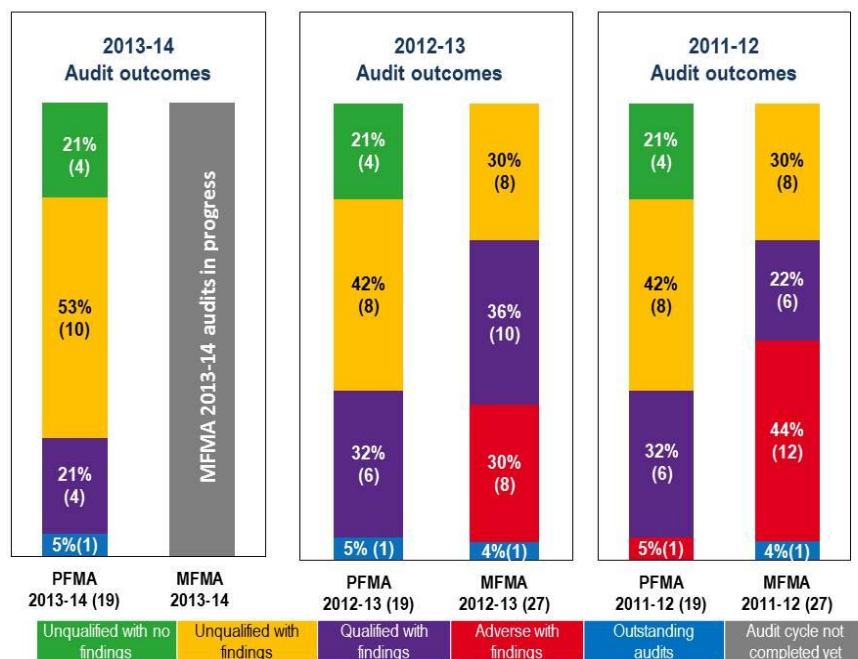
To address these shortcomings, the following controls should be implemented:

- All contracts should be revised to determine whether value for money is received.
- Contracts to be monitored rigorously and penalty clauses for non-performance in terms of the agreement used where necessary.
- Steps should be implemented to ensure that all new contracts are to the benefit of the province.
- Rigorous cash flow mechanisms to be implemented to ensure that critical projects and services are prioritised. Spending on items that do not relate to critical services and programmes should cease immediately, e.g. budgeting for critical goods and services instead of expenditures not related to the core mandate of departments.
- The province should avoid using implementing agents and should rather ensure that government employees perform the duties for which they are being paid to prevent the payment of unnecessary management fees. Where implementing agents are used they should follow the procurement processes of government to ensure fair, equitable and transparent procurement of goods and services.

### **Comparison of provincial and local government audit outcomes**

The Free State provincial government, through coordinating departments and oversight structures, supports both provincial and local government by setting standards of accountability, transparency, clean government and integrity across all institutions of government in the province. Although these two spheres of government operate autonomously, improvement in the administration and audit outcomes will benefit the province as a whole. The figure below compares the results of the two spheres of government over the last three financial years.

**Figure 1: Comparison of provincial and local government audit outcomes**



Given the province's emphasis on clean administration, the provincial government has led over the last two years on this front, receiving four (21%) clean audits in 2013-14. This was due to the provincial treasury that continued to embrace and own the assurance initiatives, and leading the collective effort to see significant improvement in the provincial government audit outcomes.

Commitments received from the provincial executive leadership during the previous year were only partially implemented and had limited impact. In certain instances, commitments obtained from the members of the executive council do not address the root causes of unsatisfactory audit outcomes and also do not result in the implementation of adequate key controls to ensure sustainable improvements in audit outcomes.

The slight improvement in assurance provided by senior management and accounting officers/authorities can be attributed to the implementation and monitoring of recommendations made by the AGSA. However, the first-level assurance providers (senior managers, accounting officers/authorities and members of the executive council) are still not providing the level of assurance as required.

Based on the 2013-14 audit outcomes, the provincial executive leadership undertook to address competencies by means of a self-assessment per department and to identify training needs at senior management and lower levels to sustain competency capabilities. Attention will also be given to compliance with supply chain management prescripts, while guidance will be provided to departments on the utilisation of

implementing agents and forcing implementing agencies to follow government procurement processes.

Although our interactions with the committees of the legislature (portfolio and public accounts committees) have improved, the resolutions adopted by the committees lack impact as these were not distributed to the departments and public entities by the department of the Premier for implementation, resulting in limited assurance being provided by these committees. Although the internal audit unit and audit committees fulfil their legislative obligations, there is only some assurance provided as management did not respond to their recommendations. This resulted in a decrease in assurance provided compared to the prior year.

However, progress towards clean audits has been comparatively slower in the local government sphere, with none of the auditees attaining financially unqualified opinions with no findings in 2012-13. The provincial treasury, department of Cooperative Governance and Traditional Affairs (CoGTA) and the department of the Premier have a direct role to play in supporting and monitoring local government, thereby providing a level of assurance. The provincial legislature provides oversight through its speakers' forum and oversight committees. CoGTA, working together with the provincial treasury and the department of the Premier as assurance providers, has an important role to play by promoting integrated service delivery. This includes developing and monitoring provincial policies and legislation to promote integration in government's development programmes and service delivery.

Overall, the level of assurance provided by the provincial treasury, CoGTA, the Free State legislature and the department of the Premier has stagnated since 2011-12. The role of oversight has to be strengthened by these coordinating ministries if the level of assurance is to be elevated and audit outcomes are to be improved.

Local government finds itself under financial distress, which is of concern. As reported in the general report for the 2012-13 MFMA cycle, local government finds itself in a net current liability position of R2 billion. Further financial pressure will be placed on the provincial budget as assistance will be sought by municipalities to alleviate their financial distress. A contributing factor is that approximately R200 million is owed by the department of Public Works to municipalities for services rendered on provincial government buildings.

The financial distress at municipal level continued during 2013-14 as Eskom is owed more than R1 billion. There is a real threat that certain municipalities may have their electricity disconnected due to non-payment unless assistance is provided by the province.

**Provincial department of cooperative governance and traditional affairs**

Although CoGTA provides financial, human resource and consultancy assistance to municipalities, the current status at municipalities compels interactions by CoGTA to be of a crisis management nature. This leaves little opportunity for CoGTA to monitor and evaluate the assistance and processes put in place at the municipalities. Apart from this, their own staff assist municipalities with financial management, administrative challenges and poor performance, which necessitate increased accountability and

transparency at municipal level together with improved coordination and cooperation across all levels in the province.

CoGTA should develop a long-term plan with specific target dates and indicators on how to move municipalities away from their current status to independent functioning, while the objectives in the department's annual performance plans, which are mostly input driven, should be reconsidered to measure the impact of delivering on their mandate.

***Key leadership actions to be taken to achieve clean audit outcomes***

We remain hopeful that the advances towards clean audits can be emulated in the local government sphere as well as by other auditees in the provincial government sphere. It is crucial to note that those auditees that advanced towards clean were commonly characterised by the following:

- a) Accounting officers/authorities were proactive in driving action plans to improve the financial control environment and to instil a culture of good financial governance and compliance with legislation.
- b) The executive authority and accounting officer/authority set a tone of zero tolerance for non-performance and held staff accountable for keeping quality financial and performance information and complying with key legislation.
- c) Robust and proactive audit committee and internal audit functions on matters regarding the implementation and monitoring of action plans to address recurring findings and the commitments made.
- d) Accounting officers/authorities and senior management successfully implemented basic internal controls and accounting disciplines by preparing regular and accurate financial statements, which enabled governance structures to play an effective review role.
- e) Improved performance and consequence management by incorporating the requirements of preparing credible and regular financial reports into senior management's performance agreements and holding them accountable.
- f) Stability at senior management level and within finance units, with the required level of technical competence and experience.

***Key leadership actions needed by both executive and oversight leadership to improve audit outcomes***

- a) Commitments obtained from members of the executive council should address the root causes of unsatisfactory audit outcomes and should result in the

implementation of adequate key controls to ensure sustainable improvements in audit outcomes.

- b) Commitments received from the provincial executive leadership should be fully implemented and, where shortcomings are identified, corrective action should be taken.
- c) The provincial executive leadership needs to give attention to compliance with supply chain management prescripts and support the administrative leadership where needed to fully enforce these prescripts.
- d) The provincial executive leadership needs to provide guidance to departments on the utilisation of implementing agents and forcing implementing agencies to follow government procurement processes.
- e) The provincial executive leadership needs to provide guidance and take action to ensure that all new contracts are to the benefit of the province; that rigorous cash flow mechanisms to be implemented to ensure that critical projects and services are prioritised, and to address the concerning financial health situation of the province.
- f) Portfolio and public accounts committee resolutions should be distributed to the departments and entities by the department of the Premier for implementation, after which the relevant committees should monitor the progress made by the departments and entities and, where shortcomings are identified, corrective action should be taken.

At the heart of improved audit outcomes is a leadership tone that must inform the seriousness and urgency with which appropriate action plans and initiatives are implemented and monitored. If the barriers inhibiting the achievement of improved audit outcomes are to be breached, political and administrative management should set the tone by ensuring that vacancies are filled with competent officials and that basic key internal controls are implemented and monitored. A performance management system should flow from measuring the strategic objectives to measuring the performance of each employee to ensure that staff are held accountable for poor performance and/or transgressions, especially transgressions relating to irregular expenditure.

We remain firmly committed to making a positive contribution to overcoming the obstacles to clean administration in the province. We will continue to make ourselves available and to provide proactive insights into the root causes of weak internal control environments. The engagements will include timely feedback on, and inputs into, the adequacy of the assurance provided by all role players.

# SUMMARY OF AUDIT OUTCOMES AND KEY RECOMMENDATIONS FOR IMPROVEMENT

# 1. Our auditing and reporting process

We audited every department and eight of the public entities in the province, also called *auditees* in this report, so that we can report on the **quality of their financial statements** and **annual performance reports** and on their **compliance with key legislation**.

We also assess the root cause of any error or non-compliance, based on the internal control that had failed to prevent or detect it. We report in the following three types of reports:

- We report our findings, root causes and recommendations in management reports to the senior management and accounting officers or authorities of auditees, which are also shared with the members of the executive council (MECs) and audit committees.
- Our opinion on the financial statements, material findings on the annual performance report and non-compliance with legislation, as well as significant deficiencies in internal controls, are included in an audit report, which is published with the auditee's annual report and dealt with by the public accounts committees and portfolio committees as applicable.
- Annually we report on the audit outcomes of all auditees in a provincial general report (such as this one), in which we also analyse the root causes that need to be addressed to improve audit outcomes in the province. Before the general reports are published, we share the outcomes and root causes with the provincial leadership, the provincial legislature and key role players in national and provincial government.

Over the past few years, we have intensified our efforts to assist in improving the audit outcomes by identifying **the key controls** that should be in place at auditees, assessing these on a regular basis and sharing the assessment with members of the executive, accounting officers and authorities, as well as audit committees.

We further identified the following **key risk areas** that need to be addressed to improve audit outcomes as well as financial and performance management, and we specifically audit these so that we can report on the status thereof: ■ quality of submitted financial statements and performance reports ■ supply chain management ■ financial health ■ information technology controls ■ human resource management (including the use of consultants).

During the auditing process, we work closely with the accounting officer or authority, senior management, audit committee and internal audit unit as they are **key role players** in providing assurance on the credibility of the auditee's financial statements, performance report as well as compliance with legislation.

We also continue to strengthen our relationship with MECs, the premier and the provincial treasury as we are convinced that their involvement and oversight have to some extent played – and will continue to play – a crucial role in the performance of auditees in the province. We share our messages on key controls, risk areas and root causes with them and obtain and monitor their commitments to implement initiatives that can improve audit outcomes.

Figure 2 provides an overview of our message regarding the 2013-14 audit outcomes, which is a continuation of what we had reported and recommended in our last report on the audit outcomes in the province.

The overall audit outcome in figure 2 shows our opinion per auditee on their financial statements and whether we raised material audit findings on the quality of their annual performance report and compliance with key legislation. The overall audit outcomes fall into four categories:

1. Auditees that received a **financially unqualified opinion with no findings** are those that were able to:
  - produce financial statements free from material misstatements. Material misstatements mean errors or omissions that are so significant that they affect the credibility and reliability of the financial statements
  - measure and report on their performance in accordance with the predetermined objectives in their annual performance plan in a manner which is useful and reliable
  - comply with key legislation.
2. Auditees that received a **financially unqualified opinion with findings** are those that were able to produce financial statements without material misstatements but are struggling to:
  - align their performance reports to the predetermined objectives they committed to in their annual performance plans
  - set clear performance indicators and targets to measure their performance against their predetermined objectives
  - report reliably on whether they achieved their performance targets
  - determine which legislation they should comply with, and to implement the required policies, procedures and controls to ensure that they comply.
3. Auditees that received a **financially qualified audit opinion with findings** have the same challenges as those that were unqualified with findings but, in addition, were unable to produce credible and reliable financial statements.

This audit outcome is also commonly referred to as a 'clean audit'.



Their financial statements contained material misstatements which they could not correct before the financial statements were published.

4. The financial statements of auditees with an **adverse opinion** contain so many material misstatements that we disagree with virtually all the amounts and disclosures therein. Those auditees with a **disclaimer of audit opinion** could not provide us with evidence for most of the amounts and disclosures in the financial statements. We were unable to conclude or express an opinion on the credibility of their financial statements. Auditees with adverse and disclaimed opinions are typically also:
  - unable to provide sufficient supporting documentation for the achievements they report in their annual performance reports
  - not complying with key legislation.

With reference to figure 2 and other figures, and when reading the rest of the report, please note that only a movement of more than 5% is regarded as an improvement or a regression. Movement is depicted as follows:

 Improved  Stagnant or little progress  Regressed

The rest of the section summarises the audit outcomes and our key recommendations for improvement, followed by a summary of the audit outcomes of the auditees in each portfolio of the member of the executive council. The report also includes three annexures that detail the audit outcomes and findings per auditee, the status of the drivers of internal controls at the auditees and a five-year view of the audit outcomes. The glossary of terms included after the annexures defines the terminology used in this report.

Figure 2: Overview of audit outcomes and key recommendations for improvement

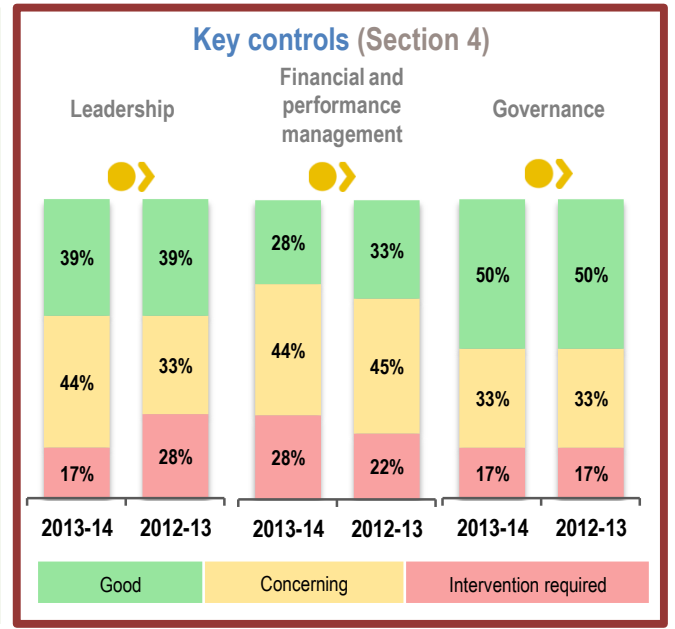
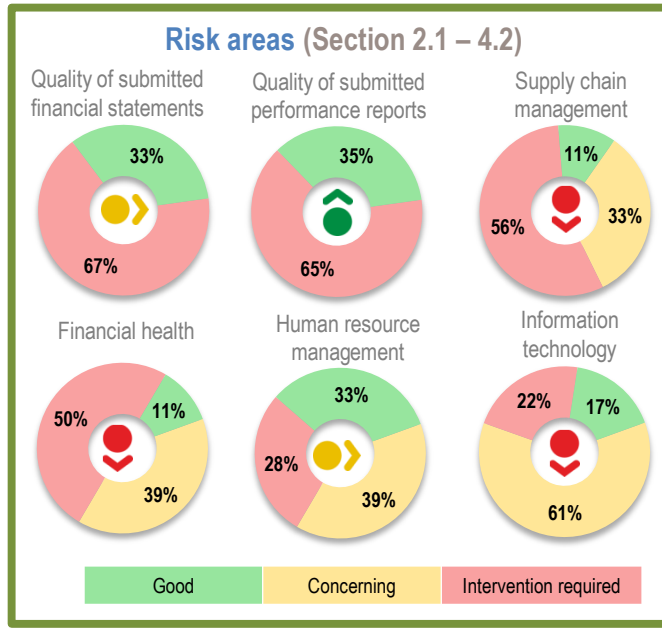
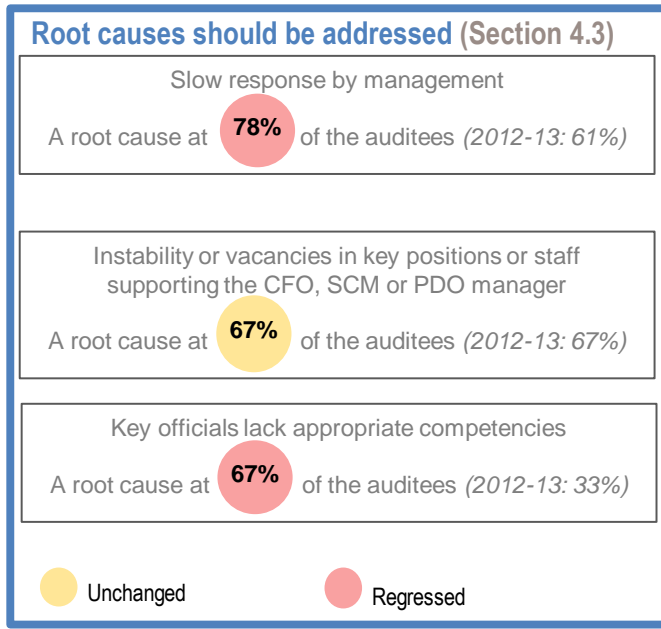
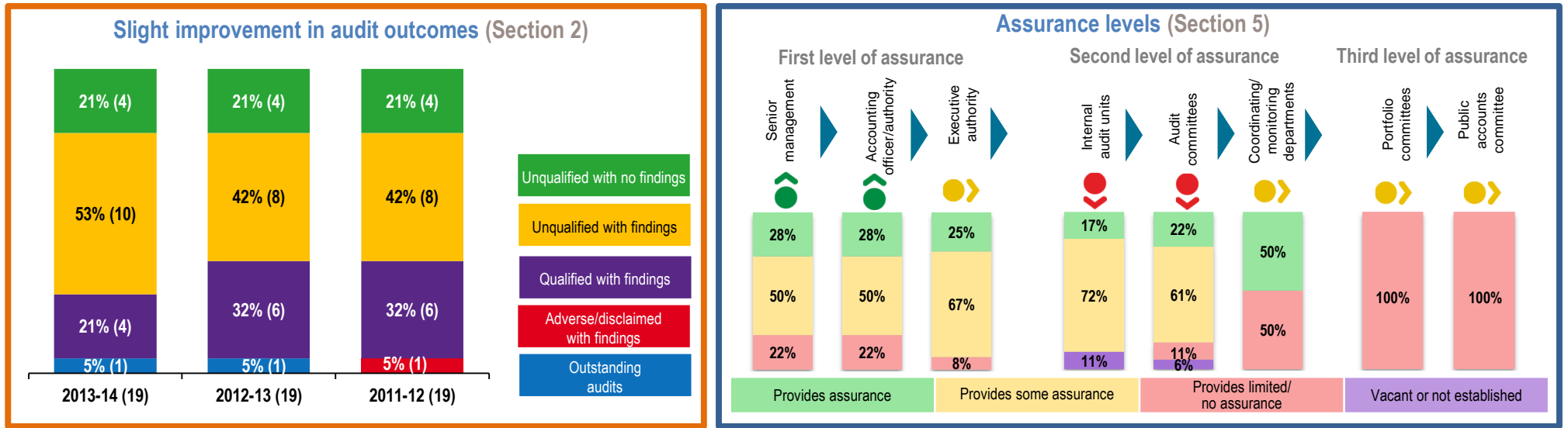


Figure 3: Movements in audit outcomes

	5 Improved	11 Unchanged	2 Regressed	1 Outstanding
Unqualified with no findings = 4	<ul style="list-style-type: none"> <li>Free State Legislature</li> </ul>	<ul style="list-style-type: none"> <li>Provincial Treasury</li> <li>Sport, Arts, Culture and Recreation</li> <li>Fleet Management</li> </ul>		<ul style="list-style-type: none"> <li>Political Party Fund</li> </ul>
Unqualified with findings = 10	<ul style="list-style-type: none"> <li>Economic Development, Tourism and Environmental Affairs</li> <li>Public Works</li> <li>Free State Development Corporation</li> <li>Tourism Authority</li> </ul>	<ul style="list-style-type: none"> <li>Agriculture and Rural Development</li> <li>CoGTA</li> <li>Police, Roads and Transport</li> <li>Social Development</li> <li>Central Medical Trading Account</li> <li>Gambling and Liquor</li> </ul>		
Qualified with findings = 4		<ul style="list-style-type: none"> <li>Health</li> <li>Human Settlements</li> </ul>	<ul style="list-style-type: none"> <li>Premier</li> <li>Education</li> </ul>	

The colour of the auditee's name indicates the audit opinion from where the auditee has moved.  
The one outstanding audit remains outstanding from the 2011-12 financial year.

## Overall audit outcomes

Provincial government consists of 13 departments (including the legislature) and eight public entities. The Free State Housing Fund and the Nature Conservation Trust Fund are not included in this report as they are dormant. Both funds received unqualified audit opinions with no findings. The Provincial Revenue Fund was also excluded from this report.

Figure 2 indicates that there has been a slight year-on-year improvement in the overall audit outcomes when compared to previous years; however, the number of clean audit opinions remained unchanged. There was a decrease of 11% in the number of auditees with qualified audit opinions. Of concern is that the improvement in audit outcomes is not aligned to the key controls of auditees where there was a stagnation overall, which questions the sustainability of audit outcomes. Figure 3 analyses the movement in the audit outcomes of the different auditees since the previous year that had resulted in the net improvement in the audit outcomes of the province. It further shows the previous year's opinion relating to the audit that had not been completed by 31 August 2014, which was the cut-off date we set for inclusion of audit outcomes in this report.

The Political Party Fund submitted their financial statements late for the 2008-09 to 2012-13 financial years, with the result that the audits up to 2011-12 were only finalised during the current year. The 2012-13 audit was still in progress at the cut-off date for this report, while the financial statements for 2013-14 have not yet been submitted. These are therefore excluded from the rest of the analysis drawn in the general report.

Two of the four oversight departments, i.e. provincial treasury and the legislature (which improved from unqualified with findings to unqualified with no findings) obtained clean audit opinions. Of concern was the slow response by the leadership of the department of the Premier with regard to the fixed asset register, which resulted in regression from a clean audit to a qualified opinion with findings on compliance with laws and regulations. The other governing department, CoGTA, was again not able to improve to a clean audit as it failed to address all findings on predetermined objectives and compliance with laws and regulations.

It is evident in figure 3 that the majority of auditees managed to obtain unqualified audit opinions with findings. This is the audit outcome that showed most improvement, but it is also where most auditees stagnate after they managed to improve to an unqualified audit opinion with findings. This is an indication that there is a greater focus by auditees to obtain an unqualified audit opinion, but not the same drive to address findings on the annual performance report and compliance with legislation. The significant irregular expenditure incurred in the province caused by non-compliance with supply chain management requirements is one of the main reasons why auditees are unable to improve to clean audit outcomes (refer to section 2.3). Another reason is that findings on the quality of financial statements and annual performance reports are not addressed due to a lack of

competencies and systems to support the collation and reporting of financial and performance information (refer to section 2.1 and 2.2).

An analysis follows of audit outcomes for financial statements, annual performance reports and compliance with legislation that contributed to the overall audit outcomes.

## 2. Status of the three areas that we audit and report on

### 2.1 Financial statements

The purpose of the annual audit of the financial statements is to provide the users thereof with an opinion on whether the financial statements fairly present, in all material respects, the key financial information for the reporting period in accordance with the financial framework and applicable legislation. The audit provides the users with reasonable assurance on the degree to which the financial statements are reliable and credible, on the basis that the audit procedures performed did not identify any material errors or omissions in the financial statements. We use the term *material misstatement* to refer to such material errors or omissions.

**Figure 4: Three-year trend – financial statements**

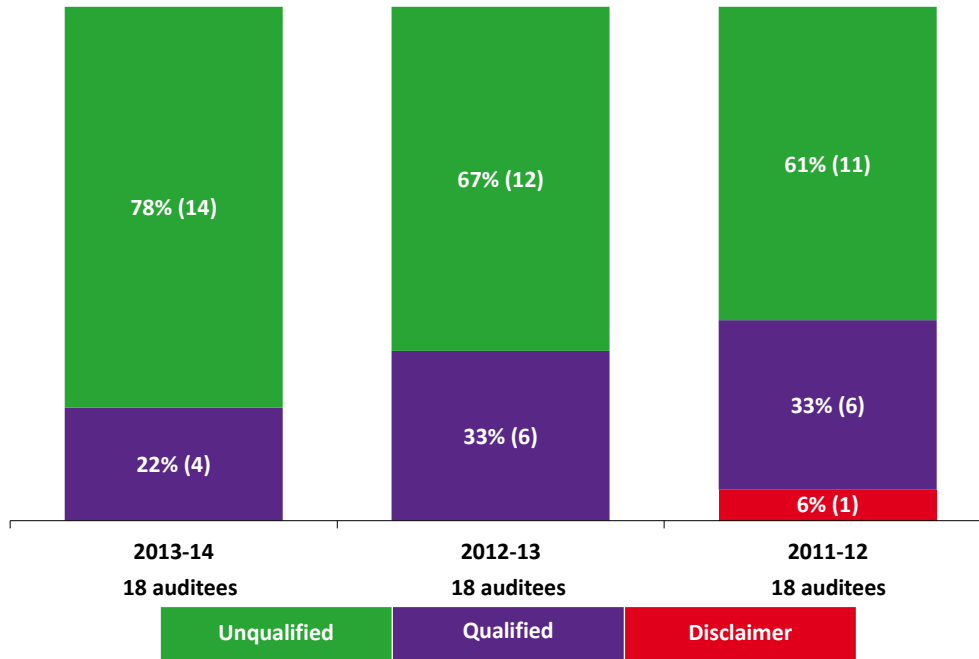


Figure 4 shows that there has been an improvement in the audit opinions on financial statements when compared to the previous year.

It is commendable that four auditees were able to improve from a qualified opinion to an unqualified opinion on the financial statements, namely Economic Development, Tourism and Environmental Affairs, Public Works, Free State Development Corporation and Free State Tourism Authority. This was due to a concerted effort by management to address prior year qualification areas.

Of concern are the department of the Premier and the department of Education, whose audit outcomes of the previous two years were not sustained as they regressed from unqualified to qualified audit opinions. This was mainly due to slow response by management to address concerns raised by the auditors regarding the quality of the submitted financial information.

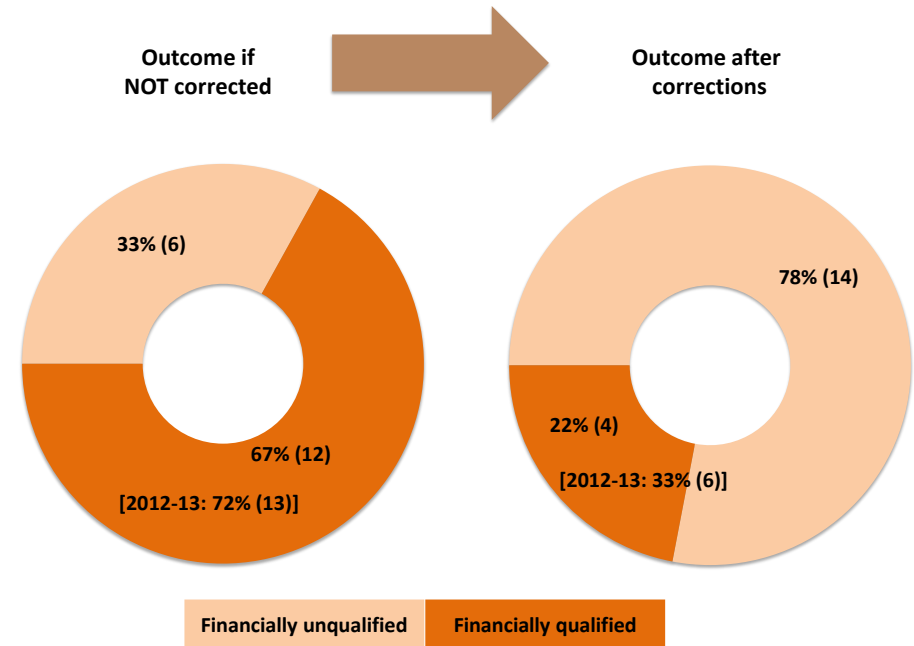
The departments of Human Settlements and Health did not manage to address all their qualifications during the past three years as their basic daily and monthly controls are not yet all functioning effectively.

All the public entities now have unqualified audit opinions, while the departments are progressing at a slower pace.

In 2013-14, the combined budgeted expenditure of the departments of Education, Health and Public Works comprised 72% of the total in the province. Although the department of Public Works improved to an unqualified opinion, Health and Education were unable to do so. This is of concern as these are service delivery departments that are responsible for the largest portion of the provincial budget but are not able to keep accurate financial records, report transparently and adhere to laws and regulations.

### The quality of the financial statements submitted for auditing

**Figure 5: Quality of financial statements submitted for auditing**



While all auditees submitted their financial statements for auditing on time, figure 5 shows that only six auditees (33%) submitted financial statements that did not contain material misstatements. These were the departments of Agriculture and Rural Development, Free State legislature, provincial treasury, Social Development, Sport, Arts, Culture and Recreation and Fleet Management Trading Entity.

Figure 5 also shows that eight auditees (45%) received a financially unqualified audit opinion only because they corrected all the misstatements we had identified during the audit. There has not been an overall improvement in the quality of financial statements since the prior year. Only two auditees, the departments of Agriculture and Rural Development and Social Development, improved the quality

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of their financial statements since the prior year as no material adjustments had to be made during the audit process to obtain an unqualified opinion. However, the quality of the department of the Premier's financial statements regressed as material findings were identified during the audit.

The poor quality of the financial statements we received is reported as material compliance findings in the audit report, as it also constitutes non-compliance with the Public Finance Management Act, 1999 (Act No. 1 of 1999) (PFMA) (refer to section 2.3). The finding is only reported if the financial statements we received for auditing included material misstatements which could have been prevented or detected if the auditee had an effective internal control system. We do not report if the misstatement resulted from an isolated incident or if it relates to the disclosure of unauthorised, irregular or fruitless and wasteful expenditure that was identified after the financial statements were submitted.

The most common areas which auditees corrected in order to achieve unqualified audit opinions are receivables, payables and accruals. This is due to the basic daily and monthly controls not operating effectively.

The disclosure notes to the departments' financial statements constitute the area where most of the corrections were made due to information which is only being compiled or updated after year-end when the financial statements are prepared. This is also one of the main reasons why departments fail to produce financial statements without material misstatements as this information should be collected and recorded throughout the year and not only at year-end. Poor record keeping further hampers the effectiveness of the financial reporting process.

Continued reliance on the auditors to identify corrections to be made to the financial statements to obtain an unqualified audit opinion is not a sustainable practice. Furthermore, it places undue pressure on legislated deadlines and increases the audit fees.

Consultants were used at four departments to assist with the preparation of financial statements or the fixed asset register due to a lack of skills and vacancies at these auditees. It is, however, of concern that material misstatements were identified in the financial statements in three of these departments in the consultants' areas of responsibility. The material adjustments in instances where consultants are appointed are due to information provided by auditees to consultants not being credible as well as poor internal controls and processes in the collation of information.

### Financial statement areas qualified

Even though we reported the material misstatements to management for correction, four auditees (2012-13: 6) could not make the necessary corrections to the financial statements, which resulted in qualified audit opinions. The main reasons why corrections were not made were the slow response by management to address findings raised in the previous year and failure to actively monitor action

plans, resulting in their daily and monthly controls not functioning effectively throughout the year.

None of the public entities had qualifications on their financial statements.

Figure 6: Top three financial statement qualification areas

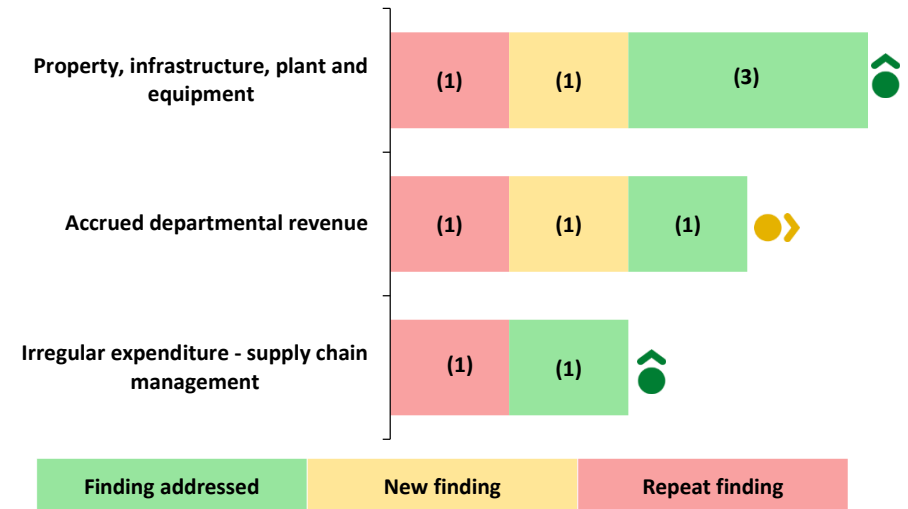


Figure 6 indicates the three most common financial statement qualification areas and auditees' progress in addressing these since the previous year. The reasons for the most common qualifications and the auditees qualified are as follows:

### Property, infrastructure, plant and equipment

The departments of Health and the Premier did not submit complete fixed asset registers that include all the assets of the department. At the department of the Premier this was due to a lack of skills in the asset management sections and the fact that the basic monthly controls (i.e. asset counts) over the fixed asset register did not function effectively throughout the financial year. The department of Health compiled a new asset register during the year but did not as part of the process perform a proper reconciliation to ensure that all the assets reflected in the previous register were also included in the current register, resulting in an incomplete asset register.

Three auditees addressed the prior year qualification on property, plant and equipment. These auditees were the departments of Public Works and Economic Development, Tourism and Environmental Affairs, as well as the Free State Development Corporation. This was as a result of action plans and recommendations being implemented and monitored. It is commendable that the department of Public Works, as custodian of all immovable assets in the province, is one of the auditees that were able to improve their asset management

processes. Although the two departments mentioned above had to make material adjustments to their financial statements during the audit process to avoid a qualification on assets, it was only possible due to their effort during the year to address the prior year findings.

### *Accrued departmental revenue*

The receivable for accrued departmental revenue could not be confirmed at the departments of Health and Human Settlements. Although the department of Health addressed the weaknesses in the current year, the qualification relates to the comparative figure as there were problems with the integrity of revenue data and management's interpretation of the reporting framework in the prior year. At Human Settlements adequate supporting documents could not be provided and an adequate system was not in place to report on this accurately. Public Works managed to address the prior year qualification on accrued departmental revenue

### *Irregular expenditure – supply chain management*

Irregular expenditure disclosed at the department of Health was not complete as the department does not have adequate processes in place to identify and record all instances of irregular expenditure. Management also did not investigate the whole population of expenditure in all instances to identify the full extent of irregular expenditure already identified by the auditors during the previous year audit. The departments of Economic Development, Tourism and Environmental Affairs were able to address the prior year qualification.

### **Recommendations**

Auditees that received qualified opinions and those that submitted financial statements of a poor quality for auditing should strengthen their processes and controls to create and sustain a control environment that supports reliable reporting. For such auditees, we recommend the implementation of at least the following key controls and best practices of those auditees that received unqualified audit opinions on their financial statements for the past three years.

- Committed and competent staff in the finance division contributed to this achievement.
- The implementation of an effective performance management system, which ensured that consequence management was implemented, also contributed to the audit outcomes.
- Controls over the departments' fixed asset registers should be implemented throughout the year. Auditees should implement processing and reconciling controls by having at least quarterly asset counts, not only at year-end, as there are simply too many assets at too many locations.
- Auditees should regularly monitor disclosures in the financial statements by implementing daily and monthly controls. The information for the disclosure

notes should not only be prepared when compiling the year-end financial statements but should be recorded on a regular basis and reviewed monthly.

In conclusion, auditees should identify the root causes of the material misstatements identified during the audit and ensure that adequate and immediate action is taken to address them. If not addressed, the quality of the financial statements may not improve or may not be sustainable in the next financial year.

## **2.2 Annual performance reports**

Auditees are required to measure their actual service delivery against the performance indicators and targets set for each of their predetermined performance objectives and to report on this in their annual performance reports. Figures 7 and 8 do not include the Central Medical Trading Account separately as their performance was reported on as part of the department of Health. We audited selected material programmes of departments and objectives of public entities to determine whether the information in the annual performance reports is useful and reliable for oversight bodies, the public and other users of the reports to assess the performance of the auditee. The programmes and objectives we select are those that are important for the delivery by the auditee on its mandate. In the audit report, we reported findings arising from the audits that were material enough to be brought to the attention of these users.

We audited the **usefulness of the reported performance information** by determining whether it was presented in the annual report in the prescribed manner and was consistent with the auditees' planned objectives as defined in their strategic plans and annual performance plans. We also assessed whether the performance indicators and targets that were set to measure achievement of the objectives were well defined, verifiable, specific, time bound, measurable and relevant.

We audited the **reliability of the reported information** by determining whether it could be traced back to the source data or documentation and was accurate, complete and valid.

**Figure 7: Three-year trend – quality of annual performance reports**

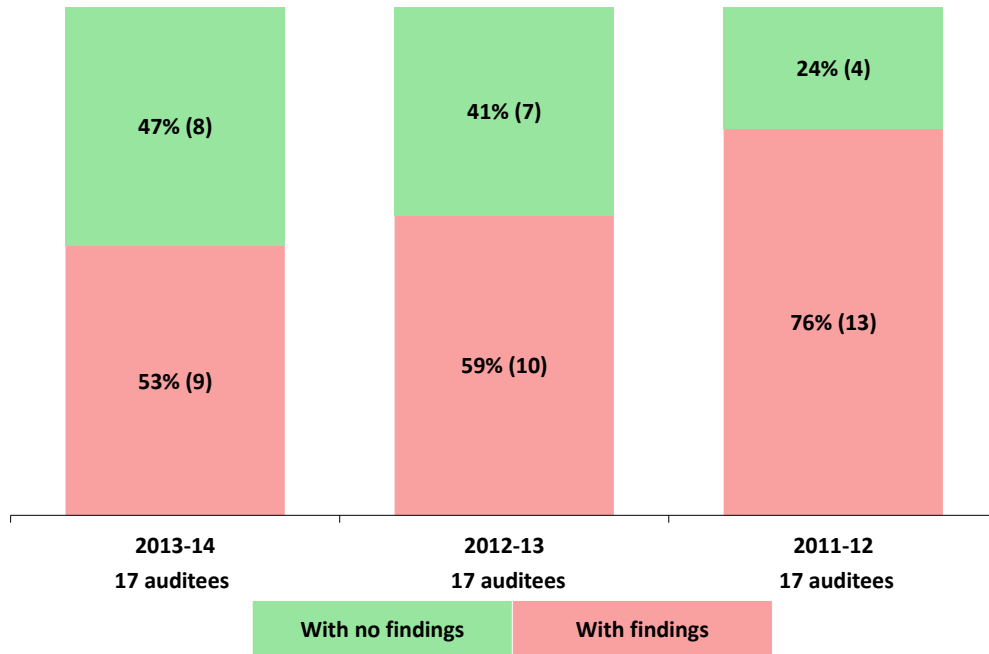


Figure 7 shows that there has been a slight increase in auditees with no material findings on the quality of their annual performance reports when compared to the previous year. This improvement only relates to departments as the quality of performance reporting at entities has remained stagnant.

The improvement from the prior year to the current year was as a result of the Free State legislature addressing the shortcomings in their reported performance information. This was due to a complete revision of the annual performance plan in the third quarter with the assistance of the provincial treasury. This resulted in the annual performance plan being more aligned to their strategic plan. Although the provincial treasury holds regular sessions with all departments regarding the annual performance plans and annual performance reports, the auditees where we reported findings attracted findings due to a lack of competencies and systems to support the collation and reporting of performance information.

The following auditees had no material findings on their performance reports for the second consecutive year: the departments of Economic Development, Tourism and Environmental Affairs, Police, Roads and Transport, Sport, Arts, Culture and Recreation, as well as the Free State Development Corporation. The department of the Premier, the provincial treasury and the Fleet Management Trading Entity had no findings on performance information for the fourth consecutive year.

In terms of the largest service delivery departments, there were no findings on usefulness of reported performance objectives at the departments of Health and

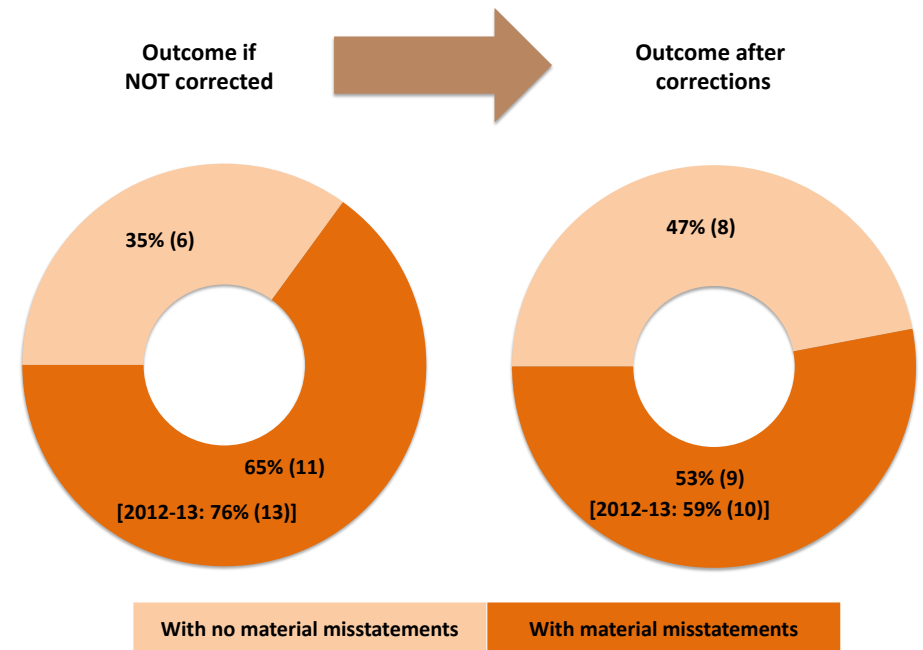
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Education. However, both departments had findings on reliability as the reported performance information did not agree to the documentation supporting it. At Public Works the reported performance information was found to be reliable as it was substantiated by adequate supporting documentation. However, it was not useful in measuring the department's required performance in terms of service delivery as it was not presented in accordance with National Treasury's annual reporting principles and was also inconsistent with planned programmes.

### The quality of the annual performance reports submitted for auditing

While all auditees submitted their annual performance reports for auditing on time, figure 8 shows that only six auditees (35%) submitted annual performance reports that did not contain material misstatements. The auditees were Economic Development, Tourism and Environmental Affairs, the Premier, Police, Roads and Transport, Free State legislature, Sport, Arts, Culture and Recreation and the Fleet Management Trading Entity.

**Figure 8: Quality of submitted annual performance report**



Nine auditees (53%) made material adjustments to their annual performance reports during the audit process. Of the nine, only two (provincial treasury and the Free State Development Corporation) corrected all the misstatements we had



identified during the audit resulting in no material misstatements remaining in performance reporting. The other seven auditees that made adjustments were unable to correct all the material misstatements in their performance reports as they also had findings on the usefulness of performance information or sufficient appropriate audit evidence could not be provided for some of the selected reported indicators. Two auditees, Health and Gambling and Liquor Authority, did not make any adjustments to their annual performance reports due to the poor quality of the reported performance information.

### Findings on usefulness and reliability of annual performance reports

Auditees' main programmes/objectives are material in relation to their budget and mandate. The following selected programmes and objectives had material findings on usefulness and/or reliability:

Auditee	Programme/Objective	Not useful	Not reliable
Agriculture and Rural Development	Programme 3: Farmer support and development	x	x
	Programme 4: Veterinary services	x	x
	Programme 5: Research and technology development service	x	
Cooperative Governance and Traditional Affairs	Programme 2: Local governance	x	x
	Programme 3: Development and planning	x	x
Education	Programme 2: Public ordinary schooling		x
	Programme 8: Infrastructure development		x
Health	Programme 2: District health services		x

Auditee	Programme/Objective	Not useful	Not reliable
	Programme 4: Provincial hospitals		x
	Programme 5: Central and tertiary hospitals		x
Human Settlements	Programme 3: Housing development, implementation, planning and targets		x
Department of Public Works	Programme 2: Public works infrastructure	x	
	Programme 3: Expanded public works programme	x	
Social Development	Programme 2: Social welfare services		x
	Programme 3: Research and development		x
Free State Gambling and Liquor Authority	Programme 1: Administration	x	x
	Programme 4: Technical services	x	x
Free State Tourism Authority	Programme 2: Marketing		x

The most common findings on the usefulness of information were the following:

- Indicators/measures not relevant to service delivery objectives
- Performance targets not measurable
- Indicators/measures not well defined

The most common findings on reliability of information were the following:

- Reported performance information not accurate
- Reported performance information not complete
- Reported performance information not valid

The prevalence of annual performance reports containing information that is not useful or reliable is a sign of weakness in the auditees' ability to adequately plan, manage and report on their performance. If addressed, it will improve the transparency and accountability of provincial government. This will ensure that performance reporting becomes more aligned to the departments' strategic goals and mandate. Proper monitoring and reporting of performance throughout the year will equip oversight bodies to measure actual service delivery against predetermined objectives and to recommend corrective action where needed.

## Findings on compliance with key legislation on strategic planning and performance management

The PFMA prescribes the manner in which strategic planning and performance management should be performed. We report material non-compliance with this legislation in the audit reports of auditees (also refer to section 2.3).

The most common finding raised at four (24%) of the auditees was that the accounting officer did not ensure that the department had and maintained an effective, efficient and transparent system of internal control over performance management. These auditees are the departments of Agriculture and Rural Development, Health and Public Works as well as the Free State Gambling and Liquor Authority.

## Recommendations

Auditees that had material findings and those that submitted poor quality annual performance reports for auditing should strengthen their processes and controls to create and sustain a control environment that supports useful and reliable reporting on performance. For such auditees we recommend the implementation of best practices that are in place at the six auditees that had no material findings on or made material adjustments to the annual performance reports. The best practice relates to a system with related internal controls that are established and monitored on an ongoing basis.

In addition, effective oversight should be exercised of district offices. There should be a consistent format for the collection of performance information from district offices. The information received by head office should also be reviewed against support on a monthly basis. Furthermore, annual and cyclical targets should be monitored throughout the year and be reported on, not only at year-end or in the relevant cycle.

Auditees also need to continue implementing the recommendations arising from the performance audit of the readiness of auditees to report on their performance as indicated in the following section.

## Free State performance audit of the readiness of government to report on its performance

The performance audit on the readiness of government to report on its performance was conducted during the 2010-11 to the 2012-13 financial years at:

- selected central performance oversight institutions
- selected national departments with concurrent functions
- provincial oversight institutions (provincial treasuries and offices of the premier) at all nine provinces
- identified provincial departments (the audit focused on the four sectors that had the highest total government expenditure, namely education, health, public works and social development).

The audit was performed transversally across the provinces and focused on the following:

- The performance reporting guidance and oversight received by government departments
- The systems and processes that government departments have put in place to report on their performance.

The audit identified the root causes of departments continuing to produce annual performance reports that are not useful and reliable. In the Free State, the audit was performed at the following oversight institutions and departments:

- **Oversight institutions**
  - Department of the Premier
  - Provincial treasury

The audit indicated that the provincial oversight institutions provided limited performance management and reporting guidance and oversight. This was due to unclear performance management and reporting guidance and oversight roles and responsibilities.

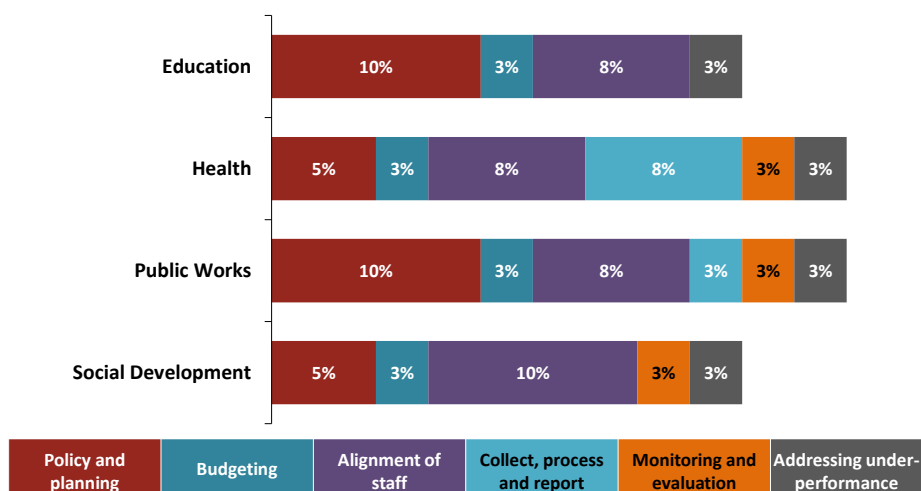
- **Departments**
  - Department of Education
  - Department of Health
  - Department of Public Works
  - Department of Social Development

The most common findings raised at the departments were the following:

- Some departments did not have approved and/or comprehensive policies and procedures for reporting on performance.
- Some performance indicators were not well defined or verifiable or did not measure whether resources were used efficiently, effectively and economically to produce the desired outputs and outcomes.
- Performance targets did not always comply with the SMART criteria and/or were not realistic. Targets were not realistic as they were not selected based on accurate baseline information or research and evaluations.
- Insufficient skilled staff to manage and report on performance
- Staff were not always held accountable for reporting on performance and/or achieving performance targets.
- At some departments approved processes and system documentation for collecting, collating, verifying, storing and reporting on actual performance did not exist.
- Material deviations between planned and actual performance were not explained by some departments. In addition, evidence to support explanations was not maintained or explanations were not reviewed by management.
- Action plans were not developed to ensure prompt corrective action where underperformance occurred and/or where shortcomings in performance reporting were identified.

Figure 9 shows the distribution of findings for the Free State.

**Figure 9: Percentage of findings per department**



Based on the findings raised on the annual performance reports in the aforementioned section, limited progress has been made by auditees to address the usefulness and reliability of their annual performance reports. This is due to a lack of effective oversight and monitoring by oversight departments. Although accounting officers/authorities are aware of the importance of valid, accurate and complete performance information, the responsible officials are not held accountable for failing to prepare credible performance information.

## 2.3 Compliance with key legislation

We annually audit and report on compliance with key legislation applicable to financial matters, financial management and other related matters.

We focused on the following areas in our compliance audits: ■ material misstatements in the submitted annual financial statements ■ asset and liability management ■ audit committee ■ budget management ■ expenditure management ■ unauthorised, irregular as well as fruitless and wasteful expenditure ■ consequence management ■ internal audit unit ■ revenue management ■ strategic planning and performance management ■ annual financial statements and annual report ■ transfer of funds and conditional grants ■ procurement and contract management (in other words, supply chain management) ■ human resource management and compensation.

In the audit report, we reported findings arising from the audits that were material enough to be brought to the attention of oversight bodies and the public.

## Status and findings on compliance with key legislation

Figure 10: Three-year trend – compliance with key legislation



Figure 10 shows that there has been no change in the number of auditees with no material findings on their compliance with key legislation when compared to the previous year. The Free State legislature has improved since the prior year to having no findings on compliance. However, the department of the Premier has regressed since the prior year.

Figure 11: Trends in findings on compliance with legislation

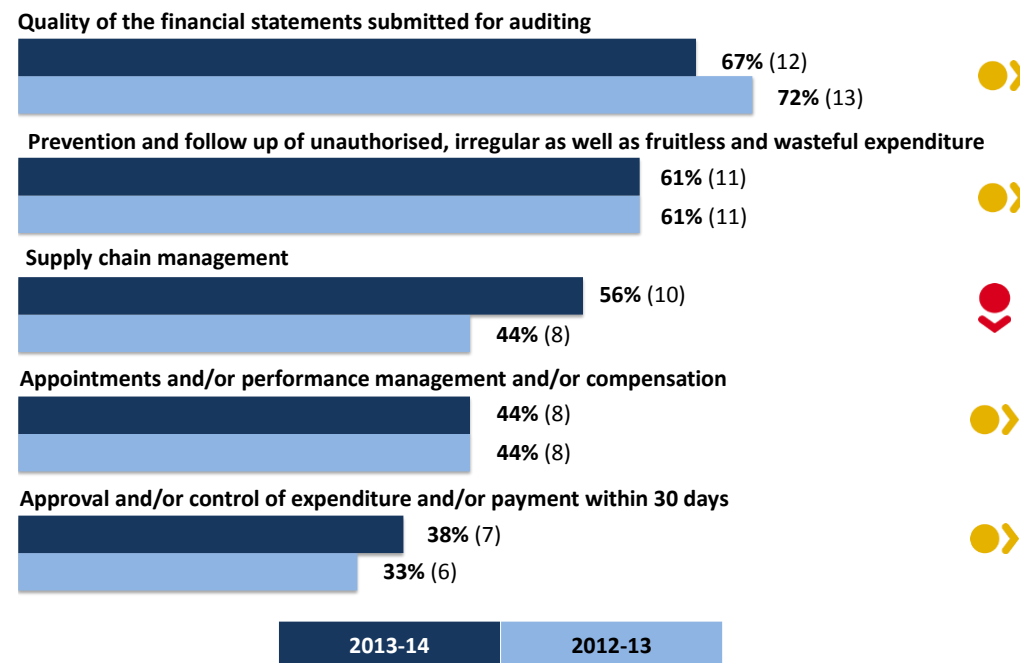


Figure 11 shows the top five compliance areas with the most material findings and the progress made by auditees in addressing these findings. There has been stagnation in the level of non-compliance with key legislation.

The most common findings across these compliance areas, as depicted in figure 11, as well as other prevalent findings, were the following:

- There were material misstatements or limitations in the financial statements submitted for auditing, as mentioned in section 2.1.
- Unauthorised, irregular and fruitless and wasteful expenditure was not prevented or adequately dealt with (refer to section 2.3.2 for more detail).
- Supply chain management legislation was not complied with (refer to section 2.3.1 for more detail).
- Funded vacant posts were not filled within 12 months (refer to section 4.1 for more detail).
- Payments to creditors were not made within 30 days from receipt of an invoice due to financial pressures experienced by the auditees.
- There were material findings relating to audit committees and internal audit, as mentioned in section 5.

- Effective steps were not taken to prevent overspending of the budget.
- Proper control systems were not implemented for safeguarding and maintenance of assets (refer to section 2.1 for financial statement qualifications on assets).
- Appropriate processes for identification, collection, recording, reconciliation and safeguarding of information about revenue were not in place.
- Appropriate measures were not taken to ensure that the receiving entity applied transfers for their intended purpose.

Sections 2.3.1 and 2.3.2 provide more information on supply chain management and unauthorised, irregular as well as fruitless and wasteful expenditure, followed by recommendations and best practices in section 2.3.3.

## 2.3.1 Supply chain management

As part of our audits of supply chain management, we tested 225 contracts (with an approximate value of R2,4 billion) and 1 037 quotations (with an approximate value of R88 million), also referred to as *awards* in this report.

We tested whether the prescribed procurement processes had been followed, which would have ensured that all suppliers were given equal opportunity to compete and that some suppliers were not favoured above others. We also focused on contract management, as shortcomings in this area can result in delays, wastage as well as fruitless and wasteful expenditure, which in turn have a direct impact on service delivery.

We further assessed the interests of employees of the auditee and their close family members in suppliers of the auditee. Legislation does not prohibit awards to suppliers in which employees or their close family members have an interest, but requires employees and prospective suppliers to declare such interest in order for safeguards to be put in place to prevent improper influence and an unfair procurement process.

We reported all the findings arising from the audit to management in a management report, while we reported the material compliance findings in the audit report.

Figure 12: Status of supply chain management

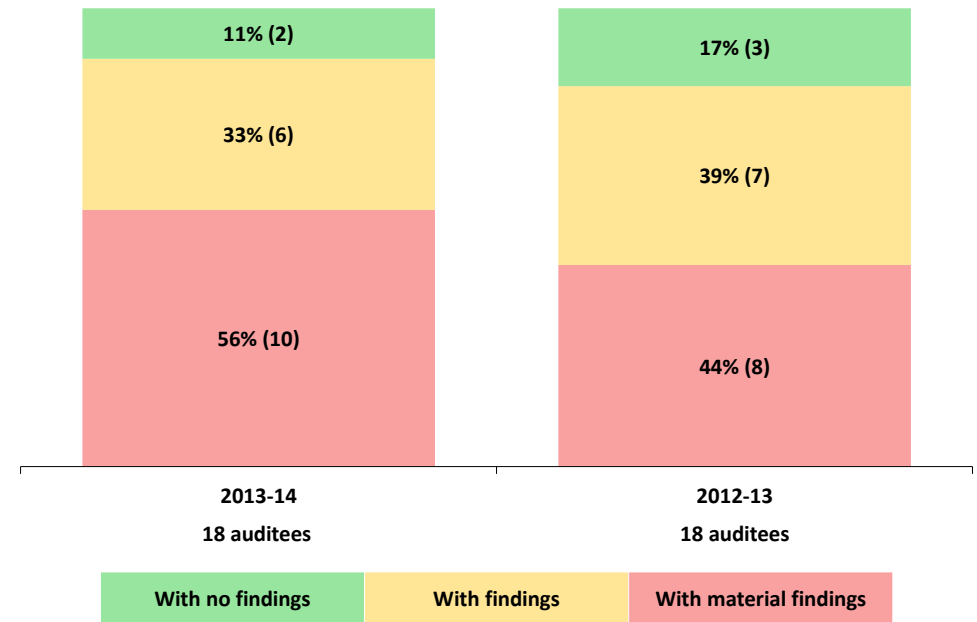


Figure 12 shows the number of auditees that had audit findings on supply chain management and those where we reported material compliance findings in the audit report in the current and previous years. It shows that there has been a regression when compared to the previous year. All departments and three of the public entities had findings on supply chain management. Only the Central Medical Trading Account and Fleet Management Trading Entity had no findings on supply chain management. Furthermore, it is of concern that more than half of the auditees had material findings on supply chain management. The departments of Public Works and Agriculture and Rural Development, as well as the Free State Development Corporation, regressed from having no material findings in the prior year to attracting material findings in the current year. Although not material, the Free State legislature had findings in the current year compared to no findings in the prior year; however, these findings did not result in irregular expenditure.

**Figure 13: Findings on supply chain management**

**Limitation on planned scope of audit of awards**

11% (2)      6% (1)



**Awards to employees**

17% (3)      22% (4)



**Awards to close family members of employees**

17% (3)      11% (2)



**Uncompetitive or unfair procurement processes**

22% (4)      50% (9)



**Inadequate contract management**

22% (4)      17% (3)



With findings

With material findings

Figure 13 indicates the extent of findings in the areas we report on and the movement since the previous year. The following were the most common findings:

- This year we again experienced limitations in auditing supply chain management. We could not audit awards with a value of R6,3 million at three auditees, as they could not provide us with evidence that awards had been made in accordance with the requirements of supply chain management legislation. We could also not perform any alternative audit procedures to obtain assurance that the expenditure incurred in this regard was not irregular. The main reason for the limitations was inadequate controls regarding recording keeping.
- There were 39 instances of awards with an overall value of R2 million to suppliers in which employees of eight auditees had a financial interest. In 51% of these instances, the employee did not declare the interest, while suppliers did not declare the interest or did not submit a declaration of interest in 46% of the cases. The persons involved included a member of the accounting authority as well as other employees not employed at senior management level.
- There were 108 instances of awards with an overall value of R16 million to suppliers in which close family members of employees of the auditees had an interest. In 78% of these instances, suppliers did not declare the interest or did not submit a declaration of interest. The employees did not declare the interest

in 47% of the cases. The persons involved included a member of the executive council where an instance was identified in which he had an indirect business relationship with the supplier, as well as a supply chain management official and other employees not employed at senior management level.

- The most common findings on uncompetitive and unfair procurement processes were as follows:
  - Three written quotations were not invited and the deviation was not approved at 10 auditees (56%).
  - The preference point system was not applied at seven auditees (39%).
  - Suppliers did not submit declarations of interest at six auditees (33%).
- The most common findings on contract management were the following :
  - Contracts were amended or extended without approval by a delegated official at five auditees (28%)
  - Lack of or inadequate contract performance measures and monitoring at four auditees (22%)
  - Payments made in excess of approved contract price (with further approved extensions) at one auditee (6%).

The following internal control deficiencies identified at auditees should be addressed to improve the status of supply chain management in the province:

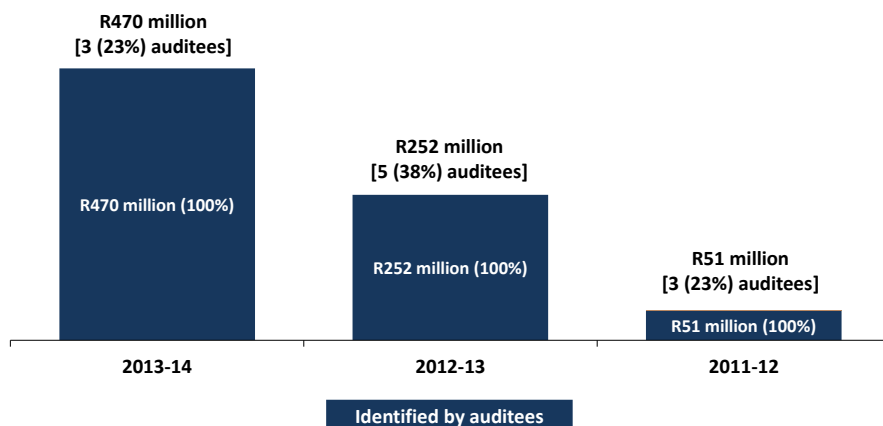
- Lack of controls and processes to ensure that staff and suppliers make declarations of interest during the procurement process.
- Supply chain management officials not adequately trained
- Supply chain management policies and procedures were in conflict with applicable legislation or did not include all the requirements.

## 2.3.2 Unauthorised, irregular as well as fruitless and wasteful expenditure

### Unauthorised expenditure

Unauthorised expenditure refers to expenditure that was not incurred in accordance with the approved budget. The PFMA requires accounting officers to take all reasonable steps to prevent unauthorised expenditure. The auditee should have processes in place to identify any unauthorised expenditure that was incurred and disclose the amounts in the financial statements. The PFMA also includes the steps that accounting officers and oversight bodies should take to investigate unauthorised expenditure to determine whether any officials are liable for the expenditure and to recover the money if liability is proven. In terms of the PFMA unauthorised expenditure is only applicable to departments and not to public entities.

**Figure 14: Trend in unauthorised expenditure**



Unauthorised expenditure of R470 million incurred in 2013-14 was due to overspending of the budget. There was a significant year-on-year upward trend in unauthorised expenditure, which increased by 87% in the current year compared to the previous year.

The departments of Health and Education were responsible for 98% of the unauthorised expenditure. Education incurred unauthorised expenditure of R427 million, which represents an increase of R348 million (441%) since the prior year.

This was mainly as a result of under-budgeting for employee cost, as well as a lack of daily and monthly disciplines to monitor the spending against the budget. The unauthorised expenditure incurred by Health decreased by R103 million (76%) since the prior year as stricter budget controls were implemented, but they still could not manage to prevent unauthorised expenditure of R33 million.

The significant unauthorised expenditure incurred by these leading service delivery departments puts further pressure on the severe cash flow constraints experienced by the province as detailed in section 3 on financial health.

It is of concern that management detects but does not prevent unauthorised expenditure.

Daily and monthly disciplines need to be implemented and monitored to ensure that effective cash flow and budget management can occur to prevent unauthorised expenditure.

### Irregular expenditure

Irregular expenditure refers to expenditure that was not incurred in the manner prescribed by legislation. Such expenditure does not necessarily mean that money had been wasted or that fraud had been committed, but is an indicator that legislation is not being adhered to, including legislation aimed at ensuring that procurement processes are competitive and fair. It is also an indicator of a significant breakdown in controls at some auditees.

The PFMA requires accounting officers to take all reasonable steps to prevent irregular expenditure. Auditees should have processes in place to detect non-compliance with legislation that results in irregular expenditure and, if incurred, such amounts should be disclosed in the financial statements. Irregular expenditure must be reported when it is identified – even if such expenditure was incurred in a prior financial year.

**Figure 15: Auditees incurring irregular expenditure**

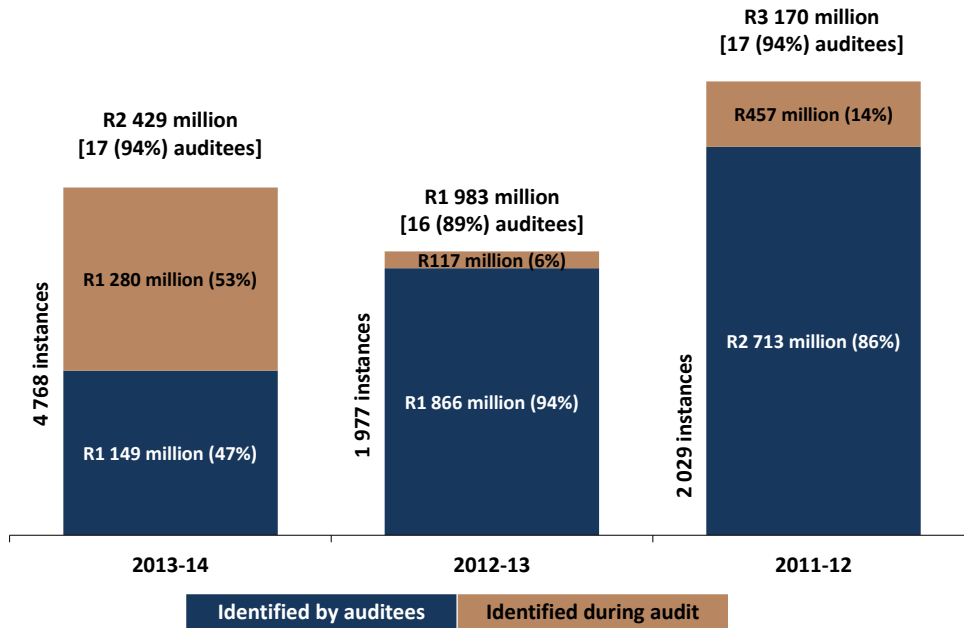


Figure 15 shows that irregular expenditure in the province remains at a very high level and had increased by R446 million (22%) since the prior year. All auditees, except the Free State legislature, incurred irregular expenditure. This means that the other three auditees with clean audit outcomes (i.e. the provincial treasury, Sport, Arts Culture and Recreation and the Fleet Management Trading Entity) also incurred irregular expenditure, although it was not significant enough to affect the audit report.

The major contributors were the departments of Health (R1,1 billion), Human Settlements (R858 million) and Education (R269 million), which represent 92% of the total irregular expenditure. This is of concern as the departments of Health and Education received the largest portion of the budget allocation (67%) in the province. Health's irregular expenditure increased by R959 million (666%) since the prior year. This was mainly due to an attempt to address the prior year qualification on irregular expenditure; however, they were still unable to avoid a qualification in the current year due to more irregular expenditure being identified during the audit which the department did not account for.

Figure 15 also shows that more than half of the irregular expenditure incurred in the province was identified during the audit, which is an indication that adequate processes are not in place to firstly prevent and then to detect irregular expenditure. The problem of auditees not having a system in place to identify irregular expenditure and therefore often relying on the auditors to identify irregular

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expenditure, is not sustainable and places undue pressure on audit fees and reporting deadlines.

The significant increase in the value of irregular expenditure identified by the auditors occurred at the departments of Health, Human Settlements and Education. This is mainly because of incorrect interpretation of supply chain management requirements and irregular expenditure guidelines as well as resistance by management to acknowledge that significant contracts were irregular and therefore to disclose such expenditure as irregular expenditure.

**Figure 16: Prior year irregular expenditure identified in the current year**

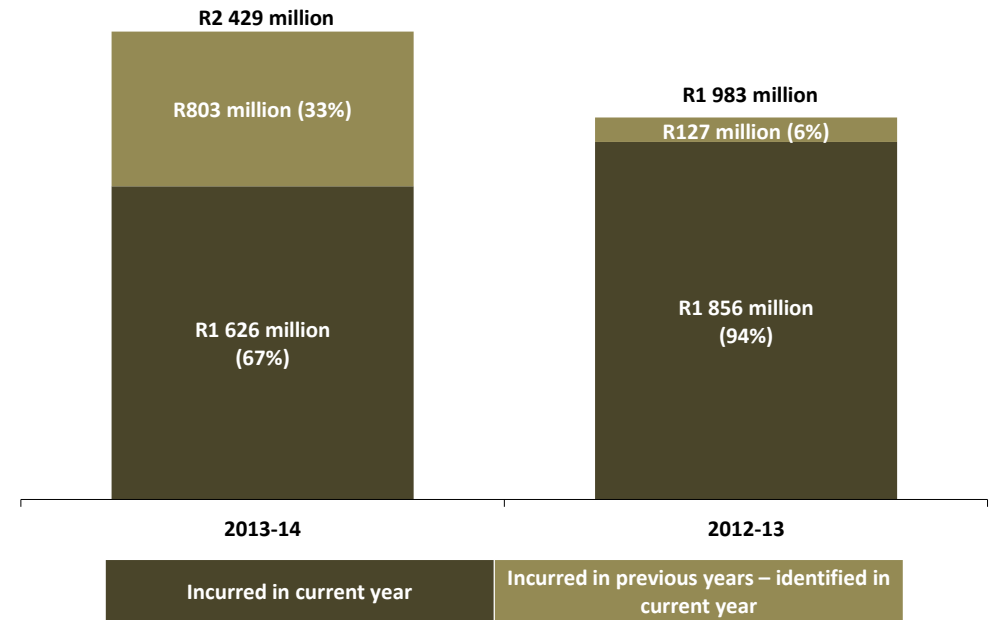


Figure 16 shows that 67% of the expenditure was the result of instances of non-compliance in 2013-14; the remainder was expenditure resulting from transgressions in previous years. The department of Health was responsible for R731 million (91%) of the irregular expenditure incurred in the previous year but identified in the current year. This relates to irregular expenditure identified by the auditors in previous years but not disclosed as irregular expenditure as the department had to investigate the full extent thereof. During the current year a number of the instances were disclosed after investigation by management and where they did not do so, it contributed to Health's qualification on irregular expenditure.



Of the R2,429 billion in irregular expenditure incurred in 2013-14, most was as a result of non-compliance with supply chain management legislation amounting to R1,978 billion (81%). Irregular expenditure relating to employee cost was R169 million (7%) while other non-compliance amounted to R282 million (12%).

The following were the main areas of non-compliance with supply chain legislation, as disclosed by the auditees in their financial statements, with an indication of the estimated value of the expenditure:

- Procurement without following a competitive bidding or quotation process – R717 million (36%)
- Non-compliance with procurement process requirements – R947 million (48%)
- Non-compliance with legislation on contract management – R61 million (3%)
- Approval of payments not according to the approved delegations of authority – R253 million (13%)

The following is an analysis of the most significant irregular expenditure incurred by the departments of Health, Education and Human Settlements:

- The department of Health incurred irregular expenditure of R162 million relating to employee cost. This was due to overspending of the employee cost budget during 2011-12 and 2012-13, as well as overtime payments made to dentists and doctors not entitled to such payments.
- The department of Health also incurred other irregular expenditure of R281 million which was as a result of budget constraints, where the department made payments from the conditional grant funds which were not in accordance with the conditions of the grant. In addition, schedule 5 and 6 transfers in terms of the Division of Revenue Act (DoRA) were made without an approved business plan for utilisation of the funds by the relevant municipalities.
- The department of Health incurred irregular expenditure of R660 million due to non-compliance with supply chain legislation. This was mainly because payments were not always approved in accordance with the department's finance delegations as the positions that should have approved the payments were vacant at the institutions or because of the unavailability of chief executive officers and other senior officials at the hospitals. The department also entered into contracts where the bidding process could not be regarded as fair, equitable, transparent, competitive and cost-effective.
- The department of Human Settlements incurred irregular expenditure of R857 million due a lack of fair, equitable, transparent, competitive and cost-effective procurement processes for housing contracts.
- The irregular expenditure of R269 million incurred by the department of Education was as a result of a high number of incidents of non-compliance with supply chain management requirements due to a weak control environment and lack of oversight by the leadership. Irregular expenditure of approximately R90 million included in the R269 million was also incurred on

infrastructure procured by the department of Public Works on behalf of Education.

The main reason for incurring irregular expenditure is that credible procurement plans are not developed, which then filters through to project plans. Auditees therefore do not follow adequate procurement processes, which results in crisis management, e.g. invalid deviations to utilise all funds before year-end in a bid to avoid surrendering unspent funds. As a result, there was a lack of transparency during procurement processes which hampered the competitiveness thereof.

The departments of Agriculture and Rural Development, Health, Education, Economic Development, Tourism and Environmental Affairs and Public Works disclosed in their financial statements that they still have to investigate the whole population to determine the full extent of irregular expenditure. This is an indication that irregular expenditure may have been significantly higher had these amounts been disclosed.

There is an increasing trend where auditees employ the strategy of delegating their functions to another entity, appointing them as implementing agents. Fair, equitable and transparent procurement processes are not always followed to appoint these implementing agents. Furthermore, once payments are made no further monitoring is done by auditees to ensure that fair, equitable and transparent procurement processes are followed by the implementing agents so that the best price is paid when they spend money on behalf of the auditee. The use of implementing agents is especially of concern in light of the poor financial health of the province since the best prices are not always paid for goods and services. In addition, management fees have to be paid although more than half (57%) of the provincial budget is already spent on employee cost, while it is expected that government employees should perform the duties delegated to implementing agents. This matter is currently disclosed as possible irregular expenditure under investigation at the departments of Agriculture and Rural Development, Education and Economic Development, Tourism and Environmental Affairs.

The PFMA provides for steps that accounting officers should take to investigate irregular expenditure to determine whether any officials are liable for the expenditure and to recover the money if liability is proven. The investigation should also confirm whether fraud had been committed or money had been wasted because goods and services were not received or were not procured at the best price. Irregular expenditure incurred remains in the auditee's financial statements until it is recovered if liability is proven, or written off as not recoverable or condoned by a relevant authority (mostly the National Treasury).

At 31 March 2013 the auditees' financial statements showed that the balance of irregular expenditure in the province that required action to be taken was R3,619 billion. It is of concern that in 2013-14 irregular expenditure of R47 million relating to the prior year had still not been dealt with as required by legislation, resulting in an accumulative balance of R5,623 billion at the end of the 2013-14 financial year to be investigated. The balance of R5,623 billion excludes an uncorrected misstatement of R378 million relating mainly to the department of Health, which

would also need further attention in the next financial year. Consequently, auditees did not determine whether the irregularities constituted fraud or whether any money had been wasted. We did not perform any investigations into the irregular expenditure as this is the role of the accounting officer and oversight body.

Through our normal audits we determined that goods and services were received for R936 million (47%) of the irregular expenditure relating to non-compliance with supply chain management legislation despite the normal processes governing procurement not being followed. We are, however, not in a position to determine whether any money was wasted or if a fair price had been paid for these goods and services. This is the responsibility of management as indicated in the previous paragraph.

For the remainder of the amount (R1 042 million – 53%) of irregular expenditure relating to supply chain management we could not specifically confirm that goods and services were not received. However, no material risks were identified for goods and services paid for but not received.

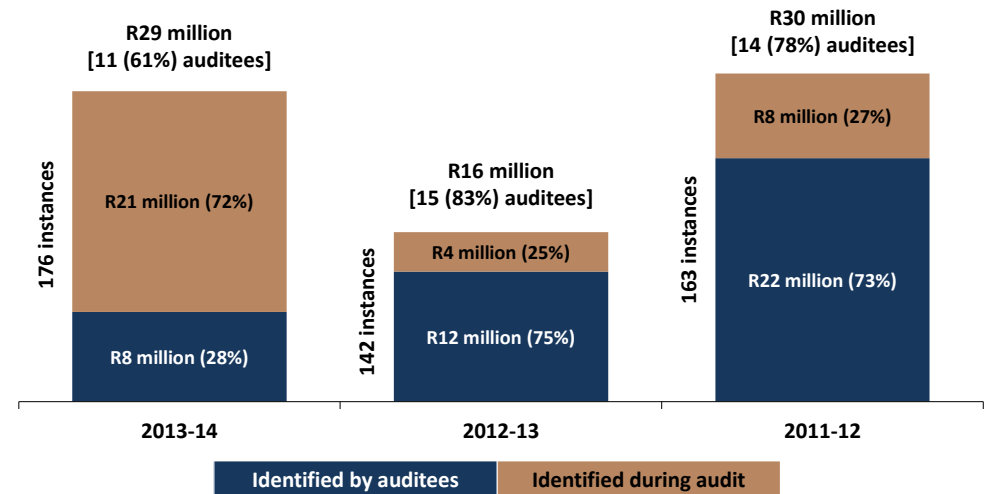
The high occurrence of irregular expenditure year-on-year is an indication of a general lack of consequences for officials responsible for incurring irregular expenditure. At 56% of auditees no steps were taken to implement consequences for poor performance or non-compliance with legislation. Leadership should give serious attention to investigating irregular expenditure already incurred and to preventing further irregular expenditure. The significant irregular expenditure incurred in the province caused by non-compliance with supply chain management requirements is one of the main reasons why auditees are unable to move towards clean audit outcomes. There is also an ongoing need for oversight role players to ensure that accounting officers and senior management are held accountable for providing the desired level of assurance that will maintain the momentum towards improved audit outcomes.

### Fruitless and wasteful expenditure

Fruitless and wasteful expenditure refers to expenditure that was made in vain and that would have been avoided had reasonable care been taken.

The PFMA requires accounting officers to take all reasonable steps to prevent fruitless and wasteful expenditure. The auditees should have processes in place to detect fruitless and wasteful expenditure and, if incurred, to disclose the amounts in their financial statements. Fruitless and wasteful expenditure must be reported when it is identified – even if the expenditure was incurred in a previous financial year.

Figure 17: Trend in fruitless and wasteful expenditure



Fruitless and wasteful expenditure increased by 81% since the previous year. The auditees were able to identify most of the fruitless and wasteful expenditure through their own processes during the previous two financial years. However, during the current year 72% of the fruitless and wasteful expenditure was identified during the audit, which is an indication that the systems in place to prevent and detect fruitless and wasteful expenditure are not effective. Management has not implemented systems and controls to prevent fruitless and wasteful expenditure and subsequently to detect it after payments have been made.

The major contributors to fruitless and wasteful expenditure were Health (R12,5 million) and the Free State Tourism Authority (R9,7 million). This is further analysed below.

The nature of the fruitless and wasteful expenditure incurred was as follows:

- Interest was paid on overdue accounts to the amount of R10 million (34%). The department of Health paid R8 million in interest due to cash flow problems and an inability to meet its obligations as they fall due, as further highlighted in section 3 on financial health.
- The Free State Tourism Authority incurred fruitless and wasteful expenditure of R9,7 million (33%) due to payments made to host an event that never took place, as well as expenditure incurred on an overseas trip by a number of the entity's officials.

- The remaining 33% of fruitless and wasteful expenditure relates to expenditure made in vain as the goods or services were not delivered or not utilised by the auditees, salary-related payments made to employees not entitled to such payment and penalties.

The PFMA provides for the steps that accounting officers should take to investigate the fruitless and wasteful expenditure to determine whether any officials are liable for the expenditure and to recover the money if liability is proven.

Auditees should ensure that the instances of fruitless and wasteful expenditure are investigated and that consequence management is enforced to ensure that officials are held accountable for expenditure made in vain.

### 2.3.3 Recommendations – compliance

Auditees that had findings on compliance with key legislation and supply chain management and those that incurred unauthorised, irregular as well as fruitless and wasteful expenditure should strengthen their processes and controls to create and/or sustain a control environment that supports compliance. For such auditees we recommend the implementation of best practices that are in place at those auditees that did not have material findings on compliance with laws and regulations. The best practice relates to ongoing review and monitoring of internal controls relating to compliance with legislation. Where a control has been found to have failed, the entire process and relevant control should be reviewed. This process of review should include both internal and external consultation. In addition, the following controls should be implemented:

- Daily and monthly controls around the prevention and detection of unauthorised, irregular and fruitless and wasteful expenditure should be improved. Management should consider all contracts that were found to be irregular to determine whether these contracts can be cancelled and new procurement processes followed.
- All instances of unauthorised, irregular and fruitless and wasteful expenditure should be investigated timeously to identify the responsible person, and there should be consequences for incurring this type of expenditure.
- Oversight of implementing agents should be improved to ensure that government funds are spent in a manner that is fair, equitable, transparent and cost-effective.

Keeping up to date with legislation, as well as regular monitoring of compliance, is an important step in ensuring that non-compliance with legislation is avoided. Having good internal controls surrounding compliance will also enable the auditee to avoid compliance findings. Without proper controls, an auditee may address a specific issue in a particular year, but the absent control will often result in the finding recurring in a future year.

In conclusion, it is recommended that urgent attention be given to ensure that responsible staff members are properly trained on supply chain management legislation and that they are held accountable for any transgressions identified. Performance and consequence management must be enforced to ensure that officials are held accountable for public funds entrusted to them.

## 3. Financial health

Our audits included a high-level analysis of departments' financial indicators to provide management with an overview of selected aspects of their current financial management and to enable timely remedial action where the departments' operations and service delivery may be at risk. We identified financial sustainability concerns at the departments of Agriculture and Rural Development, Education, Health, Police, Roads and Transport, Public Works, Social Development and Sport, Arts, Culture and Recreation.

We also performed procedures to assess whether there are any events or conditions that may cast significant doubt on a public entity's ability to continue as a going concern. We identified a going concern risk at the Central Medical Trading Account and Free State Tourism Authority due to material uncertainties relating to events or conditions which may cast significant doubt on their ability to meet their financial obligations as they fall due and to achieve service delivery as outlined in their annual performance plan.

Figure 18: Status of financial health

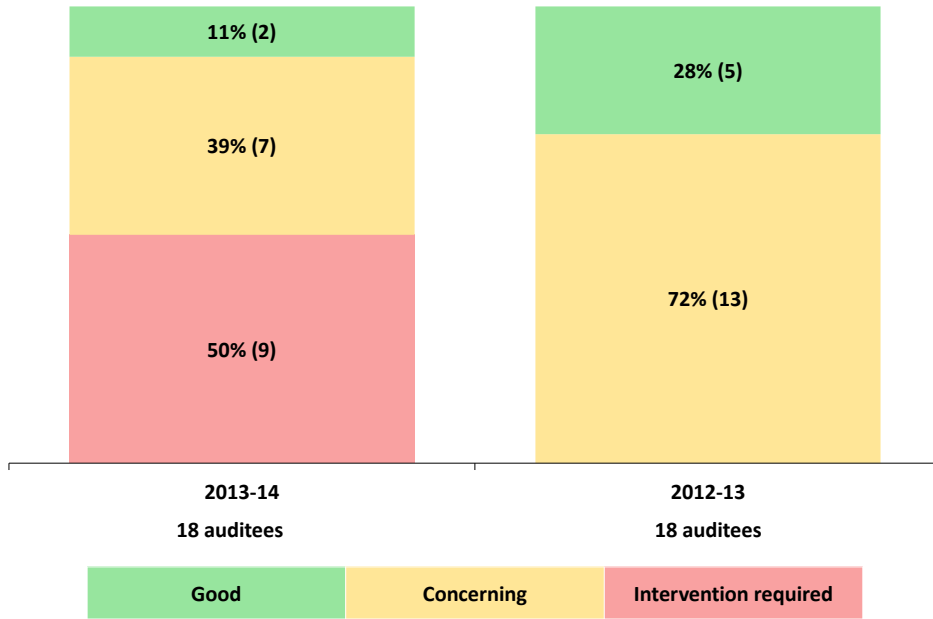
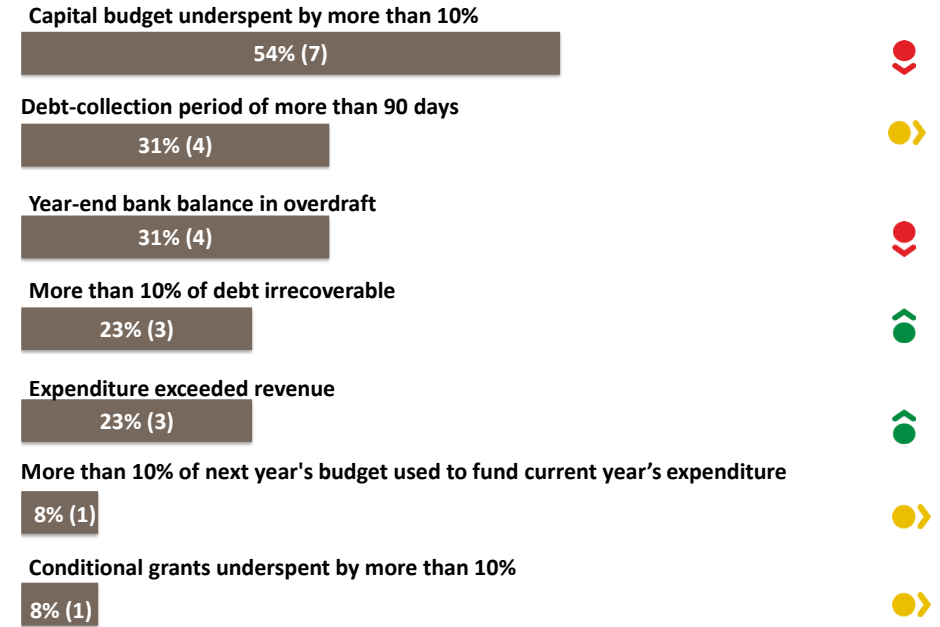


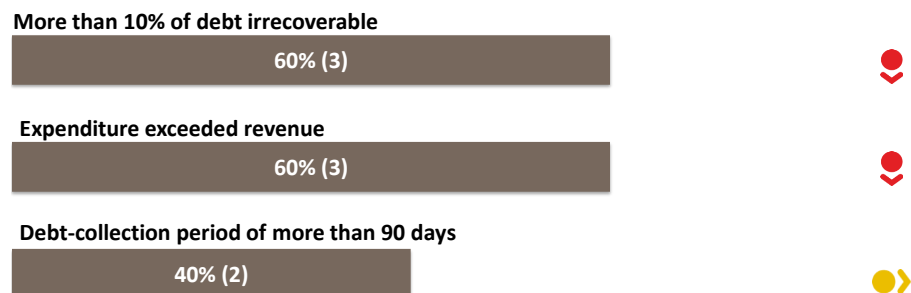
Figure 19: Areas of financial health concerns – departments



34

Figure 18 indicates the number of auditees that had more than two of the financial risk indicators (shown as 'concerning') and auditees with material going concern uncertainties (public entities) or with significant financial sustainability uncertainties (departments) (shown as 'intervention required'). There has been a significant regression in the number of auditees with financial risk indicators when compared to the previous year.

**Figure 20: Areas of financial health concerns – public entities**



Figures 19 and 20 show the number of auditees with these indicators and the movement since the previous year. These indicators are discussed in the rest of this section.

### Financial management by departments

Departments prepare their financial statements on the modified cash basis of accounting. This means that the expenditure disclosed in the financial statements is only what was paid during the year and does not include accruals (the liability for unpaid expenses) at year-end. As part of the financial health analyses, we reconstructed the financial statements to determine whether these departments would still have had surpluses for the year had these expenses been included in their financial statements. We also assessed the impact of the unpaid expenses at year-end on the following year's budget. The analysis below excludes the Free State legislature as they are not required to surrender unspent funds to the Revenue Fund.

The financial sustainability of departments and public entities is an area of grave concern due to, inter alia, the following:

- At 31 March 2014, the bank balances for departments as disclosed in the financial statements were in overdraft to an amount of R23 million. This was after a cash injection of R692 million to the province in March 2014.
- At 31 March 2014, funds to be surrendered amounted to R606 million. This amount excludes R236 million that had been approved for roll-over at Police, Roads and Transport.
- Accruals older than 30 days amounted to R976 million. These amounts are overdue and should have been paid.
- Of the amount of R976 million, R856 million (88%) relates to accruals of the departments of Education and Health.

- Taking into account the overdraft, funds to be surrendered and long-outstanding accruals, the province requires R1,6 billion to clear the backlog.
- The total provincial budget for 2014-15 is R27,7 billion. Of this, R18 billion (65%) is for salaries. Therefore only R9,7 billion remains for goods and services and other service delivery such as capital expenditure.
- Since R1,6 billion of the remaining budget will need to be used to fund the backlog, only R8 billion (29%) of the budget will be available for service delivery in the 2014-15 year.

Based on the *Medium-term expenditure framework* (MTEF) that has been published, the total budget for the province increases by 7,73% from R27,7 billion in 2014-15 to R29,9 billion in 2015-16 but then by only 0,44% to R30 billion in the 2016-17 financial year.

With inflation currently at approximately 6%, which is close to the budgeted increase in the budget for the 2014-15 fiscal year and exceeds the increase in budgeted income for the 2015-16 fiscal year, it will be increasingly difficult to improve the financial position of the province since expenses are increasing more rapidly than income.

As reported in the general report for the 2012-13 MFMA cycle, local government finds itself in a net current liability position of R2 billion. Further financial pressure will be placed on the provincial budget as assistance will be sought by municipalities to alleviate their financial distress. A contributing factor is that approximately R200 million is owed by the department of Public Works to municipalities for services rendered on provincial government buildings.

The financial distress at municipal level continues during 2013-14 as Eskom is owed more than R1 billion. There is a real threat that certain municipalities may have their electricity disconnected due to non-payment unless assistance is provided by the province.

### Underspending by departments of capital budgets

Seven departments underspent their capital budgets by more than 10%. A matter of concern is that this includes departments responsible for significant service delivery such as Police, Roads and Transport - R263 million (20,3%), Health - R164 million (23,7%) and Education - R78 million (18,7%). This is also an indicator of the financial difficulties in which departments find themselves as capital expenditure is used to fund operating expenditures due to cash flow constraints. This contributes to the amount of irregular expenditure in the case of conditional grants, or unauthorised expenditure with regard to normal capital expenditure.

### Debt management

There has been no improvement in debt management at departments. The following departments have not collected amounts owed to them within 90 days:

Agriculture and Rural Development, Economic Development, Tourism and Environmental Affairs, Health and Police, Roads and Transport.

For Agriculture and Rural Development, Economic Development, Tourism and Environmental Affairs and Police, Roads and Transport these financial difficulties are exacerbated by the fact that more than 10% of amounts receivable is deemed to be irrecoverable.

## Recommendations

As indicated in 2.3.2, departmental budgets are being overspent by R470 million. When this is coupled with the increase in irregular expenditure and the resistance by management to acknowledge that significant contracts were irregular and therefore to disclose it as irregular expenditure, it is not possible to determine whether they had received the best value for money.

This results in additional pressure on the financial health of auditees at a provincial level. To address these shortcomings, the following controls should be implemented:

- All contracts should be revised to determine whether value for money is received.
- Contracts to be monitored rigorously, with penalty clauses for non-performance in terms of the agreement used where necessary.
- Steps should be implemented to ensure that all new contracts are to the benefit of the province.
- Rigorous cash flow mechanisms to be implemented to ensure that critical projects and services are prioritised. Spending on items that do not relate to critical services and programmes should cease immediately, e.g. budgeting for critical goods and services instead of expenditures which is not related to the core mandate of departments.
- The province should avoid using implementing agents and should rather ensure that government employees perform the duties for which they are being paid to prevent the payment of unnecessary management fees. Where implementing agents are used they should follow the procurement processes of government to ensure fair, equitable and transparent procurement of goods and services.

## Financial management by entities

Only the Free State Tourism Authority and Central Medical Trading Account had material findings on financial health. The regression in the financial health of the other entities is an area of concern and should be closely monitored by the provincial departments responsible for them.

## 4. Internal controls and root causes

As part of our audits, we assessed auditees' internal controls to determine the effectiveness of their design and implementation in ensuring reliable financial and performance reporting and compliance with key legislation.

Figure 2 shows the status of the different areas of internal control and the overall movement since the previous year. There has been stagnation in key controls from the prior year to the current year. In sections 2.1 (quality of financial statements), 2.2 (quality of annual performance reports and 2.3 (compliance with legislation) we commented broadly on those key controls that should receive attention to improve or sustain the audit outcomes.

Figure 21 shows the status of the controls requiring most attention.

Figure 21: Key controls requiring the most attention

	Audit areas								
	Financial statements			Performance reports			Compliance with legislation		
Effective leadership	12	5	1	12	4	2	12	3	3
Human resources controls	7	8	3	7	7	4	4	5	9
ICT governance and controls	3	13	2	5	8	5	4	10	4
Audit action plans	7	7	4	7	9	2	7	6	5
Proper record keeping	6	8	4	3	13	2	6	8	4
Daily and monthly controls	6	10	2	7	9	2	8	6	4
Review and monitor compliance	4	4	10	6	4	8	3	3	12

Good	Concerning	Intervention required
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The key control area requiring the most attention is the review and monitoring of compliance at financial statement level, the annual performance reports as well as compliance with legislation. The lack of adequate controls in this area is evident in the high occurrence of compliance findings as detailed in section 2.3.

The slow but steady improvement in audit outcomes is not aligned to an improvement in key controls (which shows stagnation). This questions the sustainability of the audit outcomes achieved. The key control assessments over the past few years indicate that management does not take ownership of the

process as limited or no improvements are seen in internal controls from year to year. One of the main reasons is that management does not implement the recommendations of the internal audit and audit committee.

Sections 4.1 and 4.2 provide further information on the status of human resource controls and the information and communication technology (ICT) governance and controls. The effectiveness of internal control is significantly impacted by root causes. Section 4.3 describes the most common root causes that should be addressed.

Audit action plans should not be a long list of responses to each and every audit finding reported to management. Action plans should be restricted to the real root causes of the problem. By implication, auditees should aim for one-page documents, stating clearly who is held responsible for which sections of the action plan, and should also have predetermined follow-up dates when responsible persons will report on their progress and be held accountable for it. Some auditees have very good action plans in place, but simply do not regularly monitor the implementation thereof or hold people accountable for not doing their part. Accountability and consequence management are key to successful implementation of action plans.

The basic daily and monthly key controls are still not in place at all auditees, resulting in material misstatements in the financial statements, findings on performance information and non-compliance with legislation.

Another very important matter is that of compliance with legislation. Leadership should set the tone by stressing that compliance with legislation is embedded in the entity's values and set a zero tolerance for irregular expenditure. MECs and heads of department should assume the lead, not only with words, but more importantly by example.

## 4.1 Human resource management

Human resource management is effective if adequate and sufficiently skilled staff members are in place and if their performance and productivity are properly managed.

Our audits included an assessment of human resource management that focused on the following areas: ■ Human resource planning and organisation ■ management of vacancies ■ appointment processes ■ performance management ■ acting positions ■ management of leave, overtime and suspensions.

Our audits further looked at the management of vacancies and stability in key positions, competencies of key officials and performance management and consequences for transgressions, as these matters have a direct bearing on the quality of auditees' financial and performance reports and compliance by them with legislation.

Based on the results of these audits, we assessed the status of human resource management controls.

**Figure 22: Status of human resources management**



Figure 22 shows that there has been no improvement in the status of human resource management when compared to the previous year. Intervention is required at five auditees (28%), while the status of human resource management is still a concern at seven auditees (39%). This indicates that the matters of concern raised in the prior year have not been addressed and that inadequate attention was given to matters relating human resources.

## Management of vacancies and acting positions

Figure 23: Vacancies in key positions

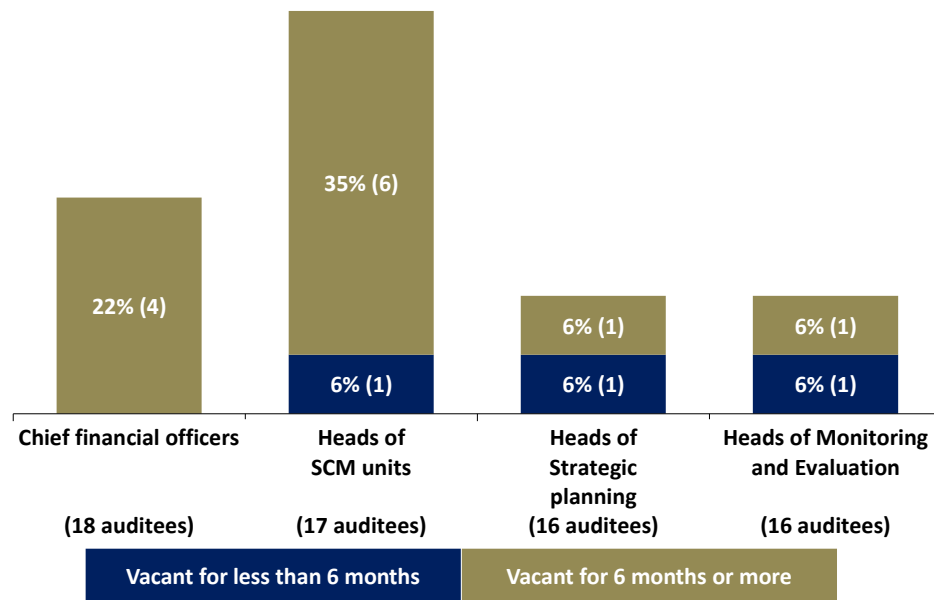


Figure 24: Stability in key positions (average number of months in position)

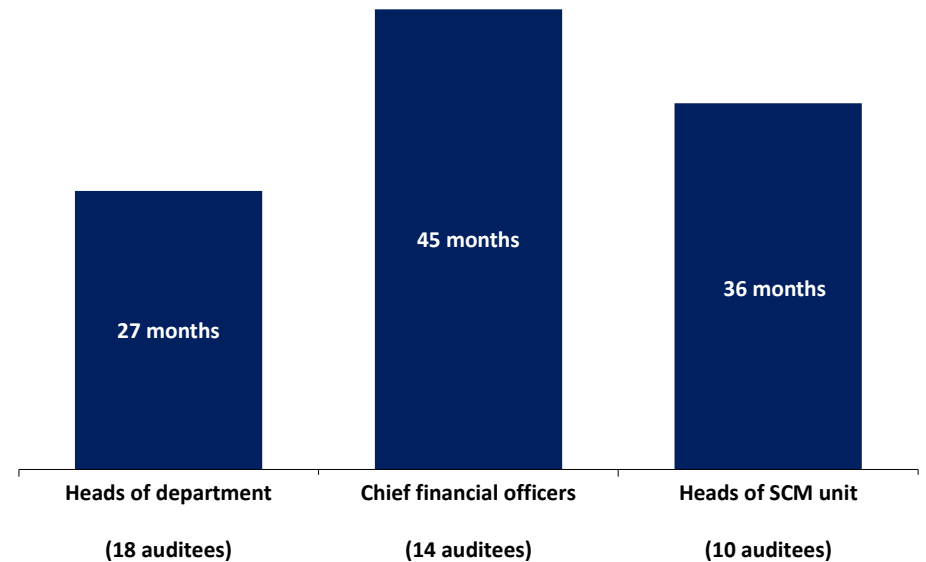


Figure 23 shows the number of auditees where the positions of the chief financial officer and heads of the supply chain management unit, strategic planning or monitoring and evaluation were vacant at year-end and also indicates the period that the positions had been vacant. Figure 24 shows the average number of months that key officials had been in their positions.

There were no vacancies at year-end in the position of accounting officer (head of department or chief executive officer). Although there were no significant vacancies and instability in the positions of accounting officer, chief financial officer and heads of supply chain management units, strategic planning or monitoring and evaluation, the vacancies and instability in the positions supporting these individuals are of concern. This was identified as one of the main root causes of audit findings, as further detailed in section 4.3, which resulted in material misstatements in the financial statements, supply chain management weaknesses and findings relating to the reporting of predetermined objectives. Contract end dates and the subsequent renewal thereof have an impact on positions filled. If not managed properly, it can have a negative impact on the departments' performance, the audit process and ultimately also on the audit outcome.

Findings were raised on the management of vacancies and acting positions at nine auditees (50%). The most common findings related to the increase in the overall



vacancy rate since the prior year and senior management positions that were vacant for more than 12 months.

## Performance management

In order to improve the performance and productivity of staff, the leadership should set the correct tone by implementing sound performance management processes, evaluating and monitoring performance, and consistently demonstrating that poor performance has consequences.

At 28% of the auditees, a number of senior managers did not have performance contracts or the contracts had not been signed early enough.

## Competencies of key officials/ consequences for transgressions

The lack of appropriate competencies of key officials was identified as one of the root causes of the slow progress towards clean audit outcomes at 67% of the auditees as detailed in section 4.3. At eight auditees proper appointment processes were not followed, which could result in auditees not appointing officials suitable for the position. The general weaknesses in the appointment processes include appointments made in posts that were not advertised, appointees without the required qualifications, prescribed selection and approval processes not being followed as well as verification processes not followed for new appointments.

In addition, there is a lack of consequences at 56% of auditees. The leadership did not always hold staff accountable for poor performance and transgressions, which creates the perception that these results are acceptable and tolerated. The impact of the lack of appropriate competencies and lack of consequences for poor performance is evident in the outcomes in the following areas:

- Recurring poor quality of annual financial statements, as reported in section 2.1.
- Recurring poor quality of the annual performance reports and high occurrence of findings on performance information, as reported in section 2.2.
- Recurring non-compliance with laws and regulations as well as supply chain management regulations. Significant unauthorised, irregular and fruitless and wasteful expenditure was incurred, as reported in section 2.3.
- Government funds are not properly managed, resulting in the poor state of financial health of the province, as reported in section 3.

It is, however, commendable that some auditees took action and started implementing consequences. At the departments of the Premier and Public Works as well as the Free State Development Corporation it was evident that consequences were implemented as action was taken against officials who did not perform their functions as expected or were responsible for incurring significant irregular expenditure.

## Other common human resource findings

The other most common human resource findings were the following:

- An approved human resource plan based on the strategic plan was not in place.
- Proper verification processes for new appointments were not always followed or the process did not cover all the verifications prescribed.
- Employees received more incapacity leave days than they were entitled to.
- Medical certificates not submitted for sick leave.

## Effective use of consultants by departments

Provincial departments spent an estimated total of R397,4 million (2013: R326 million) on consultancy services in 2013-14 to supplement their human resources. Consultancy services are services of an intellectual or advisory nature. The amount was spent by departments in the following areas:

- Financial reporting, including the preparation of the financial statements or assistance with the fixed asset register – R20,6 million (2013: R22 million).
- IT related services – R3,7 million (2013: R32 million).

A total of R373,1 million (2013: R272 million) was spent on other consultants, which mainly include specialist services, consulting firms, engineering firms and outsourced services. This amount includes R63 million for design, construction and project management for low-volume roads in terms of the township revitalisation programme; R26 million for management of infrastructure projects; R16 million for the appointment of casual labourers for operation Hlasela at the department of Public Works; R52 million for infrastructure and planning at Human Settlements; catering services for public hospitals of R63 million at Health; and approximately R36 million spent by CoGTA on consultants to assist municipalities with financial reporting. The most common reason why departments appoint consultants was a lack of skills within the department as well as vacancies.

Our audits included an assessment of the management of the consultants at 10 of the departments. Three departments did not make use of consultants during 2013-14, namely the department of the Premier, Free State legislature and Social Development. The following are our key findings on the **planning and appointment processes**:

- As with all other procurement, consultants should be contracted based on a needs assessment. Such assessment should consider cost, type and extent of service, the deliverables and whether internal capacity exists and/or there is an opportunity for the transfer of skills. At three auditees (30%) the consultants were appointed without conducting a needs assessment.

- As part of the bidding process, there should be terms of reference that clearly define what will be required from the consultant and specify the required experience and qualifications. At two auditees (20%) the consultants were appointed without terms of reference and at one auditee (10%) the terms of reference were inadequate.

We identified shortcomings in the **management and monitoring of performance** of the consultants. The measures to monitor the performance of the consultants were not defined at three auditees (30%). At three auditees (30%) the measures used to monitor delivery by the consultants were inadequate. Of greater concern was the payment of consultants without signed contracts at two auditees (20%).

Although one of the most common reasons for appointing consultants was a lack of skills, we found that the contracts at five auditees (50%) did not include any conditions or objectives in terms of the **transfer of skills** from the consultants to the employees. At the auditees where the transfer of skills was a requirement the measures to monitor the transfer of skills were not implemented at six auditees (60%). Furthermore, no evaluation on the transfer of skills was performed at the end of the consultancy project at five (50%) auditees.

In addition to poor project management, the root cause of these findings was the lack of policies or strategies on the use of consultants identified at three auditees (30%). A policy or strategy should be in place that defines the main purpose and objectives of appointing consultants and should include measures to prevent over-reliance on consultants.

## 4.2 Information technology controls

IT controls ensure the confidentiality, integrity and availability of state information, enables service delivery and promotes national security. It is thus essential for good IT governance, effective IT management and a secure IT infrastructure to be in place.

Effective **IT governance** is essential for the overall well-being of an organisation's IT function and ensures that the organisation's IT control environment functions well and enables service delivery. All state departments and public entities are therefore required to adopt and implement the IT governance framework and guidelines developed by the department of Public Service and Administration (DPSA) in phases over a period of three years. Phase 1 was due for implementation by the end of the 2013-14 financial year. The DPSA moderated the Management Performance Assessment Tool (MPAT) self-assessment results to monitor progress made with implementation. The implementation of phase 1 will be evaluated in the following audit cycle. In the 2014-15 financial year the implementation of phase 2 should be prioritised by the accounting officers and governance champions.

As the legislatures have opted to develop their own IT governance frameworks, management should prioritise the implementation of these customised governance frameworks.

**Figure 25: Status of information technology**



During our information systems audit we focused in detail on IT controls over financial systems, whereas figure 2 covers all three reporting focus areas, namely financial, performance and compliance. Our audit also included an assessment of the IT controls that focus on security management, user account management and IT service continuity. Figure 25 shows that there has been a **slight improvement** since the previous year in the number of auditees that had audit findings on IT controls relating to financial systems.

Five auditees (three more than in the previous year) had no audit findings in the category of IT security controls. However, nine auditees had not designed adequate IT security controls and three had not implemented the controls designed.

Compared to the previous year, there had been an increase (four more than the previous year) in the number of auditees with no findings in the focus area of IT service continuity. However, nine auditees had not designed adequate IT service continuity controls and three had not implemented the controls designed.

Eight auditees had not designed adequate user access management controls and nine had failed to implement the controls designed. There was consequently no improvement in this focus area since the previous audit.

**Figure 26: Status of information technology controls**

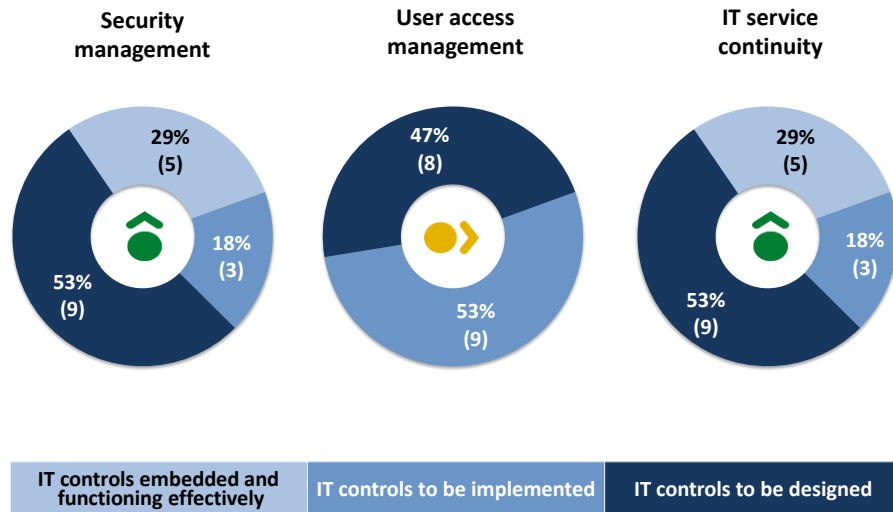


Figure 26 above indicates the status of the controls in the areas we audited and the movement since the previous year. It shows the number of auditees where the IT controls are functioning effectively, or are not in place (i.e. not designed), or have not been implemented. The most common findings were the following:

- **Security management:**

Security management controls are embedded and are functioning effectively at the departments of Agriculture and Rural Development, Economic Development, Tourism and Environmental Affairs, department of the Premier, Sport, Arts, Culture and Recreation and Tourism Authority. Firewalls had not been installed to secure the internal parameters of the auditees against unauthorised access by other departments within the environment secured by the State Information Technology Agency. Poorly configured access controls consequently exposed the IT systems to unauthorised access by both external and internal intruders. Computer programmes were also not patched to reinforce them against security vulnerabilities.

- **User access management:**

The activities of the system administrators were not monitored to detect instances of abuse of privileges. The access rights of ordinary users were also

not periodically reviewed to confirm their compatibility with the users' responsibilities on the IT systems and to detect access rights that compromised the segregation of duties.

- **Information technology service continuity:**

IT service continuity controls are embedded and functioning effectively at the departments of Agriculture and Rural Development, CoGTA, Economic Development, Human Settlements and Sport, Arts, Culture and Recreation. The most prevalent findings in the focus area of IT service continuity concerned the development of disaster recovery plans in isolation, i.e. not based on the business continuity plans, and the infrequent testing of backup tapes to confirm that they could be restored if required. In the case of departments, the data hosted on their transversal systems would be available at the disaster recovery site of the State Information Technology Agency (SITA).

Management should prioritise the design and implementation of the security management, user access management and IT service continuity controls to mitigate the risk of unauthorised access to, and unavailability of IT systems or incompleteness of data in the event of major system disruptions or data loss.

### 4.3 Summary of root causes

Our audits included an assessment of the root causes of audit findings, based on identifying the internal controls that failed to prevent or detect the error or non-compliance. These root causes were confirmed with management and shared in the management report with the accounting officer and the executive authorities.

As reported in section 2 (overall audit outcomes), many auditees produced financial statements and annual performance reports of a poor quality and did not comply with key legislation. The information that follows summarises the three most common root causes of poor audit outcomes and inadequate controls and provides recommendations to address the root causes. The four auditees with clean audit outcomes are excluded from the root cause analysis below.

#### **Slow response by management (accounting officer/ authority and senior management)**

##### *Detail of root cause*

Slow response by management has been identified as the most critical root cause of findings at 14 (78%) of the auditees (excluding the four auditees that were unqualified with no findings). It had also been identified as a root cause in the prior year, but a regression is reported for 2013-14. Adequate progress has not been made with the key controls, especially relating to the review and monitoring of compliance at 14 (78%) of the auditees as detailed in section 2.3. Section 4.1

concludes that the vacancies and instability in the positions supporting management are of concern. Management did not take ownership of the control environment as the action plans are not rigorously monitored and the same audit findings are repeated year after year. Also refer to section 5 which indicates that the different assurance providers did not provide the required level of assurance at all auditees.

Management has over-relied on the audit process to identify misstatements. Once material errors are identified by the auditors, management corrects the material misstatements to avoid qualifications. This is an indication of management's slow response to address key areas of concern. The auditees have the ability to do what is required to improve audit outcomes, but should be willing and committed to address previous root causes identified.

The steep increase in this root cause is as a result of recommendations and the commitments made in the previous years not being implemented.

The slow response by management is further supported by the general lack of consequences in the province at 56% of auditees, which has been reported and discussed over the last few years. It is evident that oversight bodies as well as political leadership failed to take transgressors and poor performers to task. Despite material findings raised during the audit process and continuous irregular expenditure being incurred, there is no accountability. The role players have not set the tone to hold staff accountable.

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## Recommendations

The following actions should be taken to address the root cause:

- Management should prioritise the filling of vacancies in positions supporting them with adequately skilled people.
- Executive leadership should ensure that regular internal controls, such as daily, weekly, monthly and quarterly reporting and reviews by senior management and internal audit units, are functioning effectively in areas of financial management, compliance and performance reporting. After implementation the key controls should be monitored regularly and staff should be held accountable for not doing their part. Accountability and consequence management are key to successful implementation of key controls.
- Management should review non-compliance on a monthly basis.
- The oversight bodies, together with the political leadership in the province, should hold management accountable for their slow response. This will set the tone from the top and ensure that discipline is instilled within the auditees.

## Instability and vacancies in key positions supporting the chief financial officer, head of supply chain management and manager responsible for predetermined objectives

### Detail of root cause

We identified instability and vacancies in key positions supporting the chief financial officer, head of supply chain management and the manager responsible for predetermined objectives as a root cause of poor audit outcomes at 12 (67%) of the auditees. It was also identified as a root cause (67%) last year, but there has been no improvement in this regard. Instability and vacancies reduce leadership's effectiveness to create a good and sustainable control environment. Policies and procedures, action plans and review and monitoring controls cannot be implemented and performed effectively without skilled and adequate resources. The management of vacancies is discussed in detail in section 4.1.

### Recommendations

The following actions should be taken to address the root cause:

- The executive leadership should prioritise the filling of vacancies in key positions with people who have the necessary qualifications, experience and competency levels to fulfil their responsibilities and exercise their powers effectively.
- The executive leadership should ensure stability in key positions.

The executive leadership was unable to make progress in addressing this root cause in spite of their commitment to do so. Suitable candidates who met requirements were identified, but declined employment.

## Key officials lack appropriate competencies

### Detail of root cause

Officials in key positions at 12 (67%) of the auditees did not have the minimum competencies and skills required to perform their jobs. This impacts directly on the quality of service delivery reporting, financial reporting and compliance with legislation (in particular, compliance with supply chain management legislation). Employees lack the business acumen necessary to achieve good administration, are not implementing ongoing training and development within their working environment and do not perform their duties with the required care and diligence. This was not raised as one of the top three root causes in the prior year and the executive leadership should focus thereon to ensure that service delivery is improved.

## Recommendations

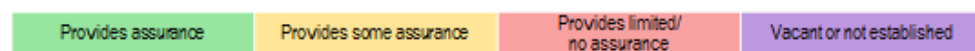
The following actions should be taken to address the root cause:

- The accounting officer/authority should put processes in place to ensure that training initiatives are implemented in the working environment.
- The accounting officer/authority should ensure that senior staff mentor and oversee the work of lower levels of staff.
- The accounting officer/authority should ensure that processes are in place that will ensure that appointments are made only after the minimum competency requirements have been verified and the necessary background checks have been completed.

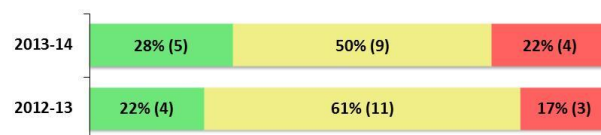
## 5. Impact of key role players

The management and leadership of the auditee and those that perform an oversight or governance function should work towards improving the key controls, addressing the root causes and ensuring that there is an improvement in the key risk areas, thereby providing assurance on the quality of the financial statements and performance reports as well as compliance with legislation.

Based on our assessment as shown in figure 2, all role players are not yet providing the necessary assurance. Below is an overview of the assurance provided by each of the assurance providers. The colours in this section have the following meanings:



### Senior management



Only five role players at the first level of assurance fully provided the required level of assurance. Senior management at the department of Sport, Arts, Culture and Recreation, the legislature, provincial treasury and Fleet Management Trading Entity once again equipped the following levels with assurance for credible decision-making. Senior management at the department of Social Development took active and immediate steps when cases of possible fraud were reported to their internal audit. The assurance provided by senior management at the departments of Education and the Premier regressed. Senior management at the department of Education lacked a sense of responsibility to ensure that information produced is complete, valid and accurate. At the department of the Premier the

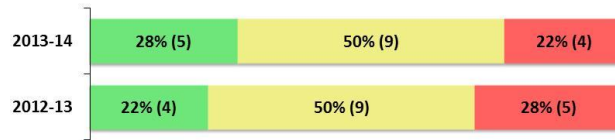
senior managers did not keep proper records of tangible capital assets, while the lack of review and monitoring thereof resulted in a regression in audit outcome. The majority of senior management staff only provided some assurance and significant strides will have to be made if the required level of assurance is to be provided for credible decision-making. Accounting officers and MECs rely on senior management, which includes the chief financial officer, chief information officer, performance manager and head of the supply chain management unit, to implement basic financial and performance management controls. These controls include the following:

- Ensure proper record keeping so that complete, relevant and accurate information is accessible and available to support financial and performance reporting.
- Implement controls over daily and monthly processing and reconciling of transactions. After these controls have been implemented, there should be adequate supervision and review to ensure accountability and consequence management where these basic controls are still not working effectively.
- Prepare regular, accurate and complete financial and performance reports that are supported and evidenced by reliable information.
- Review and monitor compliance with applicable laws and regulations.
- Design and implement formal controls over IT systems.
- Senior management needs to take responsibility for the programmes they are responsible for by ensuring that the programme is properly run in its entirety (financial, compliance and performance information). This should be the level from where accountability is enforced and senior managers need to ensure that the desired culture is instilled in all employees working within a specific programme.

The poor status of these internal controls, as reported in section 4, shows that inadequate assurance was provided. It is of concern that senior management's representations to us at the start of each audit, including those relating to the quality of the financial statements submitted for auditing, continue to be unreliable. It highlights the risk that decisions taken by accounting officers and MECs could be based on incomplete and incorrect information provided by senior management.

The human resource management challenges outlined in section 4.1 should be addressed to strengthen the assurance provided by senior management. Vacancies need to be filled and senior management staff should be held accountable for the execution of their responsibilities through a strict and proper system of performance management.

## Accounting officer or accounting authority



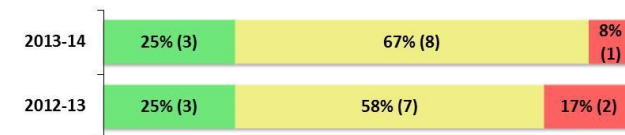
Accounting officers and authorities are responsible for auditees' internal controls, including leadership, planning, risk management as well as oversight and monitoring. While accounting officers and authorities depend on senior management for designing and implementing the required financial and performance management controls, they should create an environment that helps to improve such controls. The impact of accounting officers and authorities on creating an effective control environment was still not evident at most auditees. As reported in section 4, the status of those internal controls for which accounting officers and authorities are responsible remained unchanged since the prior year and therefore their leadership, planning, risk management, oversight and monitoring should further be improved to result in sustainable practices that translate into improved audit outcomes.

The prior year vacancy at the department of Social Development has been filled for 2013-14. An improvement in assurance levels was noted at the legislature, the department of Human Settlements and the Free State Development Corporation as accounting officers/authorities monitored the implementation of their action plans. The regression at the departments of Education and the Premier was a result of the accounting officer not attending steering committee meetings throughout the audit and the ineffective monitoring of the action plan, respectively. Although accounting officers and authorities depend on senior management for designing and implementing the required financial and performance management controls, they should create an environment that helps to improve such controls by focusing on the following:

- Provide effective and ethical leadership, and exercise oversight of financial and performance reporting and compliance with legislation.
- Implement effective human resource management to ensure that adequate and sufficiently skilled staff are employed and that performance is monitored.
- Establish policies and procedures to enable sustainable internal control practices, and monitor the implementation of action plans to address internal control deficiencies.
- Establish an IT governance framework that supports and enables the achievement of objectives, delivers value and improves performance.
- Implement appropriate risk management activities to ensure that regular risk assessments, including the consideration of IT risks and fraud prevention, are conducted and that a risk strategy to address the risks is developed and monitored.

- Ensure that the internal audit units are adequately resourced and functioning and that internal audit reports are responded to by implementing their recommendations.
- Support the audit committee and ensure that its reports are responded to by implementing their recommendations.
- The accounting officer/authority is ultimately responsible for the performance of the departments and public entities and needs to provide direction by ensuring that policies and procures are implemented and performance monitored.
- The accounting officer/authority should set the tone in the way he/she keeps senior management accountable and so-doing cascade a culture of consequence management to the auditee as a whole. The accounting officer should set an example to the senior management group of what the desired values of the entity are in the way he/she behaves on a daily basis. The group needs to be clear on what behaviour is acceptable and what not.

## Member of executive council



MECs have a monitoring and oversight role at both the departments and public entities. They have specific oversight responsibilities in terms of the PFMA and the Public Service Act. They therefore need to ensure that strategies and budgets are aligned to the mandate and that objectives are achieved. MECs can bring about improvements in the audit outcomes of their auditees by being actively involved in key governance matters and managing the performance of the accounting officers and authorities.

Our assessment that most MECs did not provide the required level of assurance is based on the unchanged status of the leadership controls (as detailed in section 4) and the impact of MECs on audit outcomes as observed through our regular interactions with them. In certain instances, commitments obtained from MECs do not address the root causes of unsatisfactory audit outcomes and also do not result in the implementation of adequate key controls to ensure sustainable improvements in audit outcomes.

The 2012-13 Speaker vacancy was filled for 2013-14.

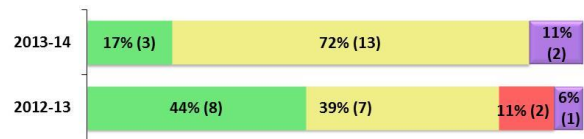
In the past four years, we have increasingly engaged with MECs on how they can bring about improvements in the audit outcomes of their portfolios. At these interactions, we discuss the status of key controls and members' commitments to improve audit outcomes, while also sharing identified risks. The meetings improve the members' understanding of the audit outcomes and messages and also

address progress made with interventions to ensure a positive impact on these audit outcomes (section 6 provides more detail on the interactions with the MECs).

The MECs should provide strategic direction to the department and any public entities within their portfolios. To achieve this, they should communicate frequently with the accounting officer/accounting authority, thereby aligning the decisions taken by the accounting officer/authority to the greater policy framework of the government of the day. MECs also need to commit to actions addressing the root causes.

The involvement of MECs, especially at the auditees that did not receive clean audit outcomes, needs to receive attention. Of importance here is not only the visibility of these members, but also the actions taken by them to address the various issues with which these auditees are dealing.

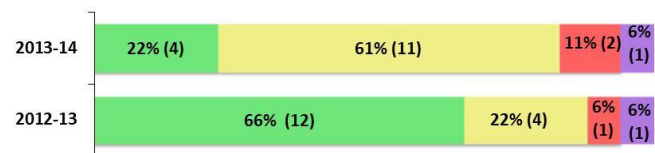
### Internal audit unit



Internal audit units assist accounting officers and authorities in the execution of their duties by providing independent assurance on internal controls, financial information, risk management, performance management and compliance with legislation. Internal audit units were in place at all auditees except the Free State Tourism Authority and the Free State Gambling and Liquor Authority. The operations of 56% of the internal audit units were compliant with the requirements of the PFMA. However, the findings and recommendations made by these units are not implemented consistently by leadership. This impacted on the assurance level of the internal audit unit, resulting in the regression in assurance provided by the internal audit unit.

Internal audit units can only be effective if they are adequately resourced, if audit committees oversee and support their operations, and if accounting officers and senior management cooperate and respond to their advice and recommendations.

### Audit committee



An audit committee is an independent body that advises the council, mayor, accounting officer or authority and senior management on matters such as internal controls, risk management, performance management as well as evaluation and

compliance with legislation. The committee is required to provide assurance to the accounting officer/authority on the adequacy, reliability and accuracy of financial reporting and information.

The regression in the assurance level assessment is mainly due to the lack of implementation by leadership of resolutions made by the audit committee. Audit committees were in place at all auditees except the Free State Tourism Authority for both years. The work of these committees was compliant with legislation, except for the department of Agriculture and Rural Development where the audit committee was not in place for the first six months of the financial year. Only 22% of the audit committees had a positive impact on the audit outcomes.

For audit committees to provide the required level of assurance as second-level assurance providers, they depend heavily on the reliability of the assurance provided by senior management and internal audit units. The lower the assurance level provided by these two role players, the more difficult it is for audit committees to accurately assess the control environment of the auditee, including being assured that significant risks are being reduced.

Strong audit committees can provide the momentum for moving forward by pulling the other role players together in a united effort. As an independent adviser and specialist in the control environment, the committee is in a position not only to evaluate the credibility of information but also to robustly report to the executive on who is delivering and who is not. This can provide the executive with assurance and empower them to enforce focused accountability. The success of this depends on the degree to which the MECs interact with and support the audit committee.

### Provincial treasury

The provincial treasury has a legislative mandate to support provincial departments and municipalities. Their role is to provide support on provincial economic analysis, fiscal policy, the management of the annual budget process and the implementation of provincial budgets by:

- influencing policy development and implementation in line with fiscal framework
- providing fiscal policy implementation support
- allocating financial resources in line with government priorities
- monitoring financial and non-financial performance of the provincial government.

### Financial governance

With regard to financial governance, the department promotes accountability through substantive reflection of financial activities of the province as well as compliance with finance norms and standards by:

- promoting sound accounting practices and reporting

- promoting sound risk management and internal audit practices, and
- promoting sound accounting practices and reporting.

In fulfilling their mandate, they are required to put appropriate processes and measures in place to enable the execution of their powers/functions.

The provincial treasury has consistently provided assurance over a number of years. Their main driving forces are the correct tone from the executive authority, effective leadership and committed and dedicated staff. In order to sustain the assurance level, provincial treasury must ensure that there is consequence management, stability in key positions and continuous appointment of competent staff. The MEC for Finance has a hands-on approach and was always readily available to discuss concerns that came to light during the audit process. The MEC facilitates and avails own staff to assist departments to clear concerns and address technical difficulties.

During the sector audit it was clear that provincial treasury fulfils its mandate to support, assist and monitor the budget process at departments and municipalities. However, their support can be enhanced by filling vacancies within the municipal budgets directorate of the provincial treasury. Provincial treasury should also continue with their effective oversight role to enhance the supporting role in accordance with its mandate. The only challenge was that the legislation defining their mandate did not specifically refer to the impact of the monitoring role. Support is focused on outputs only. Going forward, support can be further enhanced if impact is also monitored and evaluated.

## Department of the Premier

The department of the Premier has a constitutional mandate to implement and administer provincial and national legislation as well as to coordinate functions of the provincial government. The required support to and oversight of provincial and local government includes human resource management, IT management, monitoring and evaluation of performance information, monitoring of provincial alignment to national priorities and monitoring of the anti-corruption hotline. More focus should be placed on closing/resolving cases reported on the anti-corruption hotline. The intergovernmental forum did not report annually to the President's coordinating council on progress made with the implementation of national policy and legislation in the province. The department of the Premier could not submit relevant documentation to report on progress and processes in place to support the presidential priority projects. It is the custom in the province that performance agreements are entered into between the MEC and the relevant accounting officer and not between the premier and the accounting officers. The department of the Premier should enhance the monitoring and evaluation of accounting officers' performance.

Human resource planning and governance for the province are monitored and coordinated at the department of the Premier. The department of the Premier must intervene in cases where there is a lack of capacity in provincial departments. For

this purpose, a performance, monitoring and evaluation unit was established to exercise oversight across government, focusing on service delivery, strategic management, governance and accountability, human resource management and systems and financial management. However, this unit plays a coordinating role, while monitoring is performed by the provincial treasury. Therefore the department of the Premier regressed in the assurance they provided.

The premier, however, remains committed in his oversight role in provincial and local government. The challenge is that legislation regarding its mandate does not specifically define an oversight role, but concentrates on coordination and implementation activities.

Going forward the department of the Premier should focus on the implementation of policies and procedures to ensure that any lack of capacity in provincial departments is identified and resolved on a timely basis. Furthermore, record keeping of the monitoring and evaluation function should be improved to ensure that complete, relevant and accurate information is accessible and available to support financial reporting. Given the slow progress made by the provincial government in reporting on its performance, focus should also be placed on providing assistance with the monitoring and evaluation of performance reports.

In the previous year, the provincial executive leadership re-committed to addressing poor performance; finalising performance contracts for senior management; the attraction and retention of officials with relevant skills and competencies; assisting the portfolio committees in fulfilling their oversight responsibilities; meeting with the Auditor-General of South Africa on a quarterly basis to discuss the key control matrix; assigning the responsibility for predetermined objectives and compliance matters to all auditees; and ensuring that reliable financial and service delivery reports are prepared monthly. The leadership also undertook to investigate and regularise unauthorised and irregular expenditure in the province. Most commitments were only partially implemented and had limited impact.

The 2013-14 audit outcomes gave rise to a commitment from the provincial executive leadership to give direction to the departments to assess the competencies of staff within the individual departments, to identify and address gaps in both senior management and lower levels, more specifically in the finance and supply chain management units; and to curb prevalent non-compliance with laws and regulations and the escalation of irregular expenditure. This commitment will also address the identification of training needs to sustain competency capabilities of staff at all times. Furthermore, the departments will be provided with guidance on the appointment of implementing agents and how to force the implementing agents to follow government procurement processes in procuring goods and services on behalf of the state.



## Department of Cooperative Governance and Traditional Affairs

CoGTA has not been assessed as an assurance provider in their capacity as a coordinating monitoring department for the PFMA cycle, because their responsibility is to ensure an effective, efficient and responsive local government system by overseeing and coordinating the establishment, monitoring, regulating, strengthening, supporting and capacitating the municipalities. In fulfilling their mandate, CoGTA manages the process of integrated development planning by the municipalities. A regularity audit was performed, which included a sector audit, and the department maintained its audit opinion of unqualified with repeat findings on performance reporting and compliance with laws and regulations. This, however, is not reflective of the department's role as a coordinating and oversight department within the municipal sphere.

Although CoGTA provides financial, human resource and consultancy assistance to municipalities, the current status at municipalities is such that interactions by CoGTA are of a crisis management nature. This leaves little opportunity for CoGTA to monitor and evaluate the assistance and processes put in place at the municipalities. Apart from this, their own staff assist municipalities with financial management, administrative challenges and poor performance, which necessitates increased accountability and transparency at municipal level together with improved coordination and cooperation across all levels in the province.

CoGTA should develop a long-term plan with specific target dates and indicators on how to move municipalities away from their current status to independent functioning, while the objectives in the annual performance plans of the department, which are mostly input driven, should be reconsidered to measure the impact of delivering on their mandate.

## Portfolio committees and public accounts committees

The processes and enforcement of accountability for the actions, performance, financial management and compliance with legislation of all involved in government serve as a cornerstone of democratic governance in South Africa. One of the most important oversight functions of the Free State legislature is to consider auditees' annual reports as well as in-year monitoring reports. For the committees to perform their oversight function, assurance is needed that the information in the annual report and in-year reports is credible.

The lack of assurance provided by the senior management and accounting officers (see above) hampers not only the effectiveness of their executive, but also effective oversight by the portfolio committees.

The 2013-14 financial year has been marked by a lack of continuous engagement between AGSA and portfolio committees on audit information relating to non-financial matters. Of concern is that we were not consistently invited to quarterly

meetings of all portfolio committees and our message was limited to the public accounts committee. Portfolio committees therefore did not have information available to perform effective oversight or to make any commitments to us. In order to enhance accountability regarding the use of public funds it is necessary for portfolio committees to engage with us and to perform robust oversight, take resolutions and track these for implementation.

The public accounts committee adhered to their prior commitment of regular interactions with us. The committees have been assessed as providing limited assurance as their resolutions are not distributed by the department of the Premier to the departments and public entities.

The public accounts committee and portfolio committees appointed in the 5<sup>th</sup> legislature have already shown increased interest in the message of the AGSA and we will continue to enhance an understanding of our role, the audit findings and their causes and effects to ensure that we add value to the work of the committees.

## 6. Initiatives and commitments of key role players

We shared our key message on the actions needed to improve audit outcomes with accounting officers and authorities, MECs, the premier and the legislature through our reports and interactions with them.

We met with the MECs and the premier during the year. It was a challenge to secure meetings with the MECs for CoGTA and Human Settlements due to the premier's requirement for her to be more involved at municipalities and accompany him on all his visits locally and abroad. A more assertive effort will be made to ensure that we meet with the MEC to share insights and risks relating to the two departments and local government.

From our interactions it is evident that leadership received our engagements well and that the impact thereof was increasing year on year. The impact of interactions with the MECs resulted in the following:

- Five (28%) auditees improved their audit outcomes, i.e. the departments of Economic Development, Tourism and Environmental Affairs, Public Works, the legislature, Tourism Authority and Free State Development Corporation.
- Three (17%) auditees sustained their outcome of unqualified with no findings, i.e. the department of Sport, Arts, Culture and Recreation, the provincial treasury and Fleet Management Trading Entity.
- Four (22%) auditees managed to attend to their control environment resulting in some improvement in key controls, i.e. the departments of Agriculture and Rural Development; Health; Police, Roads and Transport and Social Development.

- Four (22%) auditees are expected to improve next year, i.e. the department of Education, the Premier, Central Medical Trading Account and Free State Gambling and Liquor Authority.

We will continue with quarterly engagements with the MEC, but with greater emphasis on quality conversations with an increased impact.

However, the building blocks are in place for improvements in key controls, which should lead to improved outcomes. The low impact of our interactions with certain MECs is indicative of their failure to prioritise our message and their slow response to our message.

Throughout the year, we monitor the commitments and initiatives of members of the executive, the premier and the public account committees to implement initiatives that can improve audit outcomes. The progress made with such commitments and the initiatives of MECs in response to the previous year's audit outcomes and new commitments are included in the portfolio summaries in this report.

# AUDIT OUTCOMES OF INDIVIDUAL PORTFOLIOS

# Agriculture and rural development

**Overall stagnation in audit outcome**

Audit area	Audit outcome
Financial statements (F)	Unqualified
Performance reports (P)	Material findings
Compliance with legislation (C)	Material findings

**Assurance levels**

First level	Senior management	Provides some assurance
	Accounting officer	Provides some assurance
	Executive authority	Provides some assurance
Second level	Internal audit unit	Provides some assurance
	Audit committee	Provides some assurance
Third level	Portfolio committee	Provides limited or no assurance

**Key controls**

	Audit area		
	F	P	C
Effective leadership	Good	Good	Good
Human resource controls	Concerning	Concerning	Concerning
ICT governance and controls	Concerning	Good	Concerning
Audit action plans	Good	Concerning	Good
Proper record keeping	Good	Concerning	Good
Daily and monthly controls	Good	Good	Good
Review and monitor compliance	Concerning	Concerning	Concerning

F = Financial P = Performance C = Compliance

Good Concerning

1  
To improve the **audit outcomes** ...  
... the **risk areas** and ...  
4

2  
... the key role players need to **assure** that ...  
... the **root causes** are addressed ...  
5

3  
... attention is given to the **key controls** and ...  
... and the **commitments** are honoured.  
6

**Risk areas**

Quality of submitted financial statements Good	Quality of submitted performance reports Concerning	Supply chain management Concerning
Financial health Intervention required	Human resource management Concerning	Information technology Concerning

Good Concerning Intervention required

**Most common root causes**

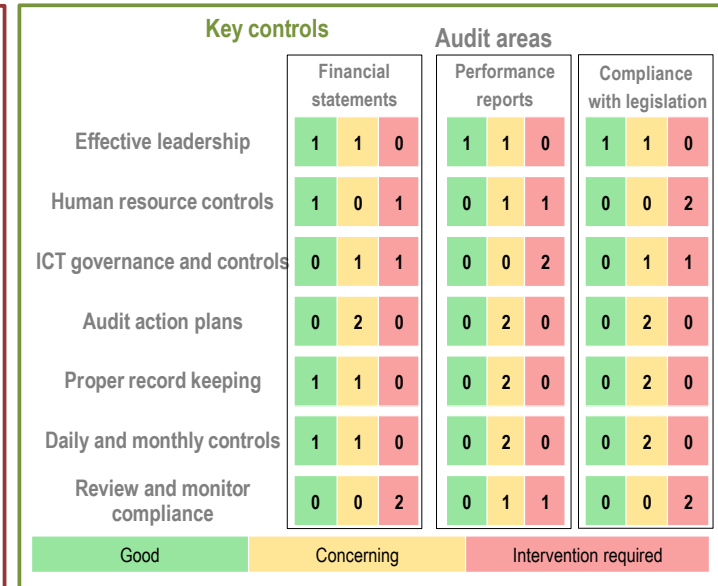
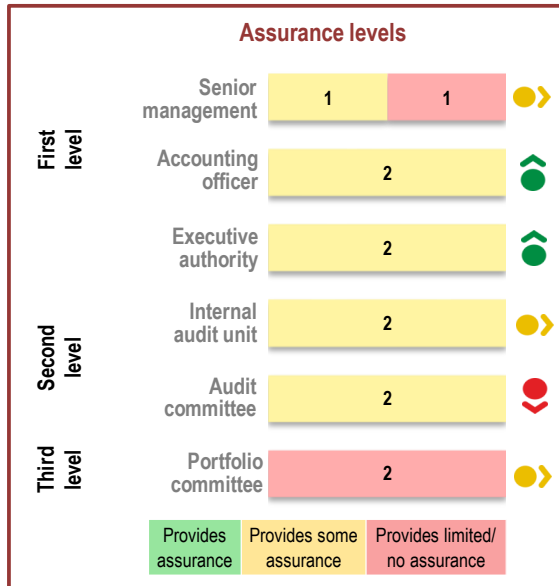
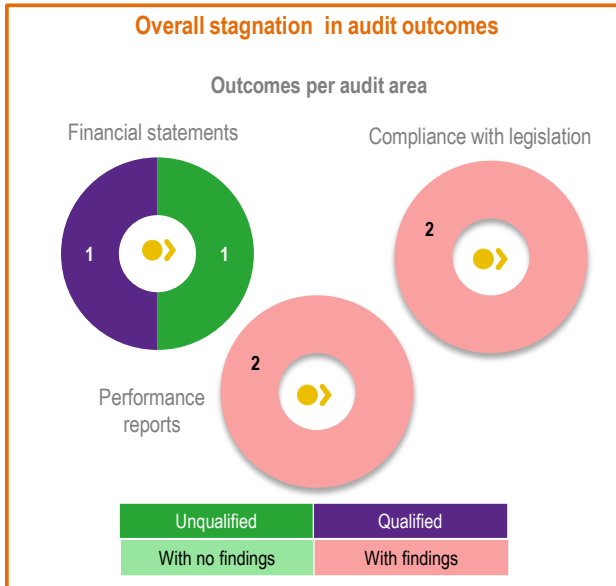
- Lack of consequences for poor performance and transgressions
- Key officials lack appropriate competencies
- Vacancies in the positions supporting the CFO, SCM manager and PDO manager

**Status of key commitments by MEC**

The new financial reporting framework will be implemented by the accounting officer and the audit committee will evaluate it before submission to the AGSA Implemented	Improve the monitoring of financial and performance reporting Implemented
HoD and senior management undertook to ensure that the possible risk areas and focus areas will be ready during the audit In progress	Exercise oversight of financial and performance reporting and compliance and related internal controls In progress

In progress Implemented

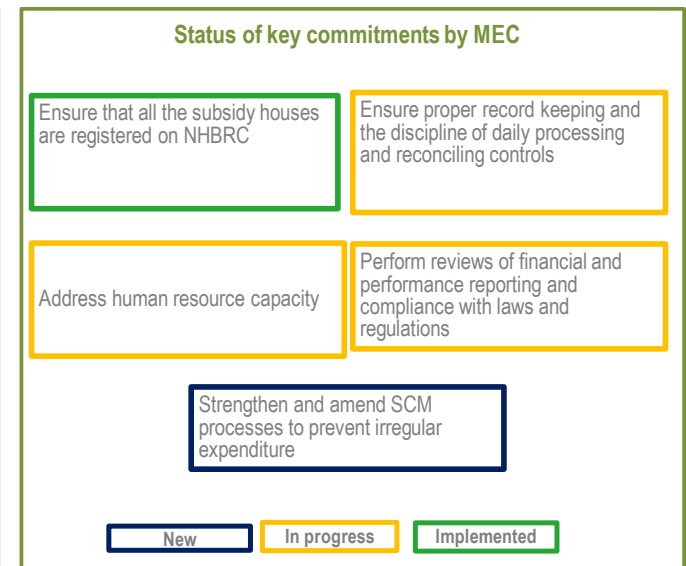
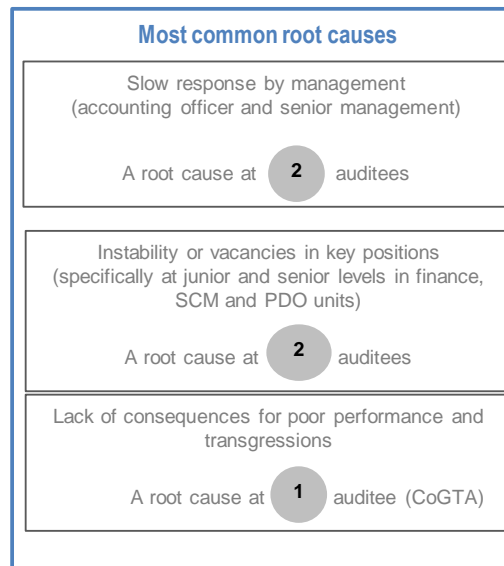
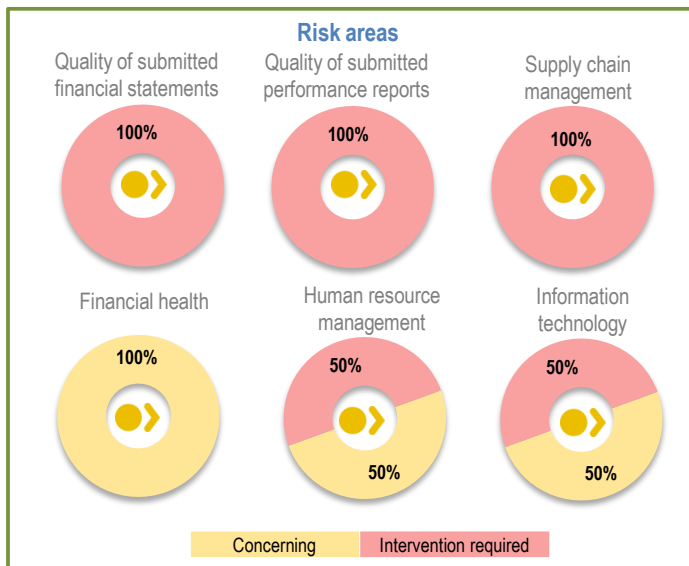
# Cooperative governance and traditional affairs and human settlements



1  
To improve the **audit outcomes** ...  
... the **risk areas** and ...  
4

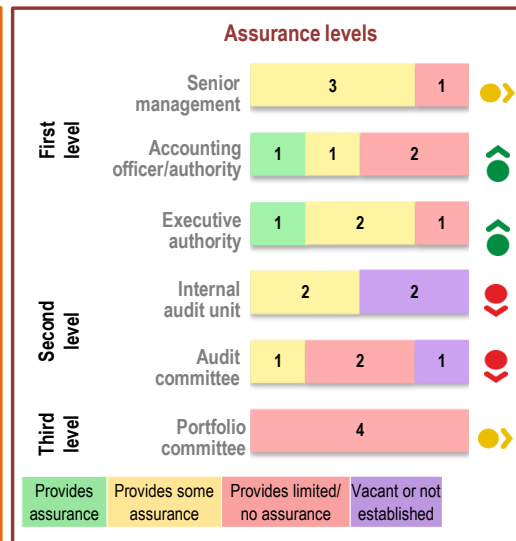
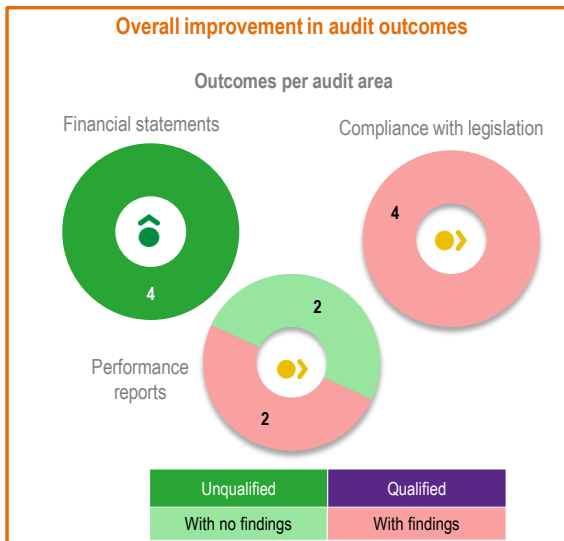
2  
... the role players need to **assure** that ...  
... the **root causes** are addressed ...  
5

3  
... attention is given to the **key controls** and ...  
... and the **commitments** are honoured.  
6



# Economic development, tourism and environmental affairs

The auditees included in the following portfolio are: Economic Development, Tourism and Environmental Affairs (unqualified opinion with findings on compliance); Free State Development Corporation (unqualified with findings on compliance); Free State Gambling and Liquor Authority (unqualified opinion with findings on compliance and PDO); Free State Tourism Authority (unqualified opinion with findings on compliance and predetermined objectives).



### Key controls

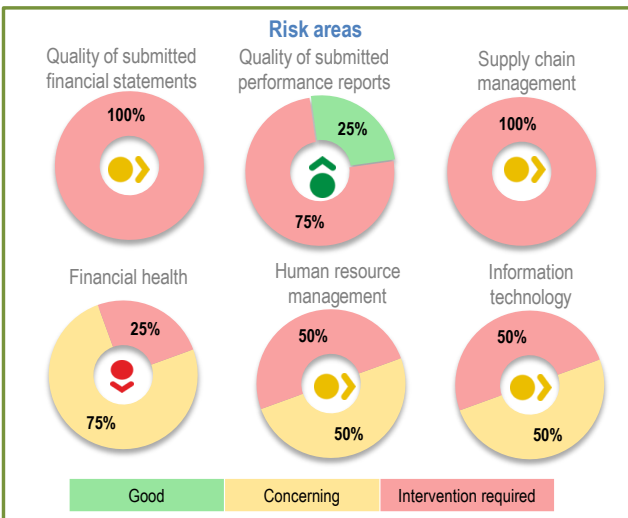
Key Control	Financial statements			Performance reports			Compliance with legislation		
	Good	Concerning	Intervention required	Good	Concerning	Intervention required	Good	Concerning	Intervention required
Effective leadership	1	2	1	2	1	1	1	1	2
Human resource controls	0	3	1	1	1	2	0	1	3
ICT governance and controls	0	3	1	0	2	2	0	2	2
Audit action plans	1	1	2	2	1	1	1	1	2
Proper record keeping	0	2	2	0	2	2	0	2	2
Daily and monthly controls	0	3	1	0	3	1	0	3	1
Review and monitor compliance	0	0	4	1	0	3	0	0	4

Legend: Good (Green), Concerning (Yellow), Intervention required (Red)

1  
To improve the **audit outcomes** ...  
... the **risk areas** and ...  
4

2  
... the key role players need to **assure** that ...  
... the **root causes** are addressed ...  
5

3  
... attention is given to the **key controls** and ...  
... and the **commitments** are honoured.  
6



### Most common root causes

- Slow response by management (accounting officer and senior management)  
A root cause at 4 auditees
- Key officials lack appropriate competencies  
A root cause at 4 auditees
- Instability or vacancies in key positions supporting the CFO, SCM manager and PDO manager or vacancies in the districts  
A root cause at 3 auditees

### Status of key commitments by MEC

Commitment was made to address issues relating to lack of leadership in the HR department. This commitment was adequately implemented.

Assemble a team to correct the assets for the 2013-14 financial year. Quarterly progress with the verification and updating of the asset register. This commitment was addressed by performing an asset count and starting the asset register from scratch. The department is still in progress as minor issues were identified.

Investigate the process with regards to identification, procurement and calculation of leases. The department is still in progress as immaterial issues were raised.

Legend: In progress (Yellow), Implemented (Green)

# Education

**Overall regression in audit outcomes**

Audit area	Audit outcome
Financial statements (F)	Qualified
Performance reports (P)	Material findings
Compliance with legislation (C)	Material findings

**Assurance levels**

Level	Entity/Committee	Assurance Level
First level	Senior management	Provides limited/no assurance
	Accounting officer	Provides limited/no assurance
	Executive authority	Provides limited/no assurance
Second level	Internal audit unit	Provides some assurance
	Audit committee	Provides some assurance
Third level	Portfolio committee	Provides limited or no assurance

**Key controls**

Audit area	Audit area		
	F	P	C
Effective leadership	Concerning	Intervention required	Intervention required
Human resource controls	Concerning	Intervention required	Intervention required
ICT governance and controls	Concerning	Intervention required	Intervention required
Audit action plans	Intervention required	Intervention required	Intervention required
Proper record keeping	Concerning	Intervention required	Intervention required
Daily and monthly controls	Concerning	Intervention required	Intervention required
Review and monitor compliance	Intervention required	Intervention required	Intervention required

F = Financial P = Performance C = Compliance

Concerning Intervention required

1  
To improve the **audit outcomes** ...  
... the **risk areas** and ...  
4

2  
... the key role players need to **assure** that ...  
... the **root causes** are addressed ...  
5

3  
... attention is given to the **key controls** and ...  
... and the **commitments** are honoured.  
6

**Risk areas**

Quality of submitted financial statements	Quality of submitted performance reports	Supply chain management
Concerning	Concerning	Concerning
Financial health	Human resource management	Information technology
Intervention required	Concerning	Concerning

Concerning Intervention required

**Most common root causes**

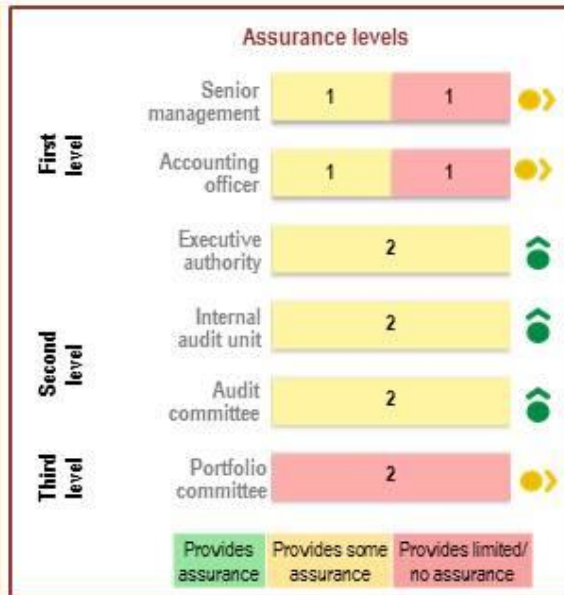
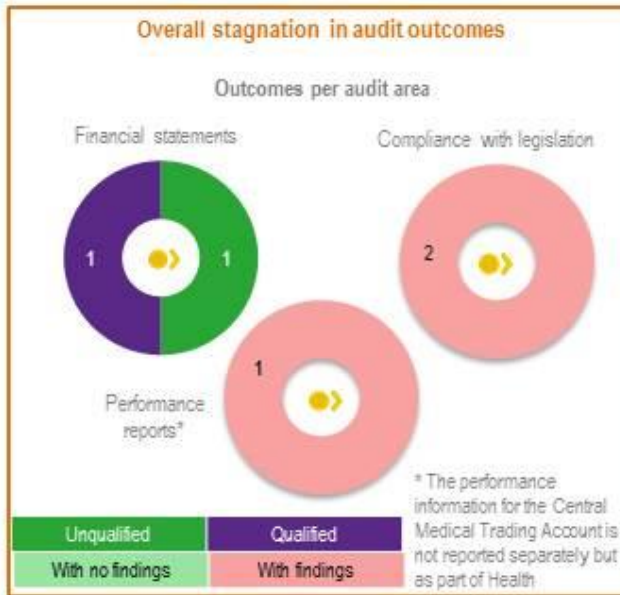
Slow response by management (accounting officer and senior management)
Key officials lack appropriate competencies
Lack of consequences for poor performance and transgressions

**Status of key commitments by MEC**

Prioritise the establishment of documented processes for performance information reporting to enhance collection, verification and collation of information.	To allocate responsibility for oversight of the asset register to a chief director to ensure that the audit opinion on asset disclosures does not regress.
Strengthen the department's performance management processes by acknowledging good performance and ensuring that there are consequences for poor or non-performance	Strengthen proper record management and controls over financial and performance reporting, especially in the area of disclosure notes to the financial statements, such as assets, accruals and commitments.

Not implemented In progress

# Health and the central medical trading account



### Key controls

Key Control	Financial statements			Performance reports			Compliance with legislation		
	Good	Concerning	Intervention required	Good	Concerning	Intervention required	Good	Concerning	Intervention required
Effective leadership	1	1	0	1	0	1	1	0	1
Human resource controls	0	1	1	0	1	1	0	0	2
ICT governance and controls	0	0	2	0	0	2	0	0	2
Audit action plans	0	2	0	0	2	0	0	1	1
Proper record keeping	0	2	0	0	2	0	0	1	1
Daily and monthly controls	0	1	1	0	2	0	0	0	2
Review and monitor compliance	0	0	2	0	1	1	0	0	2

1  
To improve the **audit outcomes** ...  
... the **risk areas** and ...  
4

2  
... the key role players need to **assure** that ...  
... the **root causes** are addressed ...  
5

3  
... attention is given to the **key controls** and ...  
... and the **commitments** are honoured.  
6



### Most common root causes

- Lack of consequences for poor performance and transgressions  
A root cause at 2 auditees
- Key officials lack appropriate competencies  
A root cause at 2 auditees
- Instability caused by vacancies in key positions (director and district manager level) across various sections within the department (Infrastructure, Legal, Procurement and Performance, HR Development)  
A root cause at 2 auditees

### Status of key commitments by MEC

All members of the audit committee have been appointed.	Strengthening proper record management and controls over performance reporting.
Implementation of a proper performance management system for all staff within the department, which will enable the department to hold staff accountable for poor performance and transgressions.	Finalisation and implementation of a service delivery transformation plan for the department.

Legend: In progress (Yellow), Implemented (Green), New (Blue)



# Premier

**Overall regression in audit outcomes**

Audit area	Audit outcome	
Financial statements (F)	Qualified	⬇️
Performance reports (P)	No material findings	➡️
Compliance with legislation (C)	Material findings	⬇️

**Assurance levels**

Level	Entity	Assurance	
First level	Senior management	Provides some assurance	⬇️
	Accounting officer/authority	Provides some assurance	⬇️
	Executive authority	Provides some assurance	⬇️
Second level	Internal audit unit	Provides some assurance	⬇️
	Audit committee	Provides some assurance	⬇️
Third level	Portfolio committee	Provides limited or no assurance	➡️

**Key controls**

Key controls	Audit area		
	F	P	C
Effective leadership	Good	Concerning	Intervention required
Human resource controls	Good	Concerning	Intervention required
ICT governance and controls	Concerning	Good	Intervention required
Audit action plans	Intervention required	Good	Intervention required
Proper record keeping	Intervention required	Concerning	Intervention required
Daily and monthly controls	Concerning	Good	Intervention required
Review and monitor compliance	Concerning	Good	Intervention required

F = Financial    P = Performance    C = Compliance

Good    Concerning    Intervention required

**1**  
To improve the **audit outcomes** ...  
... the **risk areas** and ...  
**4**

**2**  
... the key role players need to **assure** that ...  
... the **root causes** are addressed ...  
**5**

**3**  
... attention is given to the **key controls** and ...  
... and the **commitments** are honoured.  
**6**

**Risk areas**

Quality of submitted financial statements ⬇️	Quality of submitted performance reports ➡️	Supply chain management ➡️
Financial health ➡️	Human resource management ⬇️	Information technology ➡️

Good    Concerning    Intervention required

**Most common root causes**

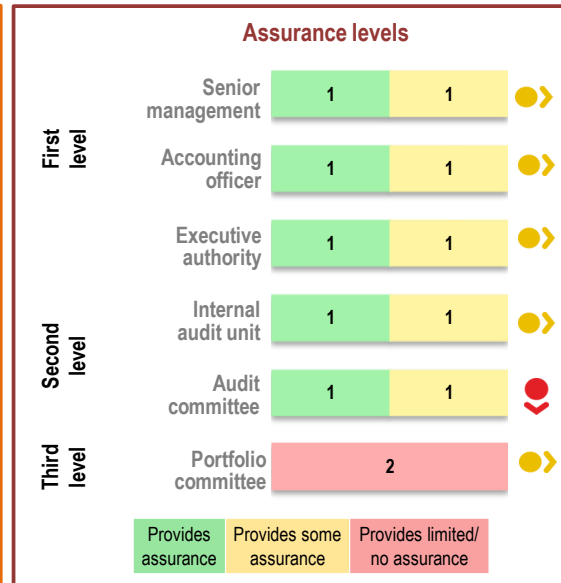
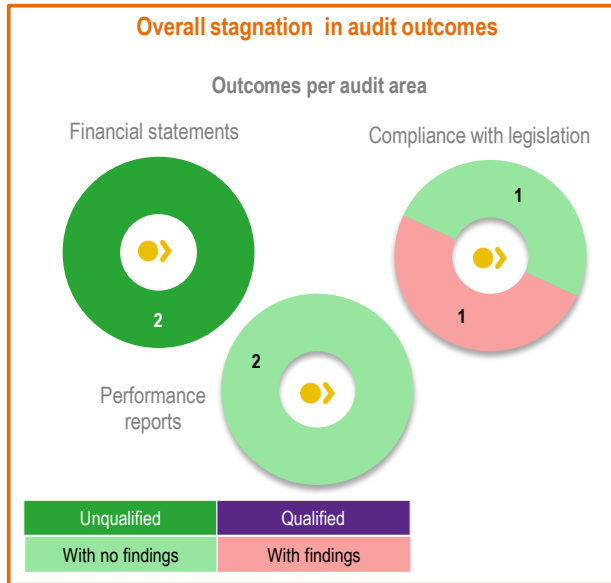
- Slow response by management (accounting officer and senior management)
- Key officials lack appropriate competencies
- Instability or vacancies in key positions (specifically in the position of CFO, SCM manager and staff in the asset management section)

**Status of key commitments by MEC**

Leadership to provide effective oversight to sustain the audit outcome.	Internal audit to review and monitor compliance with laws and regulations.
Implement proper record keeping to ensure complete, relevant and accurate information, including the review of the asset register.	Appoint competent employees within the asset management section. The controls over the movable assets will be improved and monthly checks will be performed as soon as the assets section has been capacitated.

In progress    New

# Police, roads and transport and Free State fleet management trading entity



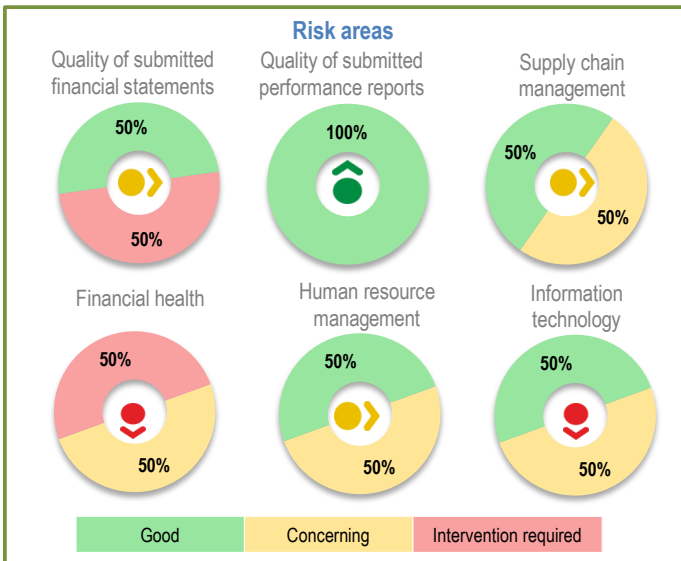
### Key controls and Audit areas

Key controls	Financial statements			Performance reports			Compliance with legislation		
	Good	Concerning	Intervention required	Good	Concerning	Intervention required	Good	Concerning	Intervention required
Effective leadership	2	0	0	2	0	0	2	0	0
Human resource controls	1	1	0	1	1	0	0	1	1
ICT governance and controls	0	2	0	1	1	0	1	1	0
Audit action plans	1	1	0	1	1	0	1	1	0
Proper record keeping	1	1	0	1	1	0	1	1	0
Daily and monthly controls	1	1	0	1	1	0	1	1	0
Review and monitor compliance	1	1	0	1	0	1	0	1	1

1  
To improve the **audit outcomes** ...  
... the **risk areas** and ...  
4

2  
... the key role players need to **assure** that ...  
... the **root causes** are addressed ...  
5

3  
... attention is given to the **key controls** and ...  
... and the **commitments** are honoured.  
6



### Most common root causes

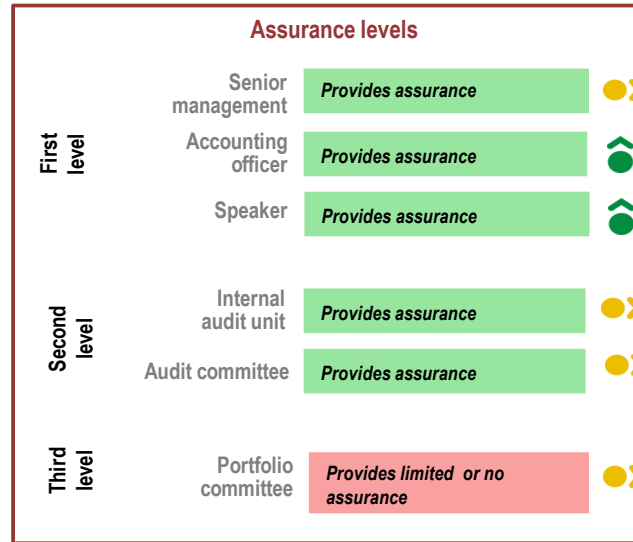
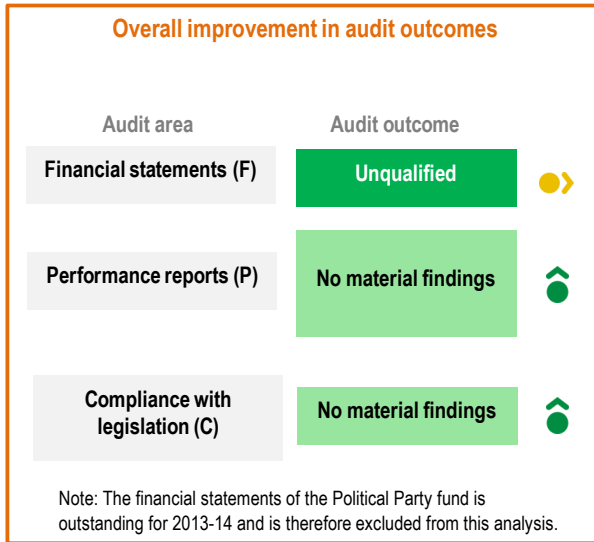
- Lack of consequences for poor performance and transgressions  
A root cause at 1 auditee
- Key officials lack appropriate competencies  
A root cause at 1 auditee
- Instability or vacancies in key positions (specifically vacancies in positions supporting the CFO, performance management unit and compliance officer)  
A root cause at 1 auditee

Note: The Free State Fleet Management Trading Entity did not have significant root causes as a clean audit outcome was sustained.

### Status of key commitments by MEC

- Measures will be taken to address the material adjustments that were made to the financial statements to improve the system of internal control. (Not implemented)
- Address the current problem with the completeness of receivables for section 56 fines. (Implemented)
- Compile an effective action plan to address the non-compliance issues. (In progress)
- Appoint staff in key vacant positions and ensure that staff are sufficiently skilled in the finance, HR and performance information sections. (New)

# Free State legislature



1  
To maintain the **audit outcomes** ...  
... the **risk areas** and ...

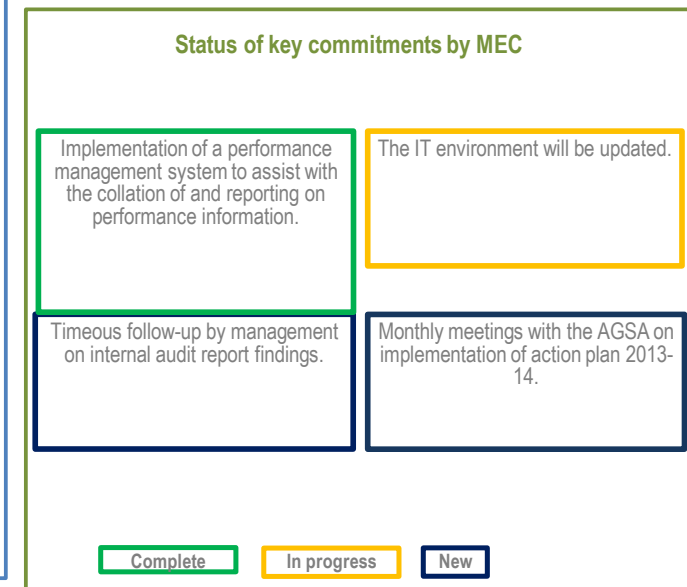
2  
... the key role players need to **assure** that ...  
... the **root causes** are addressed ...

3  
... attention is given to the **key controls** and ...  
... and the **commitments** are honoured.



### Most common root causes

There are no significant root causes as the department obtained a clean audit opinion



# Provincial treasury

**Sustained a clean audit outcome**

Audit area	Audit outcome
Financial statements (F)	Unqualified
Performance reports (P)	No material findings
Compliance with legislation (C)	No material findings

**Assurance levels**

First level	Senior management	Provides assurance
	Accounting officer	Provides assurance
	Executive authority	Provides assurance
Second level	Internal audit unit	Provides assurance
	Audit committee	Provides assurance
Third level	Portfolio committee	Provides limited or no assurance

**Key controls**

Key controls	Audit area		
	F	P	C
Effective leadership	Good	Good	Good
Human resource controls	Good	Good	Good
ICT governance and controls	Concerning	Good	Good
Audit action plans	Good	Good	Good
Proper record keeping	Good	Good	Good
Daily and monthly controls	Good	Good	Good
Review and monitor compliance	Good	Good	Good

F = Financial    P = Performance    C = Compliance

Good    Concerning

1  
To maintain the **audit outcomes** ...  
... the **risk areas** and ...

2  
... the key role players need to **assure** that ...  
... the **root causes** are addressed ...

3  
... attention is given to the **key controls** and ...  
... and the **commitments** are honoured.

**Risk areas**

Quality of submitted financial statements	Quality of submitted performance reports	Supply chain management
Good	Concerning	Concerning
Financial health	Human resource management	Information technology
Good	Concerning	Concerning

Good    Concerning    Intervention required

**Most common root causes**

There are no significant root causes as the department sustained a clean audit status

**Status of key commitments by MEC**

Financial asset checks for new appointees will be performed by 31 October 2014.	Adequate implementation of the information security policy.
A new supplier database system will be produced by 31 December 2014.	The department, with the assistance of Public Works and SITA, will obtain off-site premises to be used for disaster recovery purposes by 31 December 2014.
Senior managers and programme managers are required to certify that AoPO has been checked and verified for correctness to ensure that performance information reported is reliable..	

Implemented    New

# Public works

**Overall improvement in audit outcomes**

Audit area	Audit outcome	
Financial statements (F)	Unqualified	⬆️
Performance reports (P)	Material findings	➡️
Compliance with legislation (C)	Material findings	➡️

**Assurance levels**

Level	Role	Assurance	
First level	Senior management	Provides some assurance	➡️➡️
	Accounting officer	Provides some assurance	➡️➡️
	Executive authority	Provides some assurance	➡️➡️
Second level	Internal audit unit	Provides some assurance	➡️➡️
	Audit committee	Provides some assurance	⬇️
Third level	Portfolio committee	Provides no or limited assurance	➡️➡️

**Key controls**

Audit area	Audit area		
	F	P	C
Effective leadership	Good	Concerning	Intervention required
Human resource controls	Good	Concerning	Intervention required
ICT governance and controls	Concerning	Concerning	Intervention required
Audit action plans	Concerning	Concerning	Intervention required
Proper record keeping	Intervention required	Concerning	Intervention required
Daily and monthly controls	Concerning	Concerning	Good
Review and monitor compliance	Intervention required	Intervention required	Intervention required

F = Financial P = Performance C = Compliance

Good Concerning Intervention required

1  
To improve the **audit outcomes** ...  
... the **risk areas** and ...  
4

2  
... the key role players need to **assure** that ...  
... the **root causes** are addressed ...  
5

3  
... attention is given to the **key controls** and ...  
... and the **commitments** are honoured.  
6

**Risk areas**

Quality of submitted financial statements ➡️	Quality of submitted performance reports ➡️	Supply chain management ➡️
Financial health ⬇️	Human resource management ➡️	Information technology ➡️

Good Concerning Intervention required

**Most common root causes**

- Slow response by management (accounting officer and senior management)
- Key officials lack appropriate competencies
- Instability and vacancies in key positions (specifically instability in the CFO position as well as vacant position of the chief director responsible for properties).

**Status of key commitments by MEC**

Physical verification of all immovable assets. Implemented	Physical verification of movable assets. Implemented
Entering into new lease agreements for tenants occupying government property. Not implemented	Addressing all prior year audit findings included in the action plan and implementing controls to prevent them from recurring in future years. In progress

Not implemented In progress Implemented

# Social development

**Overall stagnation in audit outcomes**

Audit area	Audit outcome
Financial statements (F)	Unqualified
Performance reports (P)	Material findings
Compliance with legislation (C)	Material findings

**Assurance levels**

Level	Role	Assurance level
First level	Senior management	Provides assurance
	Accounting officer/authority	Provides some assurance
	Executive authority	Provides some assurance
Second level	Internal audit unit	Provides some assurance
	Audit committee	Provides some assurance
Third level	Portfolio committee	Provides limited or no assurance

**Key controls**

Key controls	Audit area		
	F	P	C
Effective leadership	Good	Concerning	Good
Human resource controls	Concerning	Good	Good
ICT governance and controls	Concerning	Concerning	Concerning
Audit action plans	Good	Concerning	Good
Proper record keeping	Good	Concerning	Good
Daily and monthly controls	Good	Good	Good
Review and monitor compliance	Concerning	Concerning	Concerning

F = Financial P = Performance C = Compliance

Good Concerning

1  
To improve the **audit outcomes** ...  
... the **risk areas** and ...  
4

2  
... the key role players need to **assure** that ...  
... the **root causes** are addressed ...  
5

3  
... attention is given to the **key controls** and ...  
... and the **commitments** are honoured.  
6

**Risk areas**

Quality of submitted financial statements (Good)	Quality of submitted performance reports (Concerning)	Supply chain management (Concerning)
Financial health (Intervention required)	Human resource management (Good)	Information technology (Concerning)

Good Concerning Intervention required

**Most common root causes**

- Slow response by management (accounting officer and senior management)
- Key officials lack appropriate competencies
- Vacancies in key positions (specifically vacancies in positions of CFO, head of SCM, head of monitoring and performance evaluation, as well as vacancies at district level)

**Status of key commitments by MEC** I1

A commitment was made to resolve the challenges regarding transfer payments.	Achieve clean audit outcome.
Internal audit should have a more robust approach to auditing, including predetermined objectives in the internal audit plan.	Engage with management regularly on progress made in resolving audit findings.

In progress Implemented

# Sport, arts, culture and recreation

**Sustained a clean audit outcome**

Audit area	Audit outcome
Financial statements (F)	Unqualified
Performance reports (P)	No material findings
Compliance with legislation (C)	No material findings

**Assurance levels**

First level	Senior management	Provides assurance
	Accounting officer/authority	Provides assurance
	Executive authority	Provides assurance
Second level	Internal audit unit	Provides some assurance
	Audit committee	Provides assurance
Third level	Portfolio committee	Provides no or limited assurance

**Key controls**

Audit area	Audit area		
	F	P	C
Effective leadership	Good	Good	Good
Human resource controls	Good	Good	Good
ICT governance and controls	Concerning	Concerning	Concerning
Audit action plans	Good	Good	Good
Proper record keeping	Concerning	Concerning	Good
Daily and monthly controls	Good	Good	Good
Review and monitor compliance	Good	Good	Good

F = Financial    P = Performance    C = Compliance

Good    Concerning

1  
To maintain the **audit outcomes** ...  
... the **risk areas** and ...  
4

2  
... the key role players need to **assure** that ...  
... the **root causes** are addressed ...  
5

3  
... attention is given to the **key controls** and ...  
... and the **commitments** are honoured.  
6

**Risk areas**

Quality of submitted financial statements	Quality of submitted performance reports	Supply chain management
Financial health	Human resource management	Information technology

Good    Concerning    Intervention required

**Most common root causes**

There are no significant root causes as the department obtained a clean audit opinion.

**Status of key commitments by MEC**

Executive and management overview of internal controls.	Implemented
Safeguarding of information and the controls over assets.	Implemented
Increase the capacity and skills of the internal audit unit and address vacancies.	New





# ANNEXURES



## Annexure 2: Auditees' five-year audit opinions

Auditee		Audit opinions				
		2013-14	2012-13	2011-12	2010-11	2009-10
<b>Departments</b>						
1	Agriculture and Rural Development					
2	Cooperative Governance and Traditional Affairs					
3	Economic Development, Tourism and Environmental Affairs					
4	Education					
5	Health					
6	Human Settlements					
7	Premier					
8	Police, Roads and Transport					
9	Free State Provincial Legislature					
10	Free State Provincial Treasury					
11	Public Works					
12	Social Development					
13	Sport, Arts, Culture and Recreation					
<b>Public entities</b>						
14	Central Medical Trading Account					
15	Free State Development Corporation					
16	Free State Fleet Management Trading Entity					
17	Free State Political Party Fund					
18	Free State Gambling and Liquor Authority					
19	Free State Tourism Authority					

Legend (audit opinions)	Unqualified with no findings	Unqualified with findings	Qualified with findings	Adverse with findings	Disclaimer with findings	Audit not finalised at legislated date
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# GLOSSARY OF TERMS, ACRONYMS AND ABBREVIATIONS

## Glossary of key terminology used in this report

*Adverse audit opinion (on financial statements)*

The financial statements contain material misstatements (see ‘misstatement’) that are not confined to specific amounts, or the misstatements represent a substantial portion of the financial statements.

*Asset (in financial statements)*

Any item belonging to the auditee, including property, infrastructure, equipment, cash, and debt due to the auditee.

*Assurance & assurance provider*

As used in this report, assurance is a positive declaration that is intended to give confidence in the credibility of financial and performance reports tabled by auditees and in the extent to which auditees have adhered to legislation to which they are subject.

Through the audit report issued to auditees, we provide assurance on the credibility of auditees’ financial and performance information as well as auditees’ compliance with key legislation.

There are role players (‘assurance providers’) in national and provincial government, other than external auditors, that are also required to contribute to assurance and confidence by ensuring that adequate internal controls are implemented to achieve auditees’ financial, service delivery and compliance objectives. Such assurance providers include senior auditee officials (heads of departments, accounting officers, and chief executive officers), various committees (risk management and audit committees), and internal audit units.

Other role players further include national and provincial oversight structures and coordinating or monitoring departments, as discussed in this report.

*Capital budget*

The estimated amount planned to be spent by auditees on capital items in a particular financial period; for example, fixed assets such as property, infrastructure and equipment with long-expected lives and that are required to provide services, produce income or support operations.

*Cash flow (in financial statements)*

The flow of money from operations: incoming funds are revenue (cash inflow) and outgoing funds are expenses (cash outflow).

*Clean audit*

The financial statements receive a financially unqualified audit opinion and there are no material findings on the quality of the annual performance report or non-compliance with key legislation.

*Commitments from role players*

Initiatives and courses of action communicated to us by role players in national and provincial government aimed at improving the audit outcomes.

*Conditional grants*

Money transferred from national government to auditees, subject to certain services being delivered or on compliance with specified requirements.

*Contingent liability*

A potential liability, the amount of which will depend on the outcome of a future event.

## *Creditors*

Persons, companies or organisations that auditees owe money to for goods and services procured from them.

## *Current assets (in financial statements)*

These assets are made up of cash and other assets, such as inventory or debt for credit extended, which will be traded, used or converted into cash in less than 12 months. All other assets are classified as non-current, and typically include property, plant and equipment as well as long-term investments.

## *Disclaimed audit opinion (on financial statements)*

The auditee provided insufficient evidence in the form of documentation on which we could base an audit opinion. The lack of sufficient evidence is not confined to specific amounts, or represents a substantial portion of the information contained in the financial statements.

## **Financial and performance management**

*(as one of the drivers of internal control)*

The performance of tasks relating to internal control and monitoring by management and other employees to achieve the financial management, reporting and service delivery objectives of the auditee.

These controls include the basic daily and monthly controls for the processing and reconciliation of transactions, the preparation of regular and credible financial and performance reports, and the review and monitoring of compliance with legislation.

## **Financially unqualified audit opinion**

*(on financial statements)*

The financial statements contain no material misstatements (see 'material misstatement'). Unless we express a clean audit opinion, findings have been raised on either the annual performance report or non-compliance with legislation, or both these aspects.

## *Fruitless and wasteful expenditure*

Expenditure that was made in vain and could have been avoided had reasonable care been taken. This includes penalties and interest on late payments to creditors or statutory obligations as well as payments made for services not utilised or goods not received.

## *Going concern*

The presumption that an auditee will continue to operate in the foreseeable future, and will not go out of business and liquidate its assets. For the going concern presumption to be reasonable, the auditee must have the capacity and prospect to raise enough financial resources to stay operational.

## *Governance (as one of the drivers of internal control)*

The governance structures (audit committees) and processes (internal audit and risk management) of an auditee.

## *Human resource management*

The management of an auditee's employees, or human resources, which involves adequate and sufficiently skilled people as well as the adequate management of the performance of staff and their productivity.

## *Information technology (IT)*

The computer systems used for capturing and reporting financial and non-financial transactions.

### *IT controls*

Computer-related controls ensure the confidentiality, integrity and availability of state information, enable service delivery and promote national security.

### *IT governance*

The leadership, organisational structures and processes which ensure that the auditee's IT resources will sustain its strategies and objectives.

### *IT security management*

The controls preventing unauthorised access to auditee networks, operating systems and application systems that generate financial information.

### *IT service continuity*

The processes managing the availability of hardware, system software, application software and data to enable auditees to recover or re-establish information system services in the event of a disaster.

### *IT user access management*

The procedures through which auditees ensure that only valid, authorised users are allowed segregated access to initiate and approve transactions on the information systems.

### *Internal control / key controls*

The process designed and implemented by those charged with governance, management and other personnel to provide reasonable assurance about the achievement of the auditee's objectives with regard to the reliability of financial reporting, the effectiveness and efficiency of operations, and compliance with key legislation.

It consists of all the policies and procedures implemented by auditee management to assist in achieving the orderly and efficient conduct of business, including adhering to policies, safeguarding assets, preventing and detecting fraud and error, ensuring the accuracy and completeness of accounting records, and timeously preparing reliable financial and service delivery information.

### *Irregular expenditure*

Expenditure incurred without complying with applicable legislation.

### *Key drivers of internal control*

The three components of internal control that should be addressed to improve audit outcomes, namely leadership, financial and performance management, and governance. (These three components are also defined individually in this glossary.)

### *Leadership* (as one of the drivers of internal control)

The administrative leaders of an auditee, such as heads of departments, chief executive officers and senior management.

It can also refer to the political leadership or the leadership in the province, such as the premier.

### *Liability*

Short-term and long-term debt owed by the auditee.

### *Material finding* (from the audit)

An audit finding on the quality of the annual performance report or non-compliance with legislation that is significant enough in terms of its amount, its nature, or both its amount and its nature, to be reported in the audit report.



## Material misstatement

*(in the financial statements or annual performance report)*

An error or omission that is significant enough to influence the opinions or decisions of users of the reported information. Materiality is considered in terms of either its rand value or the nature and cause of the misstatement, or both these aspects.

## Misstatement

*(in the financial statements or annual performance report)*

Incorrect or omitted information in the financial statements or annual performance report.

## Net deficit *(incurred by auditee)*

The amount by which an auditee's spending exceeds its income during a period or financial year.

## Operational budget / operating budget

A short-term budget, usually prepared annually, based on estimates of income and expenses associated with the auditee's operations, such as service delivery costs, administration and salaries.

## Oversight structures & coordinating and monitoring departments

National and provincial role players (1) that are directly involved with the management of the auditee (management/leadership assurance) – in other words, the first line of defence; (2) that perform an oversight or governance function, either as an internal governance function or an external monitoring function (internal independent assurance and oversight); and (3) that give an objective assessment of the auditee's reporting (external independent assurance and oversight).

## Property, infrastructure and equipment

*(in financial statements)*

Assets that physically exist and are expected to be used for more than one year, including land, buildings, leasehold improvements, equipment, furniture, fixtures and vehicles.

## Qualified audit opinion *(on financial statements)*

The financial statements contain material misstatements in specific amounts, or there is insufficient evidence for us to conclude that specific amounts included in the financial statements are not materially misstated.

## Receivables / debtors *(in financial statements)*

Money owed to the auditee by companies, organisations or persons who have procured goods or services from the auditee.

## Reconciliation *(of accounting records)*

The process of matching one set of data to another; for example, the bank statement to the cheque register, or the accounts payable journal to the general ledger.

## Root causes *(of audit outcomes being poor or not improving)*

The underlying causes or drivers of audit findings; in other words, why the problem occurred. Addressing the root cause helps ensure that the actions address the real issue, thus preventing or reducing the incidents of recurrence, rather than simply providing a one-time or short-term solution.

## Supply chain management

Procuring goods and services through a tender or quotation process and monitoring the quality and timeliness of the goods and services provided.

## Acronyms and abbreviations

AGSA	<i>Auditor-General of South Africa</i>
BAS	<i>Basic Accounting System</i>
bn (after an amount)	<i>R'-billion (rand)</i>
CEO	<i>chief executive officer</i>
CFO	<i>chief financial officer</i>
CIO	<i>chief information officer</i>
CoGTA	<i>Department of Cooperative Governance and Traditional Affairs</i>
DPISA	<i>Department of Public Service and Administration</i>
GRAP	<i>Generally Recognised Accounting Practice</i>
HoD	<i>head of department</i>
HR	<i>human resources</i>
ICT	<i>information and communication technology</i>
IFMS	<i>Integrated Financial Management System</i>
IT	<i>information technology</i>
K (after an amount)	<i>R'thousand (rand)</i>
LOGIS	<i>Logistical Information System</i>
m (after an amount)	<i>R'million (rand)</i>
MEC	<i>member of the executive council of a province</i>
PERSAL	<i>Personnel and Salary System</i>
PFMA	<i>Public Finance Management Act, 1999 (Act No. 1 of 1999)</i>
PPAC	<i>provincial public accounts committee</i>
SAP	<i>Systems, Applications and Products System</i>
SCM	<i>supply chain management</i>
SCOPA	<i>standing committee on public accounts</i>





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